Sector Update | 17 June 2025

Financials: Banks

FY26: A year of two halves

Earnings growth closer to an inflection point; NIMs to bottom out by 3QFY26E

- **Against the market expectations of a shallow rate cycle just two quarters ago, RBI has implemented a sharp 100bp repo rate cut since Feb'25 and reduced the CRR by 100bp in four tranches starting Sep'25.**
- **While the 100bp rate cut will exert pressure on margins in the near term, the benefits from the CRR cut and gradual deposit repricing will mark a likely turning point for earnings recovery from 2HFY26 onwards.**
- **We note that the banking sector's earnings growth has witnessed successive moderation—from 39.3% in FY23 to 12.8% in FY25. In FY26, we further estimate earnings growth to moderate to ~6.5%, with 1H being more muted.**
- **We, thus, estimate FY27 earnings growth to recover to ~16.1%. The normalization of credit costs in unsecured segments, continued improvement in the asset mix, and improved treasury performance will enable banks to maintain a healthy RoA trajectory despite macro and rate challenges.**
- **While the sector may undergo some near-term consolidation due to margin and growth concerns, the gradual recovery in margins and loan growth will enable improved sector performance over the medium term. We prefer banks with superior deposit franchises and prudent risk practices.**
- **Top ideas: ICICIBC, HDFCB, and SBIN. In mid-sized banks, we prefer FB and AUBANK.**

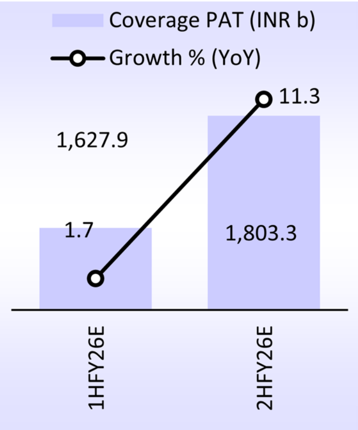
PAT Growth % (YoY)

	Private	PSU	Coverage
FY25	4.2	24.0	12.8
FY26E	9.7	3.0	6.5
1HFY26E	1.7	1.6	1.7
2HFY26E	17.9	4.3	11.3
FY27E	19.9	11.6	16.1

Repo rate: From a shallow cycle chatter to a front-ended 100bp rate cut

- Against the market expectations of a shallow rate cycle just two quarters ago, RBI has implemented a sharp 100bp repo rate cut since Feb'25 and reduced the CRR by 100bp in four tranches starting Sep'25. The sharp pace of rate cuts, supported by controlled inflation and stable trends in currency rates, will help support the consumption and investment cycle in the medium term.
- RBI has changed its policy stance from 'Accommodative' to 'Neutral', indicating that the scope for further rate cuts now largely depends on the inflation trajectory in FY26 and the broader economic performance. We believe the RBI has front-loaded the rate cuts, and with ongoing geopolitical uncertainty and crude price volatility, the likelihood of further rate cuts appears limited.
- Moreover, we continue to believe that banks will witness NIM contraction in 1HFY26, with recovery expected from 2HFY26, as deposit portfolios reprice and funding costs begin to moderate. Additionally, the benefit from CRR reduction will further boost systemic liquidity and support banking margins.

Earnings growth to bottom out in 1HFY26E; expect trend to improve from 2H



Earnings moderation to acceleration: Estimate gradual recovery from 2HFY26

- The banking sector's earnings growth has witnessed successive moderation—from 39.3% in FY23 to 12.8% in FY25. During FY26, we further estimate earnings growth to moderate to ~6.5%, with 1H being more muted at 1.7% earnings growth vs 11.3% growth in 2H earnings.
- While the 100bp rate cut may temporarily pressure NIMs, the benefits from the CRR cut and deposit repricing will mark a likely turning point for earnings recovery.
- We, thus, estimate the earnings growth trajectory to stabilize in 2H and gradually start accelerating thereafter. We project FY27 earnings growth to recover to ~16.1%.

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Margin bias negative: Will it be a soft landing vs hard landing ?

