

Banks

India

Sector View: **Attractive** NIFTY-50: **22,904**

April 06, 2025

Connecting the dots of provisional business updates

We reiterate that the explanatory power of provisional business updates (a set of closely tracked disclosures) is mixed. On one hand, the relationship between NII growth and business growth has weakened after the introduction of EBLR and a higher share of retail loans. On the other hand, the disclosure on collection efficiency does provide some early indication about slippage trends. Hence, we look at these disclosures selectively when drawing an inference on the profitability performance of individual banks.

Looking through the relationship of NII and business performance

We note that investors have placed a fair amount of importance on the provisional numbers that get released at the beginning of the quarter. We understand that investors tend to evaluate the relationship between business (loans and deposits) and NII growth. We have highlighted that the relationship is not a strong one, except where assets and liabilities have a higher share of fixed-rate loans and comparable maturity. We see that the relationship between loan growth and NII is stronger for small finance banks, while it is less significant for large private and PSU banks.

NII and NIM have many variables driving them; provisional numbers are not sufficient

We reiterate that NII growth is a function of many variables: (1) loan growth and loan mix; (2) deposits, deposit mix (CASA and term or retail and wholesale) and borrowing growth; (3) mobilization of funds into loans and investments, which accrue different yields; (4) loan yields; (5) cost of deposits and borrowings; (6) regulatory actions such as changes to repo rate, CRR, SLR, etc.; (7) company-specific actions such as capital issuance; and (8) accounting impact such as write-offs, interest on income tax refund and interest reversals/interest accrued on non-performing loans. The overemphasis on deposits and loans ignores other variables driving NII growth and likely NIM for that quarter. Further, the salience of any variable could vary over time. For example, loan growth might explain NII growth very well in some periods, while in other periods it might be the cost of deposits driving NII growth. Hence, it is useful to look at these data releases from a signaling perspective without drawing specific inferences.

On the other hand, we observe the collection efficiency disclosures do offer some early indication about potential slippages (and, hence, credit cost) in the subsequent quarters. However, even this metric is mostly not comparable across lenders because of the inconsistency in the definition applied by them.

EBLR linkage and higher share of retail loans have made NII more volatile

In recent years, NII growth has become much more volatile than earlier (see exhibits). The share of EBLR-linked retail loans, changes to policy rates and the maturity profile of liabilities are likely to play a bigger role in determining NII growth. Note that the RBI's data releases do carry a lot of information on the business performance for the sector, and, hence, these provisional business updates merely help to adjust the final forecasts for individual banks.

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M B Mahesh, CFA
mb.mahesh@kotak.com
+91-22-4336-0886

