

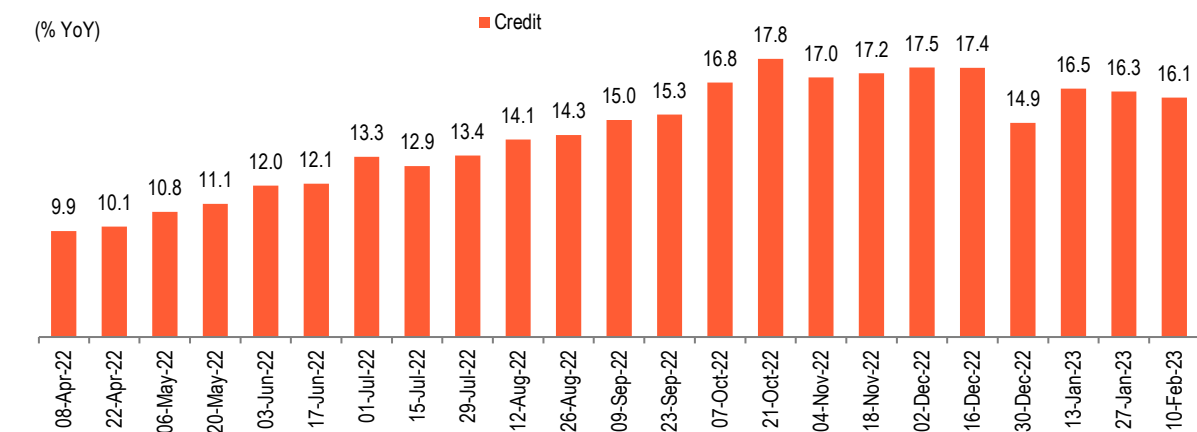
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Is credit growth tapering off?

Credit growth in India has seen a sharp revival in FY23. On a YoY basis, from just 9.9% at the start of Apr'22, credit growth picked up pace and peaked at 17.8% in Oct'22. This coincided with the festive season where the pent up demand for both goods and services showed. Thereafter, there were some signs of moderation with growth in credit eventually decelerating to 14.9% in the last fortnight of Dec'22. While there has been some revival in credit growth since then, it does beget the question of whether trend is sustainable. The RBI has been increasing the repo rate which has been transmitted to a large extent in lending rates. The main goal of increasing the repo rate is to slow down the pace of activity to control inflation. In this study, we analyze the trends in credit growth this year and its main drivers.

Figure 1: Credit growth has been robust

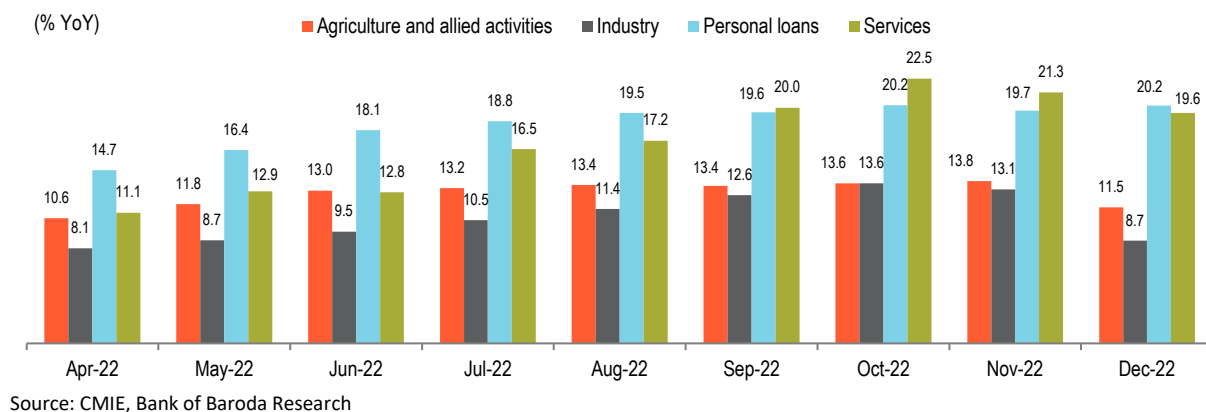


Source: CMIE, Bank of Baroda Research | Fortnightly data as of 10 Feb 2023

Figure 1 provides trends in growth in credit on a y-o-y basis for all the fortnights of the year. The trend has been upwards in the growth rate which peaked in October and then remained in the 17-18% range for the next 4 fortnights before coming down to 14.9% in the last fortnight of December. Subsequently there has been a recovery to the 16-17% range though the growth rate has been coming down. In a way policy has slowed down the growth in credit though not in a commensurate manner.