- The sharp 100bp reduction in repo rates will adversely impact lending yields for the banking sector, thereby impacting margins. Thus, we expect NIMs to contract over 1HFY26, with banks holding a higher share of EBLR-linked loans being more vulnerable.
- However, the steady improvement in systemic liquidity has enabled banks to reduce deposit rates. We note that several banks had earlier reduced SA rates as the rate cycle turned, and more recently, many have reduced bulk/term deposit rates as well. Moreover, the 100bp CRR reduction effective Sep'25 will further support banking system liquidity and boost margins.
- We, thus, believe that while near-term margins will remain under pressure—with 2Q being more vulnerable than 1Q as the full impact of the rate cut plays out—the gradual moderation in funding costs and the benefits from the CRR cut will begin to support the NIM trajectory from 2HFY26 onwards.
- Additionally, the improving asset mix—driven by a higher share of retail and granular high-yield assets—along with improved systemic liquidity from the CRR cut, which adds INR2.5t of durable liquidity, will help mitigate risks of margin contraction. This supports the case for a soft landing on margins by the end of FY26E.

Asset quality outlook stable; credit cost to stay under control

- FY25 began with notable concerns around asset quality, especially in unsecured retail and MFI segments, where several banks have witnessed higher delinquencies/credit costs.
- However, early-stage delinquencies have started to improve across most lenders, and we expect credit costs in unsecured retail and MFI segments to moderate from 2HFY26 onwards, especially for mid-sized and MFI-focused banks.
- On-ground feedback from lenders, along with RBI's acknowledgment of asset quality stabilization (post risk-weight normalization in personal loans), indicates easing stress in this segment.

MOFSL view: Continue to follow a stock-specific approach

- Systemic credit growth has decelerated to ~8.9% YoY, driven by slower momentum in retail and secured lending amid elevated CD ratio.
- Against the backdrop of a modest economic growth trajectory (RBI expects GDP to grow at 6.5% in FY26), banks with stronger liability franchises and diversified lending portfolios are better placed to sustain growth and withstand margin pressures.
- While the sector may undergo some near-term consolidation due to margin and growth concerns, the gradual recovery in margins and loan growth will enable improved sector performance over the medium term. We prefer banks with superior deposit franchises and prudent risk practices.
- The normalization of credit costs in unsecured segments, improvement in the asset mix, and improved treasury performance will enable banks to maintain a healthy RoA trajectory despite macro and rate challenges.
- **Top ideas: ICICIBC, HDFCB, and SBIN.** In mid-sized banks, **we prefer FB and AUBANK.**

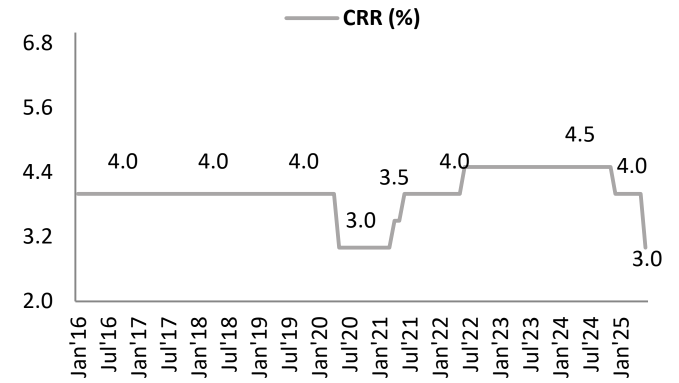
Story in charts

Exhibit 1: Measures taken by RBI under the new Governor

Date	Measures taken
11th Dec'24	# Mr. Sanjay Malhotra joins RBI as the governor, replacing Mr. Shaktikanta Das
8th Jan'25	# Lifting of restriction on Asirvad Microfinance (Manappuram) on loan sanctioning/disbursals
7th Feb'25	# Repo rate cut by 25bp to 6.25%
7th Feb'25	# Deferred implementation of LCR, Expected Credit Loss (ECL), and stricter project-finance provisioning
12th Feb'25	# Lifting of restrictions on Kotak Mahindra Bank (digital onboarding & fresh credit cards)
9th Apr'25	# Repo rate cut by 25bp to 6.0%
21st Apr'25	# Final LCR guidelines - Lower run-off factor for wholesale deposits of 40% (from 100%); New run-off factor for IMB-linked retail deposits at 2.5% vs 5% proposed earlier -> Systemic LCR improved by 6%
6th Jun'25	# Repo rate cut by 50bp to 5.50%
6th Jun'25	# CRR cut by 100bp to 3% in a phased manner (beginning Sep'25)
6th Jun'25	# Exemption from credit checks for gold loans up to INR2.5 lakh; LTV for such loans raised to 85%