Nischint Chawathe
nischint.chawathe@kotak.com
+91-22-4336-0887

Ashlesh Sonje, CFA
ashlesh.sonje@kotak.com
+91-22-4336-0889

Abhijeet Sakhare
abhijeet.sakhare@kotak.com
+91-22-4336-1240

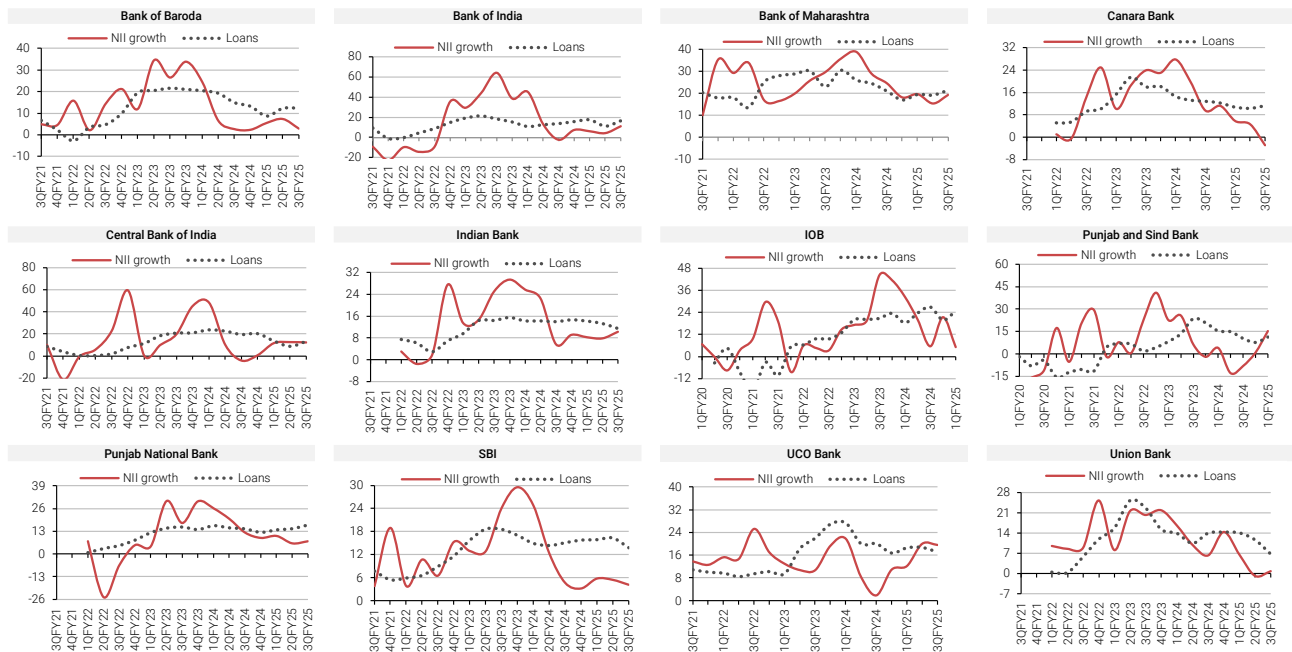
Varun Palacharla
varun.palacharla@kotak.com
+91-22-4336-0888

Nikhil Suresh
nikhil.suresh@kotak.com

jimit.harde-kotak.com

NII growth has been far more volatile in public banks

Exhibit 1: NII growth and loan growth for PSU banks, March fiscal year-ends, 3QFY21-3QFY25 (%)

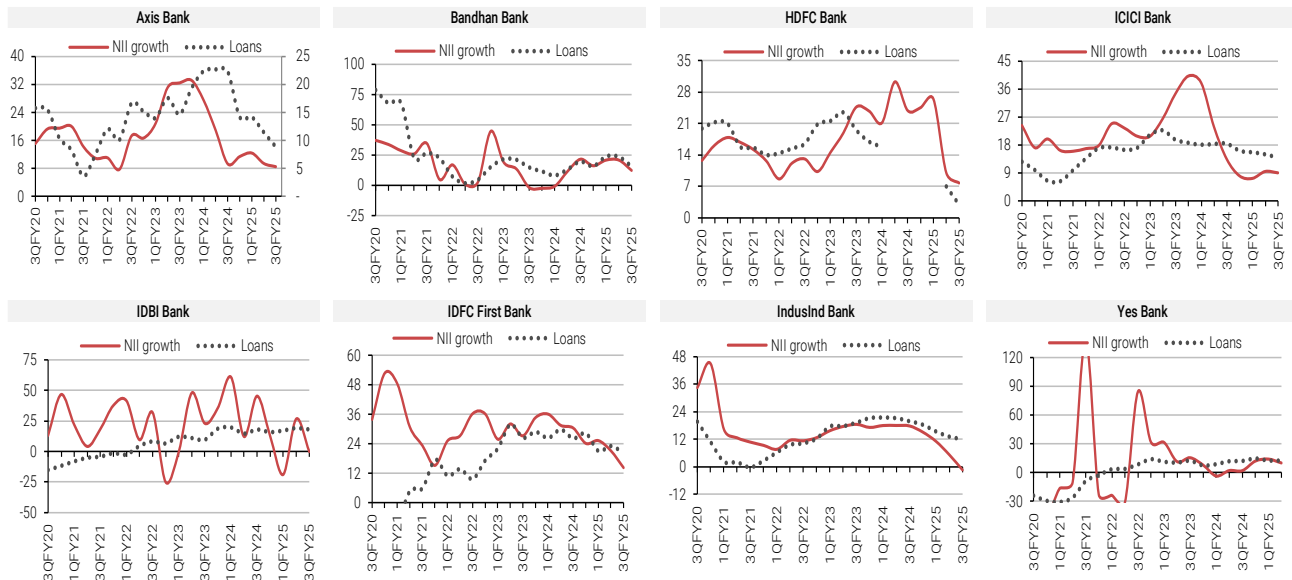


Notes: (a) We have removed the period for select public banks as there was consolidation of public and private banks to provide a better perspective

