

Tracking the pace of credit growth

YO-YOING. Growth was excessive during 2002-03 to 2013-14, cooled thereafter, only to pick up in the 2 years ending 2023-24



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Bank credit, along with other important variables like fiscal policy, industrial policy, investment and technology adoption, has implications for the real economy. Credit growth, though not sufficient, is a necessary condition for economic growth. But the pace and nature of credit growth when excessive and exuberant invariably ends up in credit losses and may even threaten financial stability. If the pace is suboptimal, it may end up in forgone real economy growth. Finding the right pace and content of credit growth is essential for sustained and consistent real economy growth.

In fact, the relationship between credit and growth is the same as between money and growth. First, there is an accommodative role. As the economy grows, it needs more money or credit. People who only emphasise the accommodative role talk about the analogy that as a man grows, he needs pants of bigger size. But by wearing pants of bigger size, he cannot grow.

But many reject the pure accommodative hypothesis. On the other hand, they argue that it can play also a stimulant role. But credit or money beyond a level can harm the economy. Against this background, bank credit growth over the last two decades is analysed.

Exuberance phase of credit growth: 2002-03 - 2007-08 (Table 1): The magnitude of exuberance can be gauged from the fact that the ratio of credit growth to nominal GDP growth reached as high as 2.2. A ratio of more than one may spell trouble with a lag.

Bank credit grew by ₹16 lakh crore, from ₹6 lakh crore in FY 2003 to ₹22 lakh crore in FY 2008. This was an increase of 266 per cent during this 5-year period as compared to an increase of ₹2.5 lakh crore, representing an increase of 81 per cent during the earlier 5-year period ending 2002. This was an all-time high for several decades.

Credit growth was more than double and even triple of real economy growth and far exceeded even nominal growth

Major sectoral increases — infrastructure: Two sectors need special mention. Infrastructure finance, inherently risky, shot up from ₹20,000 crore to over ₹2 lakh crore (900 per cent increase) and personal loans led by housing finance shot up from ₹63,000 crore to over ₹5 lakh crore (700 per cent) while the aggregate credit increased only by 265 per cent during

Nominal GDP & gross NPA (All figures in %)

Year	Credit growth	Gross capital formation	GDP real	GDP nominal	Gross NPA	Inflation CPI
2002-03	26.9	26.8	4.0	7.7	8.8	4.0
2003-04	18.4	29.0	8.2	12.0	7.2	3.5
2004-05	31.6	35.2	7.5	14.1	5.1	3.8
2005-06	31.8	36.4	9.5	14.0	3.3	4.4
2006-07	28.5	36.0	9.7	17.1	2.5	6.7
2007-08	23.0	39.1	9.3	15.1	2.2	7.9
2008-09	17.8	38.9	6.7	12.6	2.2	8.0
2009-10	17.1	39.8	8.4	15.5	2.4	12.4
2010-11	21.3	39	8.9	19.9	2.2	10.4
2011-12	16.8	38.7	6.7	14.4	2.8	8.4
2012-13	14	33.8	4.5	13.8	3.2	10.2
2013-14	14.2	33.8	6.3	13.0	3.8	9.5
2014-15	9.3	33.5	7.8	11.0	4.3	5.8
2015-16	9.1	32.1	8.1	10.5	7.5	4.9
2016-17	5.2	32	7.1	11.8	9.3	4.5
2017-18	10.2	33.9	6.5	11.0	11.2	3.6
2018-19	13.4	33.6	6	10.6	9.1	3.4
2019-20	6.1	36.4	3.9	6.4	8.2	4.8
2020-21	5.5	30.4	-4.2	-0.14	7.3	6.2
2021-22	9.7	27.9	8	18.4	5.8	5.5
2022-23	15.3	31.4	6.6	16.1	3.9	6.7
2023-24	15.0	34.0*	7.6	10.2	2.9	5.4

Source: RBI data based on Indian Economy *est

this 5-year period ending FY 2008.

Initially, monetary policy was accommodative. Inflation which was low initially, started inching up from 2006-07 onwards. Subsequently, during 2006, RBI had tightened monetary policy by enhancing risk weights and provision requirements, in order to rein in credit growth from 30s to 20s. But it took a couple of years for these measures to deliver some results.

