Financials: Banks

	Decrease in RWA as % of Total RWA	Increase in CET-1 (in bp)
Large PVBs		
HDFCB	1.6%	29.1
ICICIBC	1.4%	23.3
Axis	1.2%	17.5
Kotak	1.2%	26.0
IIB	3.2%	49.9
Mid/Small PVBs		
FB#*	1.9%	26.9
IDFCB**	1.8%	24.7
RBL	3.0%	41.9
AU SFB	1.2%	19.8
Equitas SFB	1.0%	17.6
Bandhan#	11.1%	171.8
PSBs		
SBI**	2.1%	24.1
BOB**	2.0%	27.8
PNB**	1.3%	13.4
CBK**	1.8%	22.2
UNBK**	1.4%	19.1
INBK**	1.3%	17.5

***NBFC (Non-HFC) book considered at 40% of the overall exposure, # indicates 80%, #* indicates 20%; **IIB, IDFC First, RBL, and Bandhan Bank** saw risk weights increase to 125% and, as a result, have been considered for a 25% reduction in RWA on MFI*

RBI reduces risk weight on MFI loans and loans to NBFCs

Supportive regulatory action continues; positive for both banks & NBFCs

The Reserve Bank of India (RBI) has announced a significant policy reversal, restoring the risk weights on exposures of SCBs to NBFCs, as well as Micro-Finance Institutions (MFI), to their original levels. This decision effectively reverses the 25% increase in risk weights on bank loans to NBFCs that RBI had implemented in Nov'23. Below are our views on the same:

Reduction in risk weights to support growth and improve CET-1 for banks

The earlier increase in risk weights on bank loans to NBFCs (in Nov'23) had led to a rise in RWA for banks, putting pressure on CET-1 ratios. This strained the capital adequacy, creating challenges for banks, particularly those with already thin capital buffers. The restoration of risk weights to pre-Nov'23 levels will help alleviate this pressure, especially as the profitability of many mid-sized banks is already under pressure due to asset quality concerns in unsecured segments. As a result, banks are expected to witness an improvement in their CET-1 ratios, as they will require less capital against these loans. Stronger capitalization will enhance banks' ability to absorb potential AQ shocks and support recovery in business growth.

Risk weights on MFI exposure restore to 100%/75% from 125%

The reversal in risk weights on MFI loans from 125% to 100%/75% will help reduce RWAs for banks, supporting capital adequacy levels. Universal banks like Bandhan, IIB, IDFCFB, RBK, and some SFBs with significant exposure to the microfinance sector will be the key beneficiaries. The improved capital position will enable some of these banks to operate with optimal leverage, thus supporting their RoE and alleviating the need to raise capital in the short term.

Regulatory intent more important than regulatory action

While the 25% reduction in risk weights, in isolation, may not be a significant incentive for banks to lend to NBFCs—since many are already grappling with elevated CD ratios, asset quality issues, and margin pressures—the intent behind this regulatory action and the timing of the reduction in risk-weight when the system is dealing with heightened asset quality issues, particularly in MFI, are crucial. This is because:

- It highlights the regulator's preference to support growth and sends a clear signal to lenders to avoid being overly cautious when lending to the NBFC and MFI segments.
- We note that over the past nine months, the MFI industry loan book has declined 11% YTD, while bank loans to NBFCs have seen a decline in growth to 6.6% YoY in Dec'25 vs 30% YoY growth in FY23 and 16% YoY growth in FY24. We, thus, expect a recovery in both these segments in the coming quarters.