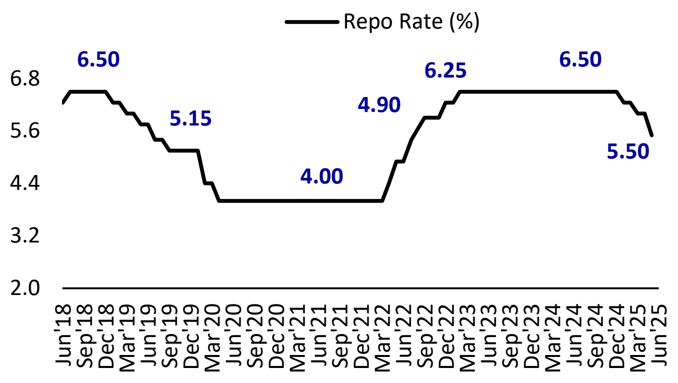
Source: Company, MOFSL

Exhibit 2: CRR (%) has seen a sharp cut to 3% and is now at the bottom range



Source: Company, MOFSL

Exhibit 3: Repo rate has been reduced to 5.5% in the Jun'25 policy



Source: Company, MOFSL

Exhibit 4: As of 4QFY25, PSBs had a sizeable mix of MCLR-linked loans (%)

Loans Mix (%) - 4QFY25	MCLR	EBLR		Repo Linked	Others (Fixed, base rate, foreign currency-floating)
AUBANK	30		7		63
AXSB	9	4		57	30
CBK	56	44			0
FB	9		51		40
HDFCB*	25			45	30
ICICIBC	15	1		53	31
INBK*	57		37		5
KMB**	13	60			27
PNB	31	15		44	11
RBL	9		46		45
SBIN	35		29		36
BOB	47			35	18
Equitas*			20		80

**As of 2QFY25, *As of 3QFY25; Source: MOFSL, Company

Exhibit 5: Banks have already seen a contraction in NIMs amid CoF repricing

NIM (%)	4Q23	1Q24	2Q24	3Q24	4Q24	1Q25	2Q25	3Q25	4Q25	YoY Change (bp)
AXSB	4.22	4.10	4.11	4.01	4.06	4.05	3.99	3.93	3.97	(9)
HDFCB	4.10	4.10	3.40	3.40	3.44	3.47	3.46	3.43	3.54	10
ICICIBC	4.90	4.78	4.53	4.43	4.40	4.36	4.27	4.25	4.41	1
IDFCFB	6.41	6.33	6.32	6.42	6.35	6.22	6.18	6.04	5.95	(40)
IIB	4.28	4.29	4.29	4.29	4.26	4.25	4.08	3.93	2.25	(79)
KMB	5.75	5.57	5.22	5.22	5.28	5.02	4.91	4.93	4.97	(31)
FB	3.36	3.20	3.22	3.19	3.21	3.16	3.12	3.11	3.12	(9)
BoB	3.53	3.27	3.07	3.10	3.27	3.18	3.10	2.94	2.86	(41)
CBK	3.07	3.05	3.00	3.03	3.07	2.90	2.86	2.71	2.73	(34)
PNB	3.24	3.08	3.11	3.15	3.10	3.07	2.92	2.93	2.81	(29)
SBIN	3.60	3.33	3.29	3.22	3.30	3.22	3.14	3.01	3.00	(30)
UNBK	2.98	3.13	3.18	3.08	3.09	3.05	2.90	2.91	2.87	(22)
INBK	3.59	3.61	3.52	3.49	3.52	3.53	3.49	3.57	3.48	(4)
AUBANK	6.10	5.72	5.50	5.50	5.10	6.00	6.05	5.90	5.80	70
RBK	5.62	5.53	5.54	5.52	5.45	5.67	5.04	4.90	4.89	(56)
BANDHAN	7.30	7.30	7.20	7.20	7.60	7.60	7.40	6.90	6.70	(90)
DCBB	4.18	3.83	3.69	3.48	3.62	3.39	3.27	3.30	3.29	(33)