The period also witnessed high gross capital formation, surpassing 39 per cent. Real GDP growth was very high, recording around 9.5 per cent for three years in a row starting 2005-06. Gross NPAs, which were high at 8.8 per cent in 2002-03, were on the decline reaching a low of 2.2 per cent.

Excessive credit growth: 2008-09 - 2013-14 (Table 2): Though credit growth was less than the earlier period in relative terms, its ratio to nominal GDP continued to be above one indicating credit excesses. In absolute terms credit grew by ₹34 lakh crore to ₹60 lakh crore during this period against ₹16 lakh crore during the previous

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period. But the growth rate was only 130 per cent against 265 per cent during the previous period.

Sectoral credit flows: Credit expansion was evenly distributed across all three sectors — agriculture, industry and personal loans. All these three sectors witnessed around 100 per cent increase in line with overall credit expansion. Industry credit doubled from ₹10 lakh crore to ₹20 lakh crore, personal loans from ₹5.5 lakh crore to ₹10 lakh crore, agriculture from ₹3.3 lakh crore to ₹7 lakh crore.

Infrastructure finance — push by public sector banks: However, infrastructure credit grew much faster by a huge 240 per cent from ₹2.5 lakh crore in 2008-09 to ₹8.5 lakh crore in 2013-14. Infrastructure finance grew by a whopping 38 per cent in just one year — that is, during 2010-11. Power sector accounted for a high of 50 per cent. Inflation shot up to as high as 12.4 per cent by 2009-10. Even though gross NPAs look comfortable at 3.8 per cent, restructured advances were as high as 7 per cent, taking the impaired advances to as high as 10.8 per cent. A new phase of slowdown of credit growth began in 2011-12.

Credit growth lower than nominal GDP growth: 2014-15 - 2021-22 (Table 3): In a reversal of the earlier trend, the ratio of credit growth to nominal GDP was less than one, indicating a cooling of

credit growth. This was the slowest growth rate in decades. The deceleration of credit growth which started during 2011 continued during the most of this period. During the 5-year period ending 2015-20 (excluding Covid affected years), credit grew by ₹38 lakh crore to ₹103 lakh crore, representing a growth rate of only 60 per cent when compared to previous two five-year periods' growth rates of 265 per cent and 111 per cent, respectively. This period was marked by intense supervisory action by way of AQR (Asset Quality Review), Prompt Corrective Action (PCA) on over 12 banks and recognition of several big ticket NPAs and their resolution. All these measures impeded credit growth, mostly of public sector banks.

Sectoral credit flows — 2015-22: While the overall credit grew by only 84 per cent over the 7-year period, the personal loans segment grew by a whopping 200 per cent from ₹12 lakh crore in 2014-15 to as high as ₹36 lakh crore. This sector surpassed the industrial sector, which grew by a mere 23 per cent from ₹26 lakh crore to ₹32 lakh crore. Thanks to regulatory forbearance and the government's ECLG scheme, MSME sector credit more than doubled from ₹4.7 lakh crore to ₹10 lakh crore. Infrastructure finance continued to grow, but at a slower pace, registering a growth of 33 per cent from ₹9 lakh crore to ₹12 lakh cores. Gross NPAs spiked as high as 11.8 per cent by 2017-18, as regulatory forbearances were withdrawn. Exuberance had shifted from corporate lending to the personal loan segment.

Resumption of credit growth: 2022-23 and 2023-24 (Table 4): After almost 11 years of deceleration, credit growth had picked up during these two years with an annual growth rate of around 15 per cent (Table 4). Outstanding credit grew from ₹143 lakh crore in 2022-23 to ₹164 lakh crore during 2023-24. But again, credit to nominal GDP growth at around 1.5 indicates probable credit excess.

Sectoral flow: The personal loans segment continued its high growth rate, recording an increase of nearly 51 per cent from ₹35 lakh crore in FY 2022 to ₹53 lakh crore in FY 2024. Infra sector grew by a mere 8 per cent from ₹12 lakh crore to ₹13 lakh crore, and industrial sector grew only 11 per cent from ₹32 lakh crore to ₹36 lakh crore. Outstanding personal loans, at ₹53 lakh crore, far exceed industrial sector loans of ₹36 lakh crore. The growth of personal loans may be unsustainable.

To be concluded

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