Source: Company, Kotak Institutional Equities

Private banks such as Axis Bank and ICICI Bank have shown higher volatility of NII growth post the introduction of EBLR

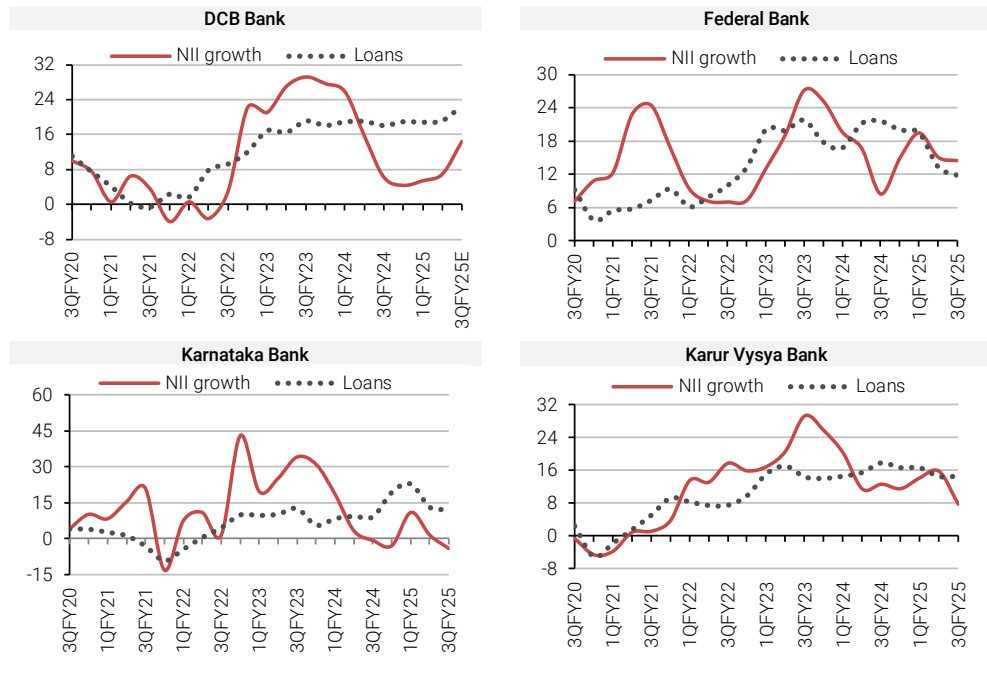
Exhibit 2: NII growth and loan growth for private banks, March fiscal year-ends, 3QFY20-3QFY25 (%)



Source: Company, Kotak Institutional Equities

Similar weak correlation observed for regional banks as well

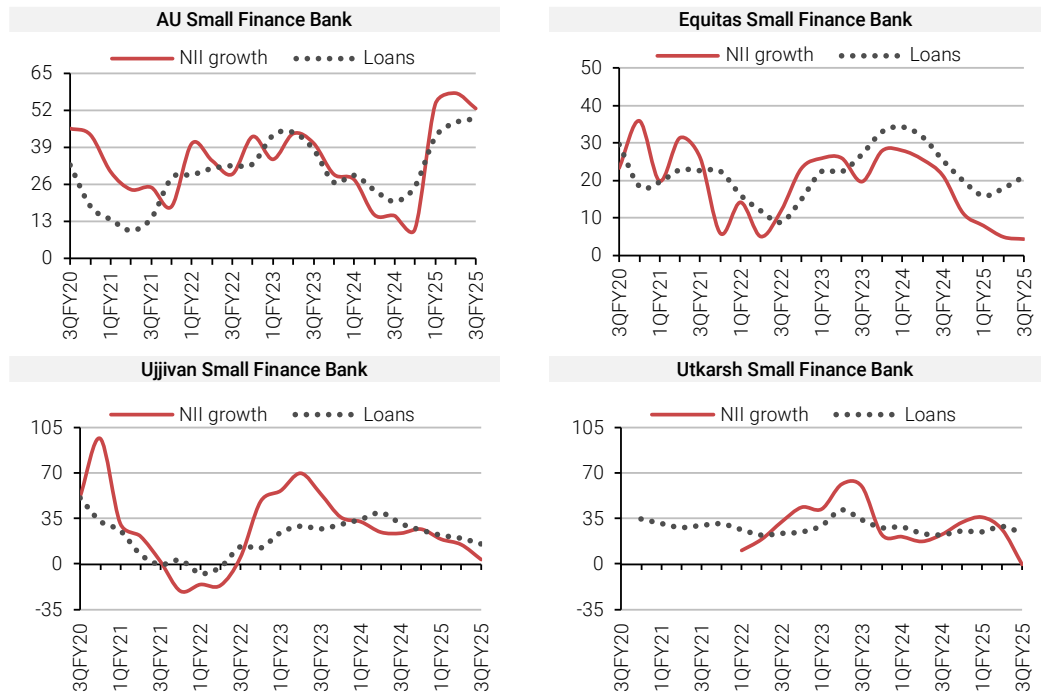
Exhibit 3: NII growth and loan growth for regional private banks, March fiscal year-ends, 3QFY20-3QFY25 (%)



