

# Analysis of RBI's Financial Stability Report and NPA

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The RBI's FSR released yesterday presents a rather satisfactory picture of the Indian banking system. Probably the most important indicator that is used to check on the health of the banking system is the NPA related number. Here the system does well with the ratio of GNPA being 6.9% for September 2021. This is contrary to expectations last year when one expected a double digit GNPA number given the covid environment.

In terms of sector wise GNPA there has been an improvement in most of the segments where the numbers were high:

- Construction is down from 21.5% in September 2020 to 21.1% in September 2021
- Gems and Jewellery from 24.1% to 20.7%
- Engineering from 19.4% to 18%
- Food processing moved up from 13% to 14.2%
- Mining from 15.6% to 14.3%
- Infrastructure from 11.9% to 9.2%
- Textiles unchanged at 11.7%

The case for worry is when one looks at the NPAs across the four broad segments of agriculture, industry, services and retail.

## Gross NPA ratio (%)

	September 2019	September 2020	September 2021
Agriculture	10.1	9.6	10.2
Industry	17.3	12.4	9.9
Services	6.3	6.9	6.7
Retail	1.8	1.7	2.5

The retail segment has witnessed an increase in GNPA from 1.7% to 2.5%. Though well below the average the fact that it is increasing is significant considering that banks have been focussing more on retail than industry given the state of the economy as well as demand for funds. Also rates of lending have come down sharply to attract more households to borrow. This has led to easy lending which should be monitored especially so when the NPA rates are inching up. Here again the RBI has provided a break-up of the ratios in different sub-segments within retail for September 2021:

- Education 7.2%
- Credit cards 3.1%
- Vehicles 2.6%
- Housing 2.1%

Interestingly the RBI has also done the stress tests on the assets of banks and juxtaposed the same with economic conditions that drive them and the conjecture is that by September 2022 the GNPA in the baseline scenario would increase to 8.1% from 6.9% in September 2021. The medium and severe stress scenarios would lead this number to increase to 8.7% and 9.5% respectively.

In the past, the RBI's baseline projections have tended to be rather pessimistic: for September 2020 it was projected at 9.9% but came at 7.5%. For September 2021 it was projected at 13.5% but came at 6.9%. Therefore, the final numbers have been lower than that of the baseline projections. Will the September 2021 projection buck this tendency? There is a palpable concern on SMEs and retail loans registering higher NPAs in future and hence the 8.1% number may not be off the mark this time.

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