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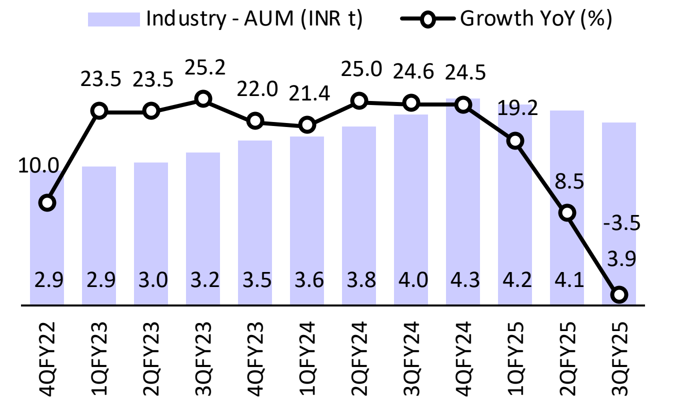
Supportive regulatory actions continue; positive for both banks & NBFCs

RBI has initiated several regulatory measures in recent months to support the sector and enhance the operating performance of lenders. This includes: i) a reduction in the repo rate, ii) undertaking of several liquidity-enhancing operations, iii) deferment of LCR, ECL, and project-financing regulations, and iv) the lifting of supervisory restrictions on KMB and many others.

- The current step to reduce the risk weight for lending to NBFCs and MFIs comes at a time when the system is still navigating asset quality stress, with MFI lenders, in particular, expected to face elevated provisions in the upcoming quarter.
- This highlights the regulator's intent to focus on growth and ensure credit availability to underserved sections of society, aligning with the government's goal of improving rural income and supporting overall consumption.
- The reduction in risk weights will lower capital consumption for banks, which are likely to pass on partial benefits to NBFCs in the form of lower lending rates, in addition to the transmission from the recent repo rate revision. This could potentially reduce borrowing costs for NBFCs and support margin and growth recovery. **Key beneficiaries:** Bandhan, IndusInd, and RBL Bank.

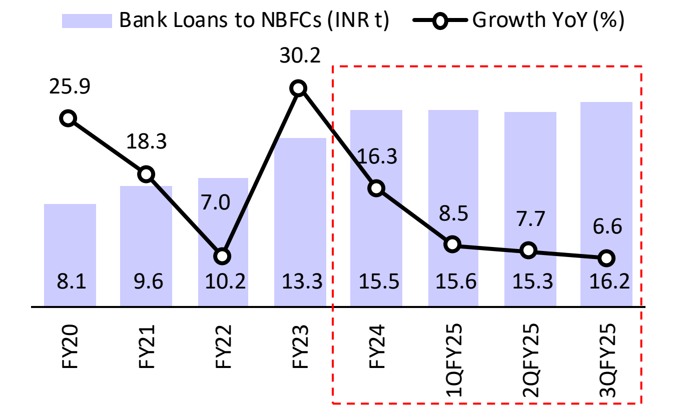
Charts

Exhibit 1: MFI industry growth turned negative to 3.5% YoY; During 9MFY25YTD, the segment reported 11% decline



Source: MOFSL, MFIN

Exhibit 2: Growth in bank loans to NBFCs declining since the increase in risk weights in Nov'23



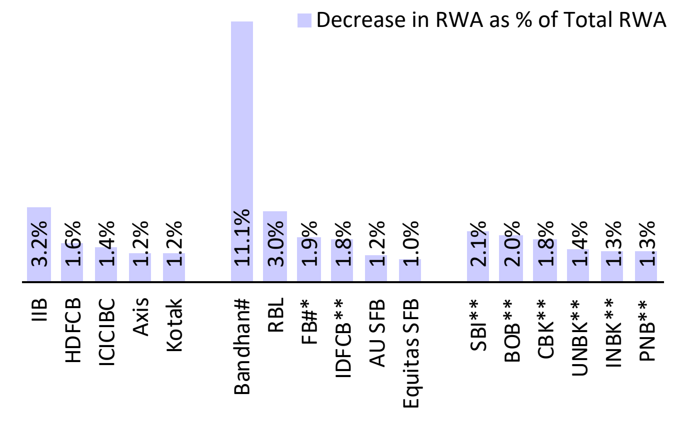
Source: MOFSL, RBI

Exhibit 3: Estimated CET-1 accretion for banks under our coverage (bp)