Source: Company, Kotak Institutional Equities

Relationship is relatively stronger for SFBs, reflecting the fixed-rate loans and shorter-duration liabilities

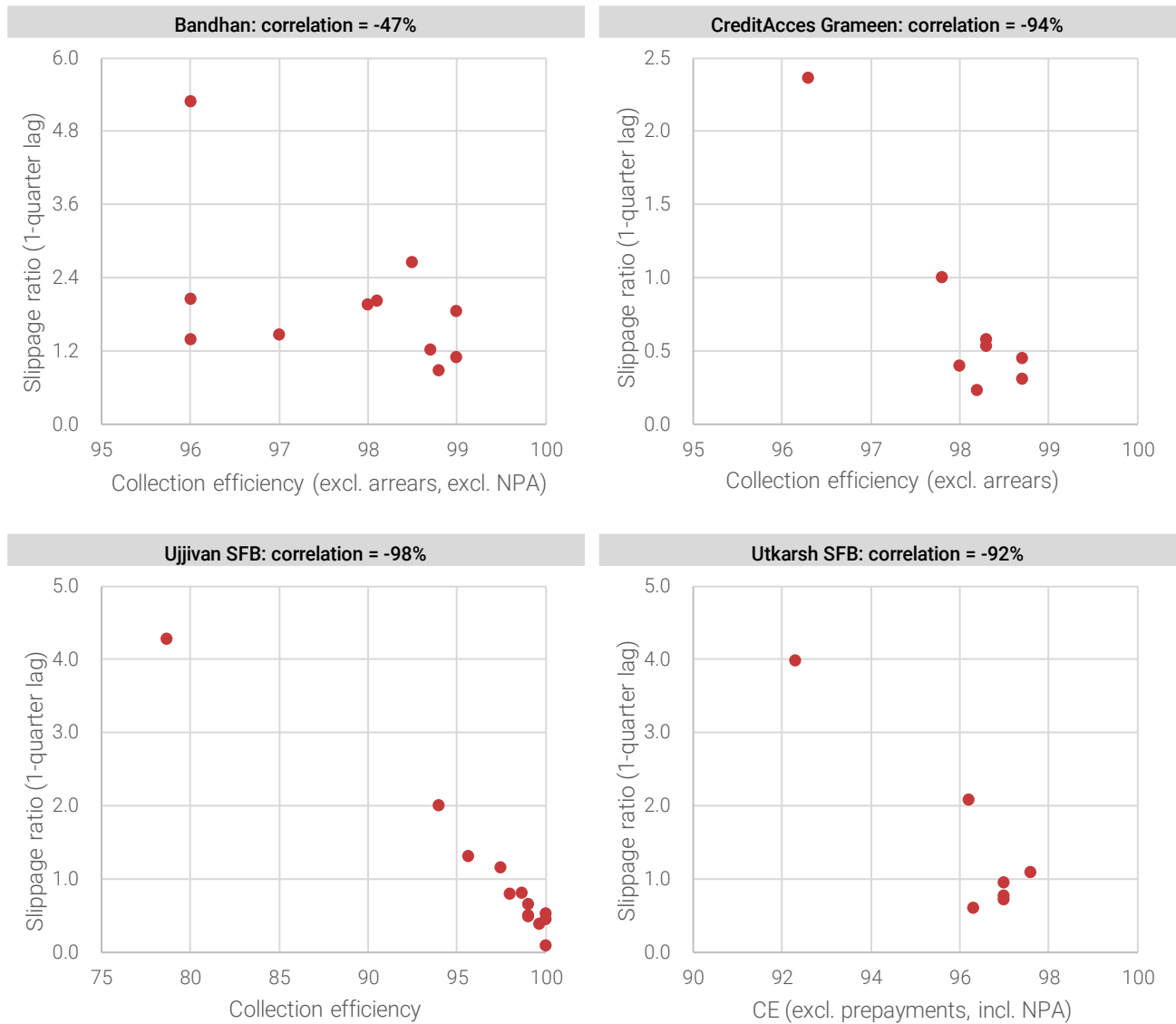
Exhibit 4: NII growth and loan growth for small finance banks, March fiscal year-ends, 3QFY20-3QFY25 (%)



