Banking – An Abandoned Baby Could Be The Long Term Bestie

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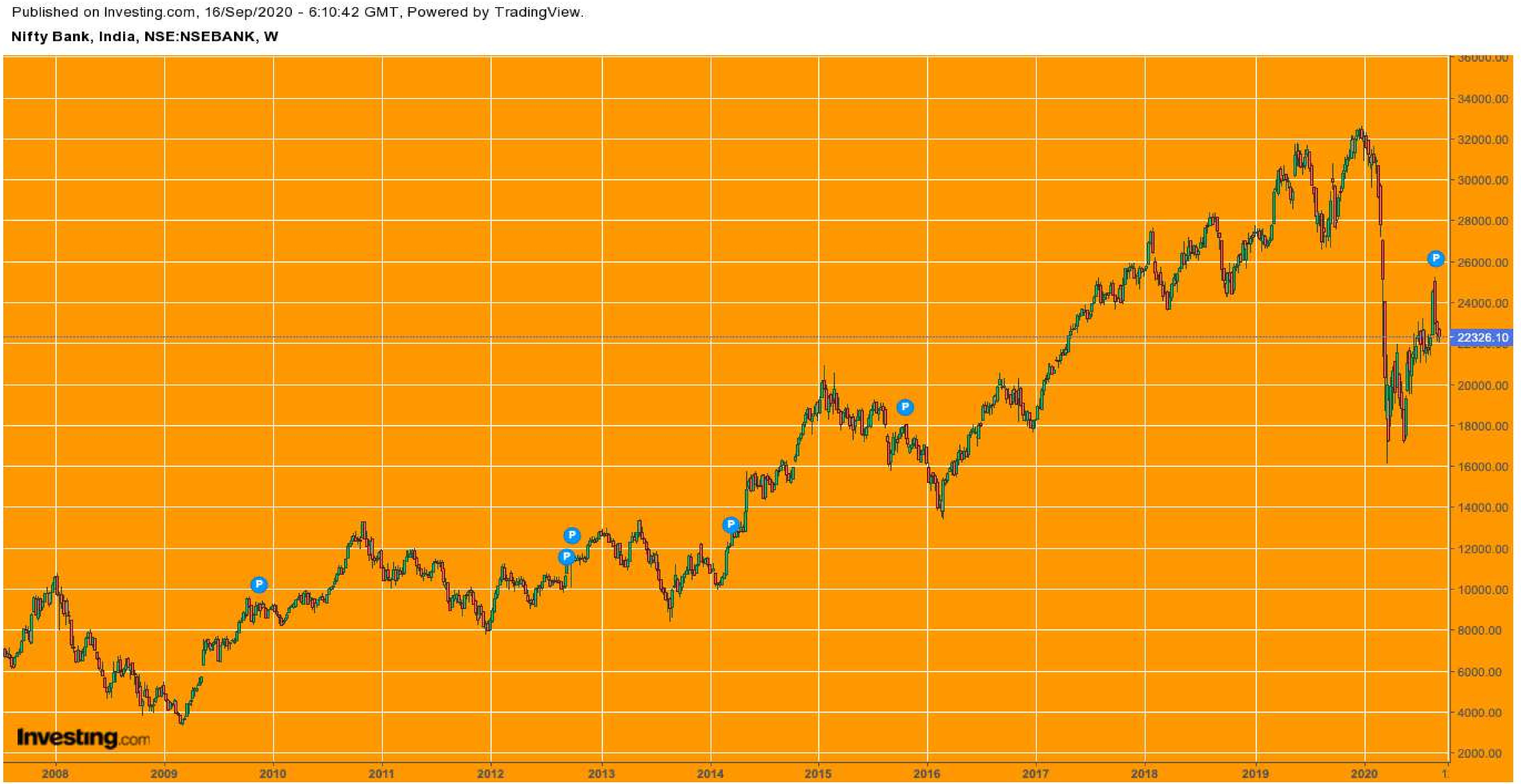
BANKS, A LONG RUNWAY; PATIENCE IS KEY



AN ABONDONDED BABY COULD BE THE LONG TERM BESTIE

- There is a lot that depends upon credit growth as far as the economic growth is concerned. The banking credit supports and fuels consumption which is the backbone of Indian economic growth as well as meets the investment demand by the industries.
- The current outstanding banking credit is about 50% of GDP of India. Government of India (GOI) target to make India a USD 5 Trillion economy. If that be the case then banking credit will also grow accordingly. The growth in banking credit, in turn, will boost the topline of the banks.
- The NPA trend has been declining off late and banks' balance sheet are becoming much more cleaner. RBI directives to banks to implement automated process to recognize non-performing loans (NPL) and daily recognition of NPL is re-emphasizing its intention of keeping the balance sheets much transparent and cleaner. One thing which has always troubled global economists is, India having one of the highest NPAs in the region. These steps are certainly in a direction to bring that down and would entail confidence in the global arena as well.
- On the back of Covid19, banking sector has been hit badly because there is a possibility of NPAs wobbling the system. The overhang of expected supreme court verdict regarding charging/waving interest on interest during the period of moratorium has marred the sentiments in the sector further. Having said that most of the negatives are already in the stock price of banking stocks.
- KV Kamath report on loan restructuring will further aid banks with meaningful loan restructuring. The committee took note that 70% of banking system credit was impacted by Covid19; some less, some more.
- Under this type of situation certainly the banks with more of retail exposure and less exposed to troubled sector would benefit, but according to me, as a fallout of Covid19, the larger banks will grow even larger. Agreed, that there are clouds of uncertainty over short term but the best investments are made when there is extreme pessimism and I believe, the pessimism in banking sector is highest ever, even higher than what I had seen in 2008.
- The price to book ratio of banking sector as an average is below their mean and when the good times will come back, the most of the money will be made in the expansionary phase.
- Bonds yields might have largely bottomed out. Low interest rates are not so favourable to banks' topline. It looks to me that 10 year G-sec yield has bottomed out and it will travel higher over a year time.
- Banking stocks may grapple in the short term and situation will become more clear after September 2020 and December 2020 quarterly results. Even the overhang of supreme court judgement can keep the minds clouded in immediate future.
- My belief in banking stocks emerges more from the potential growth in Indian economy that GOI is eyeing for. I have my strong conviction that India long term growth story is intact and is emerging even stronger with passage of time. Times have not been kind enough for Indian economy in the past but for what I know, times change and this time it may change for good.
- As per my analysis, it is just the matter of uncertainty getting over and the banking stocks will regain their mojo; and once they regain, sky is the limit over 4-5 years.