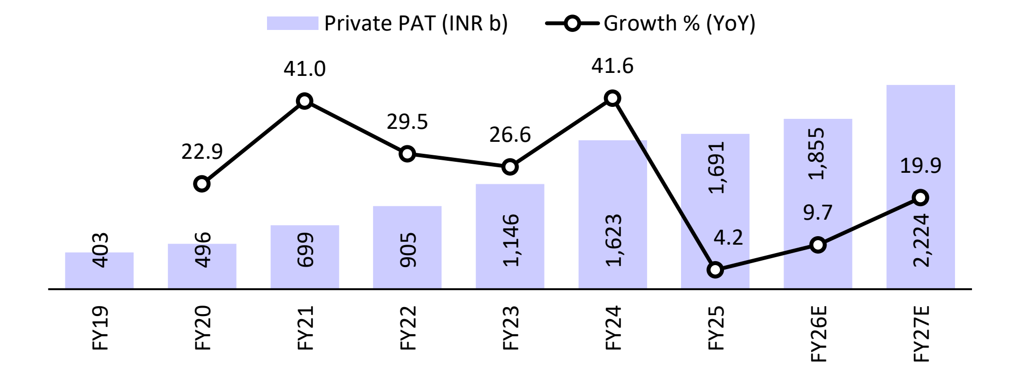
Source: Company, MOFSL

Exhibit 6: Earnings trajectory to stabilize over 2HFY26 and recover thereafter

INRb	Earnings							Growth YoY (%)						
	FY23	FY24	FY25E	FY26E	1HFY26E	2HFY26E	FY27E	FY23	FY24	FY25	FY26E	1HFY26E	2HFY26E	FY27E
Private Banks														
AXSB	92.2	248.6	263.7	275.6	127.8	147.8	327.8	-29	170	6	4	-1	10	19
BANDHAN	21.9	22.3	27.5	31.8	11.2	20.6	38.5	1645	2	23	16	-44	177	21
DCBB	4.7	5.4	6.2	7.5	3.6	3.9	9.7	62	15	15	22	26	18	29
HDFCB	441.1	608.1	673.5	726.4	352.8	373.5	850.5	19	38	11	8	7	9	17
ICICIBC	319.0	408.9	472.3	514.1	249.0	265.1	605.5	37	28	16	9	9	9	18
IDFCFB	24.4	29.6	15.2	27.0	8.1	18.8	49.2	1575	21	-48	77	-8	193	83
IIB	74.4	89.8	25.8	33.9	12.3	21.6	44.1	55	21	-71	32	-65	-333	30
KMB	109.4	137.8	137.2	150.9	72.0	78.9	176.6	28	26	0	10	5	15	17
FB	30.1	37.2	40.5	42.8	20.9	21.9	54.2	59	24	9	6	1	10	27
RBK	8.8	11.7	7.0	13.3	4.8	8.5	21.3	-1281	32	-40	91	-20	739	60
AUBANK	14.3	15.3	21.1	27.1	11.2	16.0	36.9	26	7	37	29	4	55	36
EQUITASB	5.7	8.0	1.5	4.5	1.6	2.9	10.0	104	39	-82	203	312	164	125
Total Pvt	**1,146.0**	**1,622.6**	**1,691.3**	**1,854.7**	**875.3**	**979.4**	**2,224.3**	27	42	4	10	2	18	20
YoY growth (%)	**26.6**	**41.6**	**4.2**	**9.7**	**1.7**	**17.9**	**19.9**							
PSU Banks														
BOB	141.1	177.9	195.8	201.3	88.8	112.5	224.2	94	26	10	3	-8	14	11
CBK	106.0	145.5	170.3	176.2	82.5	93.7	195.8	87	37	17	3	4	3	11
INBK	52.8	80.6	109.2	112.3	56.9	55.4	126.2	34	53	35	3	11	-5	12
PNB	25.1	82.4	166.3	192.1	86.8	105.3	221.4	-27	229	102	16	15	16	15
SBIN	502.3	610.8	709.0	711.2	349.0	362.2	796.1	59	22	16	0	-1	2	12
UNBK	84.3	136.5	179.9	183.4	88.7	94.8	196.2	61	62	32	2	6	-1	7
Total PSU	**911.7**	**1,233.8**	**1,530.4**	**1,576.5**	**752.6**	**823.8**	**1,759.8**	59	35	24	3	2	4	12
YoY growth (%)	**59.2**	**35.3**	**24.0**	**3.0**	**1.6**	**4.3**	**11.6**							
Total Banks	**2,057.7**	**2,856.4**	**3,221.7**	**3,431.2**	**1,627.9**	**1,803.3**	**3,984.1**	39	39	13	7			16
YoY growth (%)	**39.3**	**38.8**	**12.8**	**6.5**	**1.7**	**11.3**	**16.1**							

