Signs of a turnaround

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Signs of a turnaround-Regulatory vigil should not ease after the half-yearly decline in banks' gross NPA ratio

- The fog of bad loans shrouding the banking sector appears to be lifting after a long period of sustained stress.
- The Reserve Bank of India's Financial Stability Report reveals the first half-yearly decline in the ratio of gross non-performing assets (GNPA) to advances since September 2015.
- A stress test for credit risk at banks that models varying levels of macro-economic performance shows that for the baseline assumption, the GNPA ratio would narrow to 10.3% by March 2019.
- This prompted RBI Governor Shaktikanta Das to prognosticate that the sector "appears to be on course to recovery".
- Still, state-owned banks continue to have higher levels of bad loans than their private sector peers and are projected to show slower improvements over the second half of the fiscal.
- The GNPA ratio for public sector banks (PSBs) is posited to only inch lower to 14.6% by March, from 14.8% in September.
- Interestingly, the RBI's Prompt Corrective Action (PCA) framework, which attracted criticism including from a government appointee on the central bank's board, has significantly helped lower contagion risk to the banking system.
- The RBI's report has justifiably spotlighted the urgent need to tighten the oversight framework for financial conglomerates in the wake of the IL&FS meltdown, which continues to ripple across the financial system, including at mutual funds and non-banking financial companies.
- Regulators and policymakers need to work together to insulate the economy from the risks of similar fiascos.

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