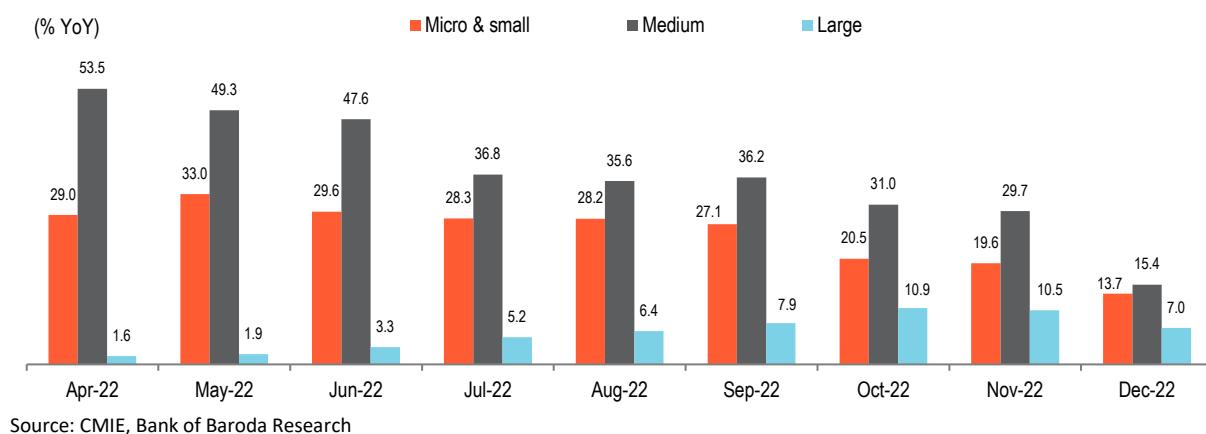
Credit growth in FY23 has been driven by increased credit demand in the personal loans and services segment (Figure 2). Demand for agricultural credit has also shown traction. On the other hand, credit to industry though improving, has remained muted as credit demand has moderated sharply from 13% in Nov'22 to 8.7% in Dec'22. Retail credit which has been driving majority of credit growth this year, has continued to accelerate and registered a solid growth of 20% YoY in Dec'22 as well. Credit growth from the services sector despite moderating a bit in Dec'22, continues to grow at a robust pace.

Figure 2: Retail and services driving credit growth



Within industry (Figure 3), credit demand from the MSME segment has seen a marked slowdown since the start of the year. In fact, while credit growth to micro and small segment has moderated from 29% in Apr'22 to only 13.7% in Dec'22, for medium industries the decline has been much alarming from 53.5% to just 15.4% in Dec'22. A part of the explanation lies in the fact that a large quantum of such loans are linked to the external benchmark like the repo. Hence with the repo rate going up there has been a proportional transmission to their borrowing cost. This is different for the larger companies which borrow on the basis of MCLR. Hence there is a contrast here where credit to large corporates had shown an increasing trend for much of the year. From just about 1.6% in Apr'22, credit to large industry peaked at 10.9% in Dec'22. However, here too credit demand has slowed down in recent months from 10.9% in October to 10.5% in November and further to 7.5% in December. The growth in credit here has been driven by the sectors roads, airports, steel and automobiles.

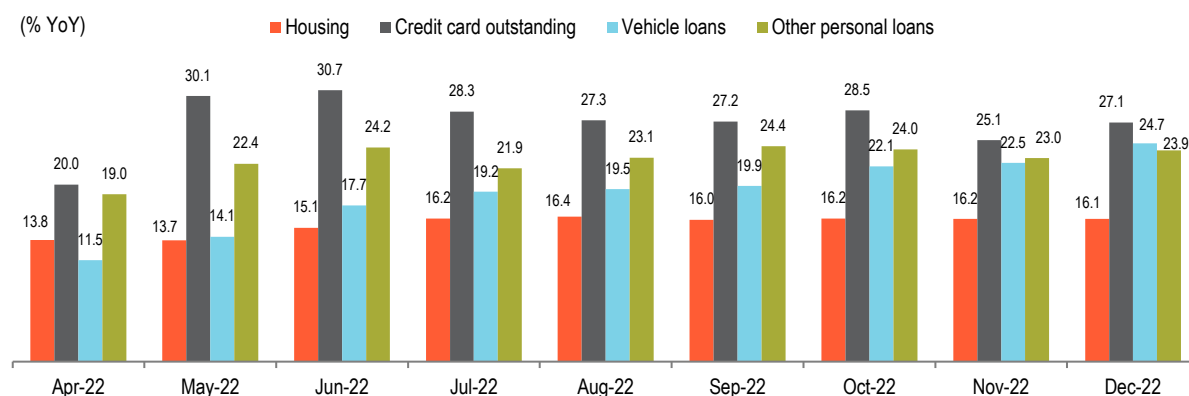
Figure 3: MSME credit has been decelerating