Source: Company, Kotak Institutional Equities

There does exist an inverse relationship between collection efficiency and slippages in the subsequent quarter

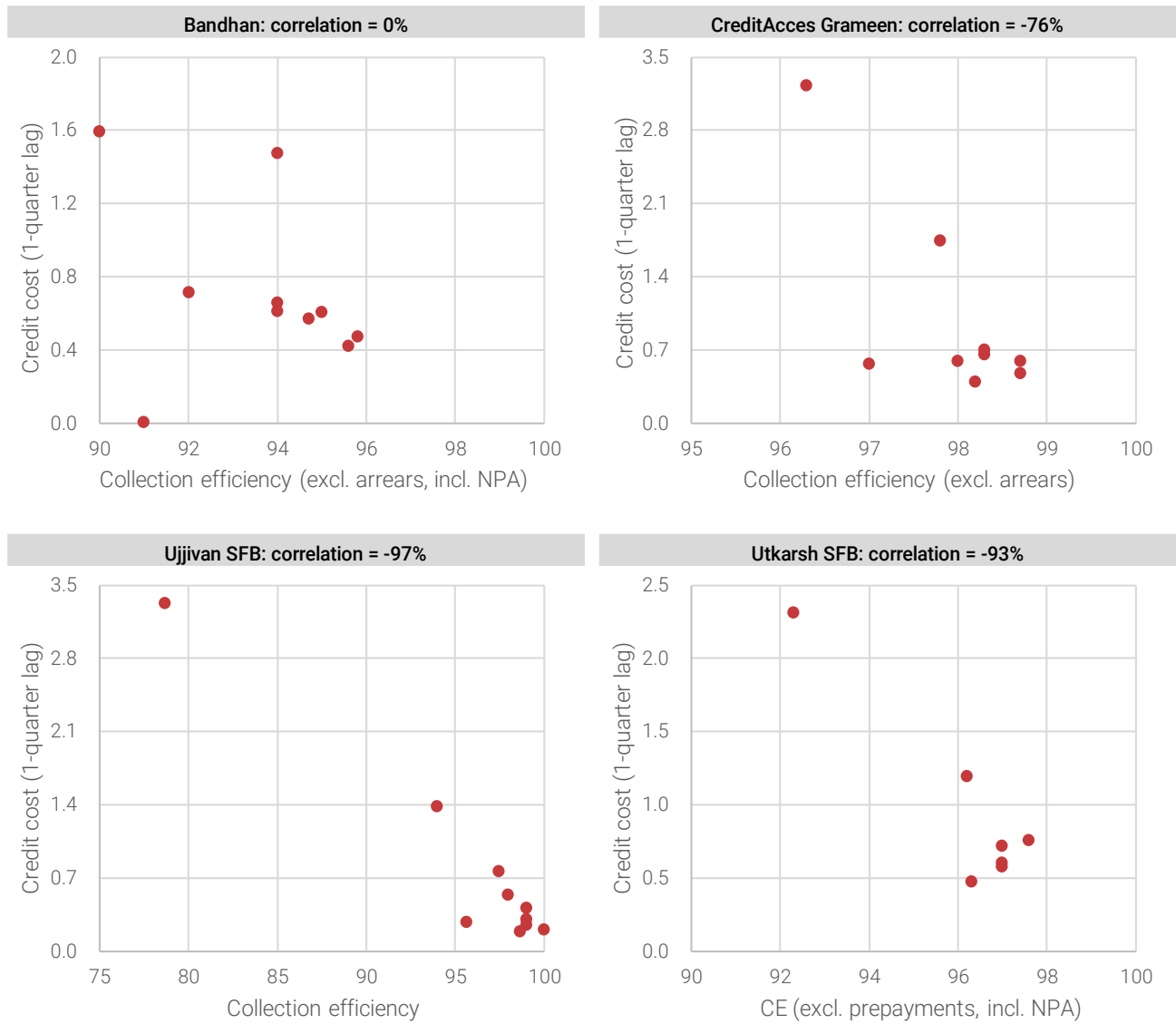
Exhibit 5: Historical relationship between collection efficiency and slippage ratio (1-quarter later), (un-annualized, %)



