

Lending Sector Allocation

Historically, Indian banks were seen as a stable barometer of economic growth, but they have recently become more cyclical. The Indian banking sector is currently in an advantageous position characterized by **cleaner balance sheets and a re-acceleration in credit demand**.

In this note, we position Nifty Bank Index to obtain an exposure to the banking sector, giving us a broader exposure to the space.

Factors Driving allocation:

- ▶ **Asset Quality:** Non-Performing Assets (NPAs) across both public and private sectors have declined significantly since FY18 due to a focus on credit quality and judicious corporate borrowing. Gross NPAs have fallen from >5% to ~2.5%, with Net NPAs under 1% at an overall level
- ▶ **Capital & Growth:** Banks are well-capitalised, maintaining buffers comfortably above regulatory requirements, which supports a projected credit growth of approximately 15%.
- ▶ **Infrastructure and capex pick up** – There is a push for infrastructure investment and private capex to pick-up for capacity addition. This provides an additional tailwind for credit growth.
- ▶ **Pickup in consumption** – As Private Final consumption expenditure expands, the demand for credit will pick-up in that segment.
- ▶ **Key Risks:** A primary concern is the Credit-Deposit (CD) ratio, which stands at ~82%, indicating that credit growth is outpacing deposit growth. Additionally, the "financialization of savings" is seeing funds move toward equities rather than traditional bank deposits.

Nifty Bank Index: Favourable Valuations

The Nifty Bank Index, which tracks **14 major public and private banks**, is currently viewed as an attractive tactical allocation.

- ▶ **Historical Context:** After a massive rally from 2000–2008 (36% CAGR), the index became more cyclical post-Global Financial Crisis (GFC), delivering only an 8% CAGR between 2008 and 2020 (pre-covid).
- ▶ **Current Valuation:** The index is trading at a Price-to-Book (P/B) multiple of 1.9x, which is meaningfully below its 25-year average of 2.3x.
- ▶ **Recommendation:** We recommend a lumpsum tactical allocation to the Nifty Bank Index over an 18–24-month horizon. Improving fundamentals, attractive valuations, and an accelerating capex cycle create a compelling mean-reversion opportunity in the near term. As valuations re-rate and risk-reward moderates, we would rotate capital back into direct infrastructure beneficiaries. Our preferred vehicle is the Nifty Bank Index in the mutual fund universe.

Detailed note on - Allocation to lending Sector

Banks have been one of the largest contributors of market rallies in the past, they are seen as the barometer of economic growth. Private banks had an optionality attached to them such as insurance, NBFC, asset management, wealth management, etc. which led them to trade at higher multiples, relative to public sector banks were seen as plain vanilla banks and hence traded at discounted multiples.

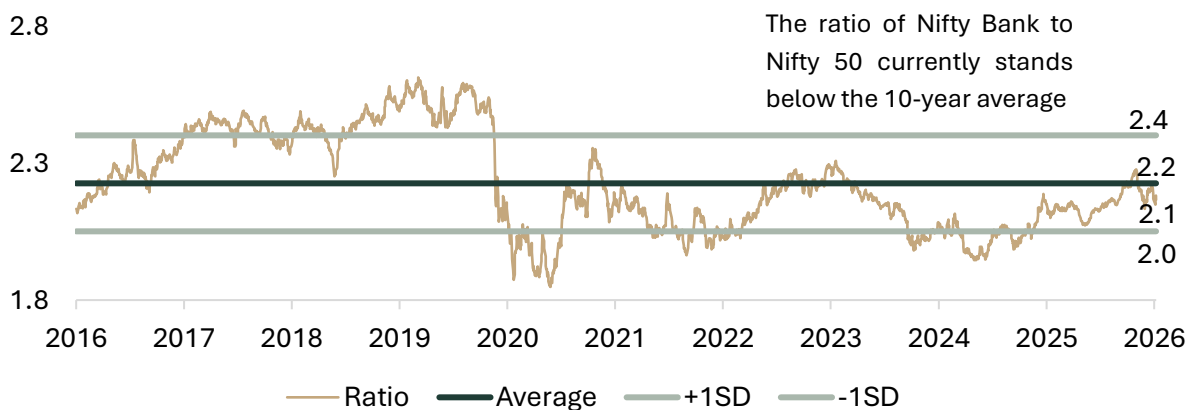
However, most private banks have now demerged other business segments, the asset quality of PSU banks has improved reasonably. Now, both private and public sector banks are valued purely based on their lending ability.