	% of Loans affected	Total Loans (INR m)	as a % of total assets	Decrease in RWA as % of Total RWA	RWA/Total Assets – Revised	CET-1 Ratio – Existing	Revised CET-1 Ratio	Increase in CET-1 (in bp)
Banks								
Large PVBs								
HDFCB	6.5%	2,51,82,482	67%	1.6%	65.9%	17.5%	17.8%	29.1
ICICIBC	6.8%	1,31,43,661	77%	1.4%	75.7%	15.9%	16.2%	23.3
Axis	5.3%	1,01,45,641	73%	1.2%	72.1%	14.6%	14.8%	17.5
Kotak	6.1%	41,38,390	84%	1.2%	82.9%	21.7%	22.0%	26.0
IIB	15.0%	36,68,890	78%	3.2%	75.6%	15.2%	15.7%	49.9
Mid/Small PVBs								
FB#*	6.7%	23,03,700	60%	1.9%	58.5%	13.8%	14.0%	26.9
IDFCB**	8.4%	22,31,039	79%	1.8%	77.6%	13.7%	13.9%	24.7
RBL	14.2%	9,04,120	77%	3.0%	74.5%	13.7%	14.1%	41.9
AU SFB	3.9%	9,95,590	59%	1.2%	57.9%	16.9%	17.1%	19.8
Equitas SFB	3.3%	3,53,860	58%	1.0%	57.4%	17.5%	17.7%	17.6
Bandhan#	54.1%	12,73,800	84%	11.1%	74.6%	13.7%	15.4%	171.8
PSBs								
SBI**	7.6%	4,00,45,669	54%	2.1%	52.7%	11.0%	11.2%	24.1
BOB**	5.8%	1,15,13,156	49%	2.0%	47.9%	13.8%	14.0%	27.8
PNB**	4.0%	1,06,99,568	47%	1.3%	46.6%	10.7%	10.8%	13.4
CBK**	5.2%	1,02,37,269	46%	1.8%	44.9%	12.0%	12.2%	22.2
UNBK**	4.1%	92,01,782	48%	1.4%	47.5%	13.6%	13.8%	19.1
INBK**	3.9%	54,21,170	49%	1.3%	48.2%	13.3%	13.4%	17.5

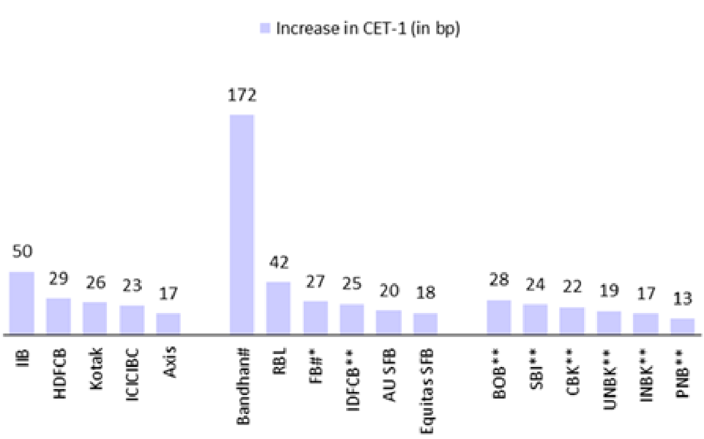
NBFC (Non-HFC) book considered at 40% of the overall exposure, # indicates 80%, #* 20%; **IIB, IDFC First, RBL, and Bandhan Bank saw risk weights increase to 125% and, as a result, have been considered for a 25% reduction in RWA on MFI; Source: MOFSL, Company

Exhibit 4: Most banks expected to see a decline of 1-3% in RWA barring Bandhan, which is expected to see a 11.1% decline



**NBFC (Non-HFC) book considered at 40% of the overall exposure, # indicates 80%, #* indicates 20%; Source: MOFSL, Company

Exhibit 5: Most banks will see a 13-50bp increase in the CET-1 ratio; Bandhan to see a CET-1 accretion of 172bp



**NBFC (Non-HFC) book considered at 40% of the overall exposure, # indicates 80%, #* indicates 20%; Source: MOFSL, Company

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BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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