

NPLs to rise to 4.5-5%: CRISIL

Retail to be key driver for NPL's: CRISIL

We hosted a conference call with Mr. Tarun Bhatia, Head- Financial Sector Ratings, CRISIL, India's leading credit rating agency, to have a perspective of the asset quality issues in India. CRISIL expects NPLs to rise sharply through FY10-11 and reach 4.5%-5.0% of loans by FY11 from 2.3% in FY08. However, this incl. loans that may be restructured. This compared with BAS-ML est. of around 4% for NPLs and +6% (incl. restructured). As per CRISIL, retail is the key driver (pegged at around 5%); with corporate NPLs at 3.5% by FY11.

Retail NPLs: CVs; lower end mortgage to hurt

As per CRISIL, retail NPL formation could begin to peak around end of FY10; with retail NPLs rising to about 5% by FY11. Sectors that could see more pain could be CVs and smaller mortgages, especially loans of <Rs0.5mn. This, in our view, makes smaller HFCs (housing finance cos.) more vulnerable. We est. average home loan is >Rs1.5mn for most large HFCs. 10% of home loans could see EMI >60% of monthly salary (per CRISIL).

Corporate: SME to be a problem area

Within Corporate segment, CRISIL expects NPLs to come primarily from SME, impacted by export cycle (textiles, gems and jewelry, auto anc.). However, it was fairly sanguine on corporate and infra. loans. Gross NPLs in corporate segment forecast to rise to 2.6% (FY10) and 3.5% by FY11 (incl. restructured).

NPL cycle to be better than last one; solvency not a issue

While downgrades may happen, per CRISIL, the current NPL cycle is likely to be better and shorter than the previous one as a) Company responses are quicker and; b) Leverage levels are much lower (eg. <0.4x for larger cos v/s 0.9x last time). Further, CRISIL emphasized solvency of banks was not an issue, with banks' capital levels being >2x the stressed asset levels.

Profitability may be impacted adversely

Banks' profitability could, however, be adversely impacted owing to rise in credit costs and moderation in growth (CRISIL est. loan growth at 15% in FY10). This is largely in sync with BAS-MLe (earnings growth to collapse in FY10 -see- [here](#)).

Table 1: Gross NPLs to rise but solvency to be much better- system wide

Ratio -%	FY03	FY04	FY05	FY06	FY07	FY08	FY09E	FY10E
Gross NPL/ Gross Loans	8.8	7.2	5.3	3.3	2.5	2.3	2.6	3.8
Net NPLs % of NW	33%	21%	14%	10%	9%	8%	10%	15%

Source: Banc of America Securities-Merrill Lynch Research Estimates



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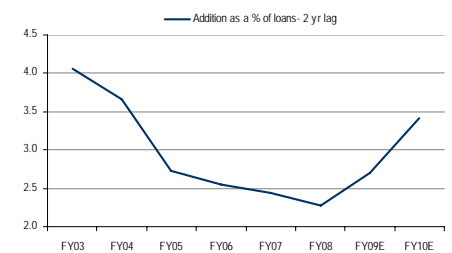
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Chart 1: NPL formation to rise



Source: Banc of America Securities-Merrill Lynch Research Estimates

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