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'Banks' asset quality woes, capitalization stress to continue'

By PTI | Updated: Aug 02, 2016, 03.53 PM IST

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NEW DELHI: Indian banks will continue to face pressure on their asset quality, profitability and capitalization over the next 12-24 months, S&P Global Ratings said today.

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The US-based agency expects that non-performing loan ratios of Indian banks with high exposure to companies in troubled sectors will continue to rise.

"India's economic risk trend is negative. Prolonged weakness in the asset quality of Indian banks could lead us to assess that economic risks have increased," S&P Global Ratings credit analyst Geeta Chugh said.

In a report titled "Economic woes cast a shadow on Indian and Chinese banks", S&P Global Ratings compared banks in these two countries on parameters such as asset quality, profitability, capitalisation and credit growth.

Banks in India and China will continue to face pressures on their asset quality, profitability and capitalisation over the next 12-24 months, the report said.

"We expect economic risks to remain high for Indian and Chinese banks, which will constrain their credit profiles," Chugh said.

"Asset quality for Indian and Chinese banks is likely to remain under pressure due to slow industrial recovery in India and overcapacity in many Chinese industries," Chugh added.

[Interest-rate liberalisation](#) and deepening [debt capital markets](#) in India could weaken the banking sector's net interest margin (NIM).

"We believe that NIMs will compress for Indian banks with corporate focus and higher bad loans. Banks are also likely to reduce lending rates further, after having cut base lending rates by 70-90 bps in the past few quarters," S&P Global Ratings credit analyst Amit Pandey said.

Continuing high credit costs will also limit any meaningful improvement in profitability, Pandey added.

S&P Global Ratings expects Indian banks to have sizable capital needs to support growth and meet Basel III requirements, which kicked in on April 1, 2013, and will gradually increase until 2019.

"Most Indian public sector banks will have to rely on external capital infusion, given their reduced ability to generate internal capital, largely because of the pressure on asset quality in the past few years," Chugh said.

In view of the potential shortfall in capital, India's PSU banks will need to continue to explore other funding options, including additional Tier-1 issuance, and funding from insurance companies or equity capital markets, she added.

Credit growth in India has fallen sharply, reflecting the weak corporate credit demand as well as capital challenges that most public sector banks are facing.

"We expect loan growth in India's banking sector to be 11-13 per cent in fiscal 2017. We anticipate that corporate capital spending will be weak, given low capacity utilisation and high leverage in certain sectors," it added.

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