In the personal loans segment (Figure 4), housing which accounts for more than 50% of the credit under this segment, has shown a stable and smart growth over the last few months. It must be noted that this is despite the fact that interest rates on home loans have increased due to rate hikes by the RBI. It is possible to conclude that higher repo rates and hence borrowing costs for home loans has not dented demand significantly. The same is true for vehicle loans which have also been increasing from 11.5% in Apr'22 to 24.7% in Dec'22. The pent up demand for vehicles due to supply side issues

last year has made customers less interest rate sensitive. For credit cards growth has been robust, although the trend has varied over the months. Growth in o/s here is dependent more on consumerism which was driven by pent up demand for an extended period of time. Even other personal loans segment has shown significant variation this year, but have grown at a decent rate.

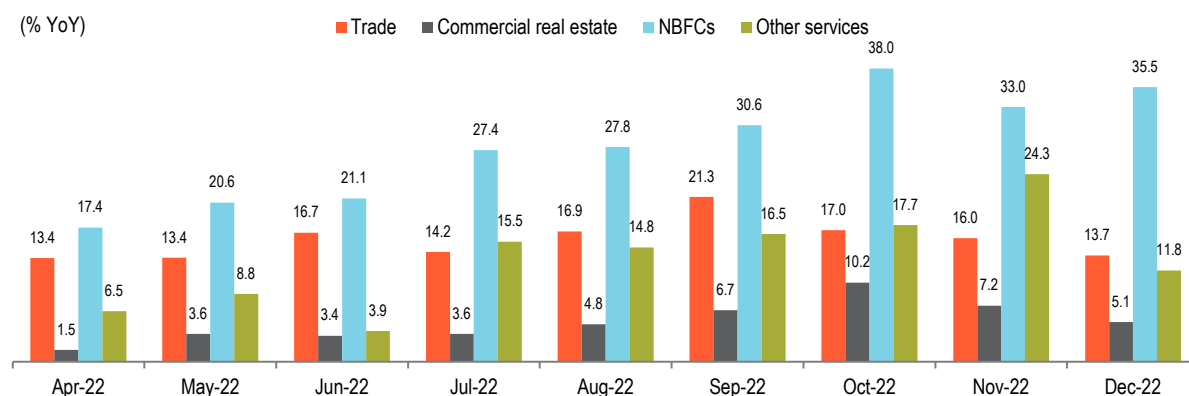
Figure 4: Housing credit demand has been robust



Source: CMIE, Bank of Baroda Research

Within services (Figure 5), much of the growth has come from NBFCs which have been growing at a rate of more than 30% even in Dec'22. Credit to wholesale and retail trade, which showed momentum initially, has shown deceleration in recent months. Credit to commercial real estate has also shown a similar trend, though the growth in this segment has been much more muted. In general growth remains stable though has shown a decline in the last two months.

Figure 5: NBFCs lead in growth in credit to services



Source: CMIE, Bank of Baroda Research

Conclusion:

Ever since the RBI embarked on the rate hike cycle, concerns were being raised on its impact on credit demand. As the year unfolded, credit growth showed continued signs of resilience despite a cumulative 250bps hike in policy rate by RBI. In FYTD23, credit growth has grown in double digits at 16.1% (as of 10 Feb 2023), after increasing at a subdued pace of 8.6% in FY22. *However after being in the region of 17-18% in 5 successive fortnights ending December 16th 2022, growth is now in the range of 16-17% in the last 3 fortnights. Another interesting observation so far is that loans linked to external*

benchmark have behaved differently: for MSMEs growth in credit has slowed down while in case of personal loans, growth has been maintained. To recap:

- Retail credit has been a major driver of credit growth in this period. Within this, housing segment has seen continued momentum amidst an increasing demand for housing, despite higher interest rates and prices. This is unlikely to change in the near-term, and hence retail credit demand will continue to register strong growth.
- Another segment which has continued to do well is the services segment, where led by NBFCs, credit growth has been strong.
- However, alarmingly, credit growth to industry has been decelerating after peaking in October and remains a key area of concern. With global growth likely to slowdown, exports and domestic manufacturing will also come under stress, which may dampen the credit offtake from this sector even more.

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