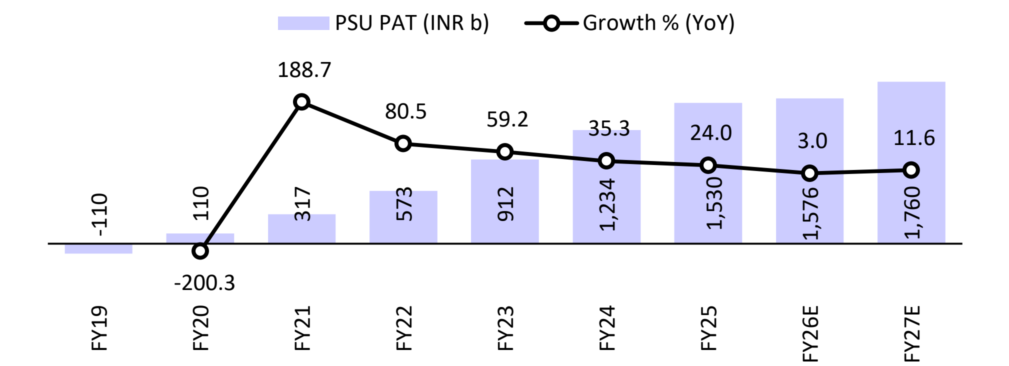
Source: Company, MOFSL

Exhibit 7: Estimate Private Banks earnings to recover to 19.9% in FY27 from 9.7% in FY26



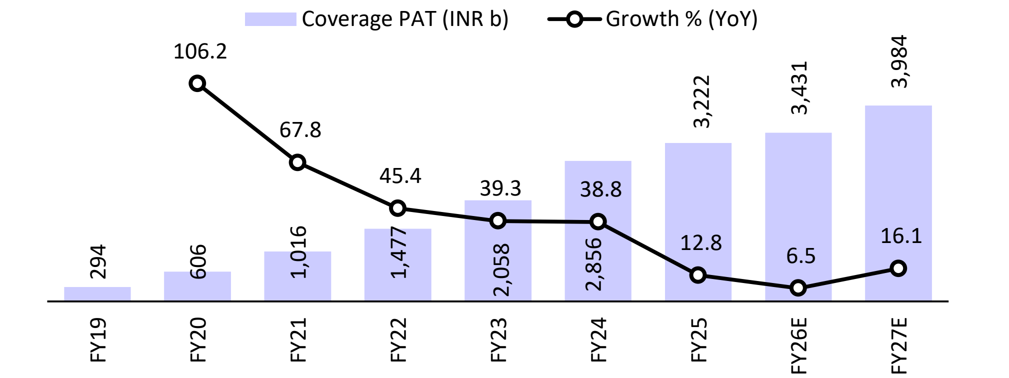
Source: Company, MOFSL

Exhibit 8: Estimate PSU bank earnings to recover to 11.6% in FY27 vs 3% in FY26



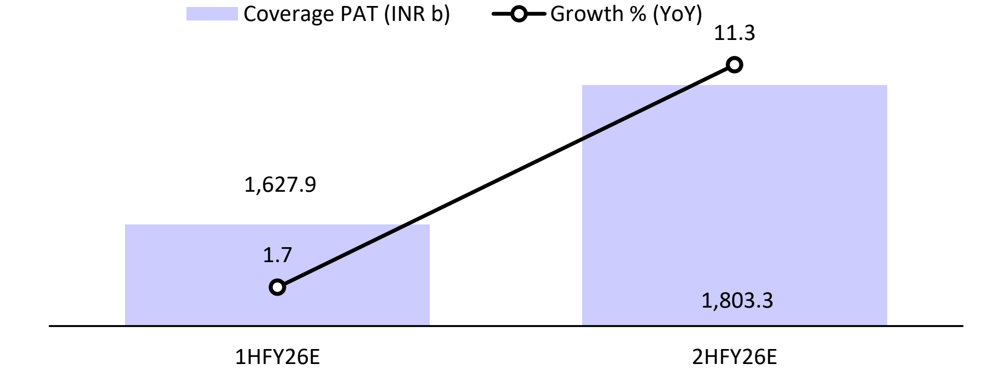
Source: Company, MOFSL

Exhibit 9: We estimate our banking universe earnings growth to bottom out at 6.5% in FY26, followed by a recovery from FY27



