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June 26, 2018

RBI releases June 2018 Financial Stability Report

The Reserve Bank of India today released the [Financial Stability Report \(FSR\)](#), 17th in the series.

The FSR reflects the overall assessment of the stability of India's financial system and its resilience to risks emanating from global and domestic factors. The Report also discusses issues relating to developments in and regulation of the financial sector.

Overall assessment of systemic risks

Global and domestic macro-financial risks

- Global growth outlook for 2018 remains positive despite some recent softness.
- Spillover risk from advanced financial markets to emerging markets, however, has increased.
- Tightening of liquidity conditions in the developed markets alongside expansionary US fiscal policy and a strong US dollar have started to adversely impact emerging market currencies, bonds and capital flows. Firming commodity prices, evolving geopolitical developments and rising protectionist sentiments pose added risks.
- On the domestic front, economic growth is firming up. However, conditions that buttressed fiscal consolidation, moderation in inflation and a benign current account deficit over the last few years, are changing, thereby warranting caution.
- In the domestic financial markets, structural shifts are altering the pattern of credit intermediation and impacting market interest rates. These developments, while a healthy sign of diversified financing of the economy, call for greater vigilance of the system as a whole in order to safeguard financial stability.

Financial Institutions: Performance and risks

- The stress in the banking sector continues as gross non-performing advances (GNPA) ratio rises further.

- Profitability of SCBs declined, partly reflecting increased provisioning. While this has added pressure on SCBs' regulatory capital ratios, the provision coverage ratio has increased.
- Credit growth of SCBs picked up during 2017-18 notwithstanding sluggish deposit growth.
- Macro-stress tests indicate that under the baseline scenario of current macroeconomic outlook, SCBs' GNPA ratio may rise from 11.6 per cent in March 2018 to 12.2 per cent by March 2019. The system-level capital to risk-weighted assets ratio (CRAR) may come down from 13.5 per cent to 12.8 per cent during the period; eleven public sector banks under prompt corrective action framework (PCA PSBs) may experience a worsening of their GNPA ratio from 21.0 per cent in March 2018 to 22.3 per cent, with six PCA PSBs likely experiencing capital shortfall relative to the required minimum CRAR of 9 per cent.
- The capital augmentation plan announced by the government will go a long way in addressing the potential capital shortfall, while also playing a catalytic role in credit growth at healthier banks. In parallel, the Reserve Bank's PCA framework, by preventing further capital erosion at weaker banks, is intended to help strengthen these banks to a point of resilience from where they can restart normal operations. In addition, governance reforms - If undertaken promptly and well - would not only improve the financial performance of the banking sector but also help reduce operational risks.
- Overall, the regulatory and supervisory measures bode well for allocative efficiency and financial stability in the medium term even if there is some short-term pain in the process.