Source: Companies, Kotak Institutional Equities

There does exist a meaningful relationship between collection efficiency and credit cost as well in most cases

Exhibit 6: Historical relationship between collection efficiency and credit cost ratio (1-quarter later), (un-annualized, %)



Source: Companies, Kotak Institutional Equities

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REDUCE. We expect this stock to deliver -5+5% returns over the next 12 months.

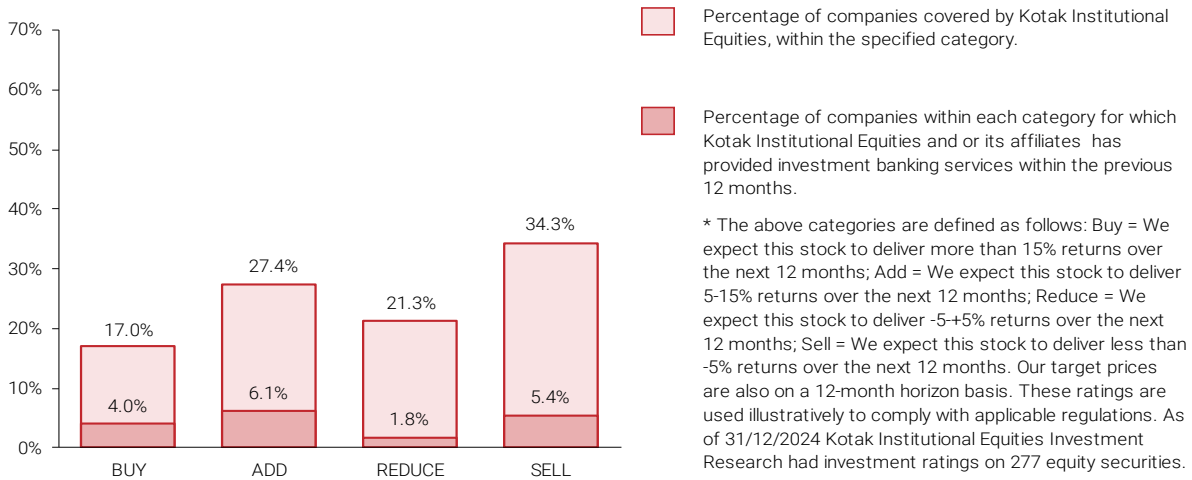
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Source: Kotak Institutional Equities

As of December 31, 2024

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Corporate Office

Kotak Securities Ltd.
27 BKC, Plot No. C-27, "G Block" Bandra Kurla
Complex, Bandra (E) Mumbai 400 051, India
Tel: +91-22-43360000

Overseas Affiliates

Kotak Mahindra (UK) Ltd
8th Floor, Portoken House
155-157 Minories, London EC3N 1LS
Tel: +44-20-7977-6900

Kotak Mahindra Inc
PENN 1,1 Pennsylvania Plaza,
Suite 1720, New York, NY 10119, USA
Tel: +1-212-600-8858

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Details of	Contact Person	Address	Contact No.	Email ID
Customer Care/ Complaints	Mr. Ritesh Shah	Kotak Towers, 8th Floor, Building No.21, Infinity Park, Off Western Express Highway, Malad (East), Mumbai, Maharashtra - 400097	18002099393	ks.escalation@kotak.com
Head of Customer Care	Mr. Tabrez Anwar		022-42858208	ks.servicehead@kotak.com
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