Source: Company, MOFSL

Exhibit 10: Earnings growth to bottom out in 1HFY26E; expect trend to improve from 2H



Source: Company, MOFSL

Exhibit 11: Banking valuation matrix

Val summary	Rating	CMP (INR)	Mkt. Cap (INRb)	Mcap (USDb)	EPS (INR) FY26E	EPS (INR) FY27E	RoA (%) FY26E	RoA (%) FY27E	RoE (%) FY26E	RoE (%) FY27E	P/E (x) FY26E	P/E (x) FY27E	P/BV (x) FY26E	P/BV (x) FY27E
Private Banks														
ICICIBC*	Buy	1,423	10,063	116.9	72.9	85.5	2.3	2.3	17.1	17.5	15.9	13.5	3.2	2.7
HDFCB*	Buy	1,930	14,853	172.5	96.7	112.6	1.8	1.9	14.0	14.6	16.8	14.4	2.7	2.4
AXSB*	Neutral	1,217	3,756	43.6	90.9	107.1	1.6	1.7	14.6	15.0	12.0	10.2	1.8	1.6
BANDHAN	Neutral	175	286	3.3	19.8	23.9	1.6	1.7	12.7	14.3	8.8	7.3	1.1	1.0
KMB*	Buy	2,137	4,227	49.1	76.6	89.7	2.1	2.1	12.6	13.3	17.8	15.2	3.4	3.0
IIB	Neutral	809	646	7.5	44.2	57.0	0.6	0.7	5.2	6.4	18.3	14.2	0.9	0.9
FB	Buy	205	507	5.9	18.0	22.5	1.2	1.3	12.5	14.0	11.4	9.1	1.4	1.2
DCBB	Buy	142	46	0.5	24.2	31.0	0.9	1.0	13.3	15.1	5.9	4.6	0.7	0.6
IDFCFB	Neutral	70	518	6.0	3.5	5.8	0.7	1.1	6.5	10.0	20.1	12.1	1.3	1.2
EQUITASB	Buy	67	79	0.9	4.0	8.9	0.8	1.5	7.4	15.2	16.7	7.5	1.2	1.1
AUBANK	Buy	773	579	6.7	36.9	49.7	1.6	1.7	15.2	17.7	20.9	15.6	3.0	2.5
RBK	Buy	219	136	1.6	22.6	35.6	0.9	1.2	8.6	12.8	9.7	6.2	0.8	0.8
PSU Banks														
SBIN*	Buy	792	7,190	83.5	79.7	89.2	1.0	1.0	16.1	15.9	6.8	6.1	1.5	1.3
PNB	Buy	106	1,242	14.4	16.9	19.4	1.0	1.0	15.3	15.5	6.3	5.4	0.9	0.8
BOB	Neutral	238	1,248	14.5	39.4	43.6	1.1	1.1	15.1	15.4	6.0	5.5	0.9	0.8
CBK	Buy	109	1,049	12.2	19.7	21.8	1.0	1.0	18.3	18.0	5.5	5.0	0.9	0.8
UNBK	Buy	145	1,148	13.3	24.2	25.9	1.2	1.1	16.2	15.2	6.0	5.6	0.9	0.8
INBK	Buy	634	842	9.8	84.4	94.3	1.2	1.3	17.0	16.9	7.5	6.7	1.2	1.0
Payments & Fintech														
SBI Cards	Neutral	991	958	11	33	45	4.4	5.0	20.6	23.0	30.1	22.0	5.7	4.6
					EPS (INR)		**RoA (%)**		**RoE (%)**		**P/E (x)**		**P/BV (x)**	
One 97 Comm.	Neutral	865	561	7	3	16	0.9	4.4	1.5	7.9	294.7	55.0	4.3	4.3

*Adjusted for subsidiaries

Explanation of Investment Rating	
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BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
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