TradingView

At the current juncture the banking sector stands at an advantageous position combined by **favourable valuations, improved fundamentals, and a re-acceleration of credit demand.** Moreover, the sentiment around lenders has turned negative, giving an opportunity in the sector.

Nifty Bank to Nifty 50 - below 10 year average

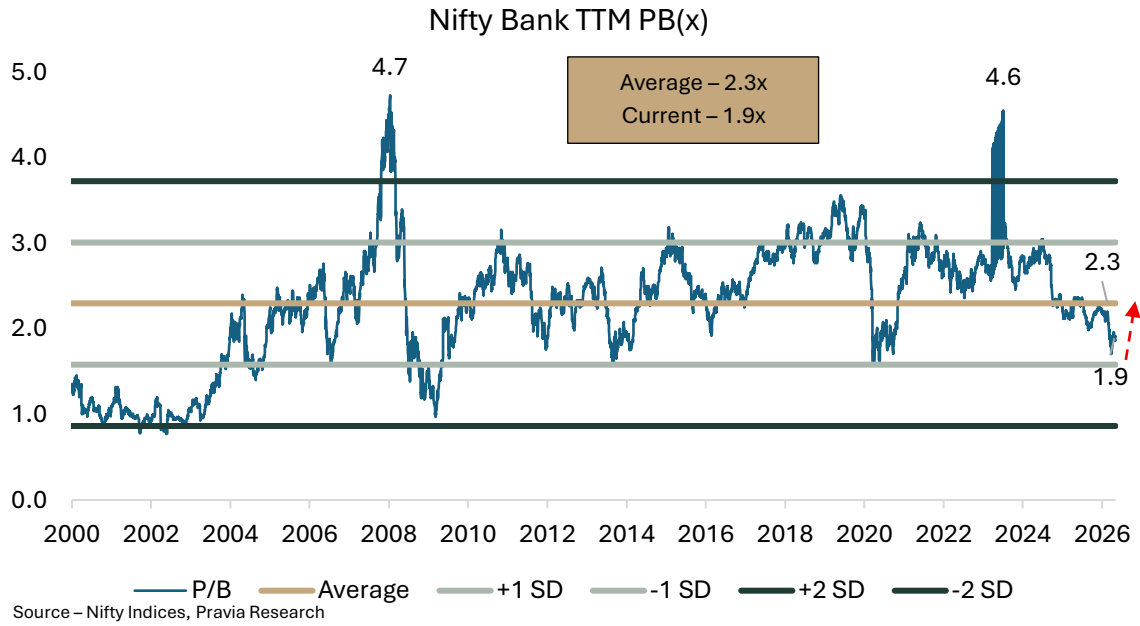


Source – Nifty Indices, Pravia Research



Valuations of the sector – Favourable with a potential of mean reversion

Nifty Bank Price-Book multiple – meaningfully below 25-year average



Decomposition of price movement – Valuation multiple compression



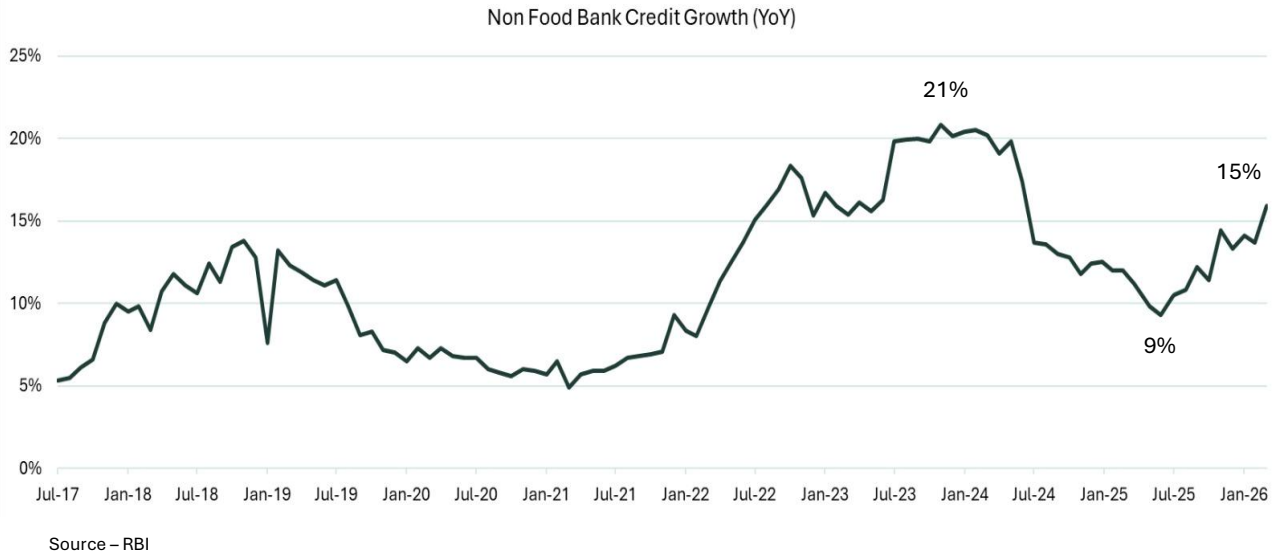
Source – Nifty Indices, Pravia Research

Fundamentally, the bank index has improved in book value terms, the moderation in returns is majorly on account of shrinking of the price to book multiple of private banks which comprise 65% of the overall portfolio.

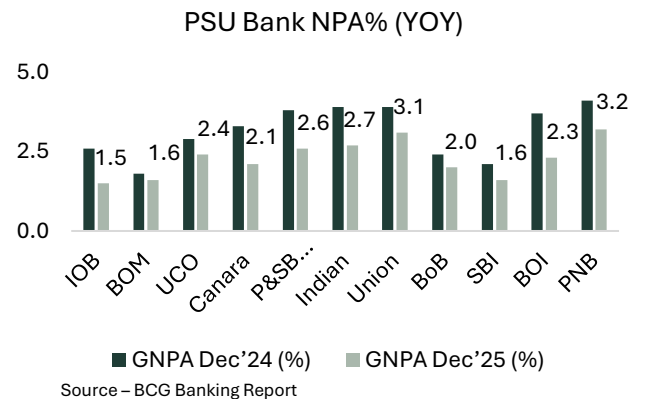
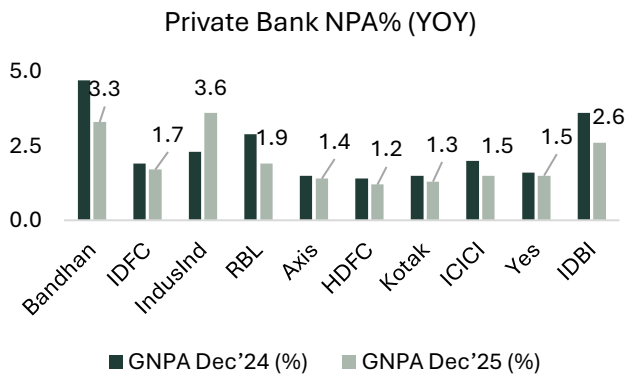
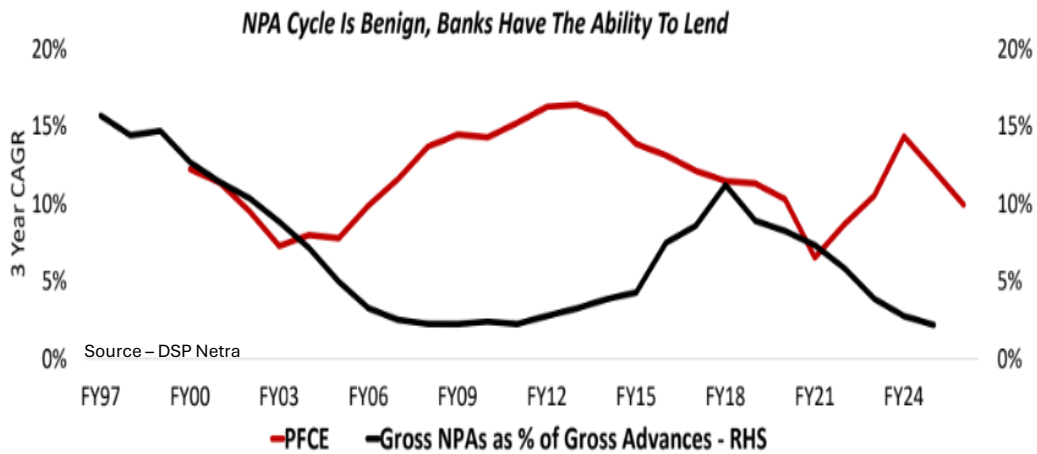


Improving Fundamentals of banks

1) Credit Growth – Improving

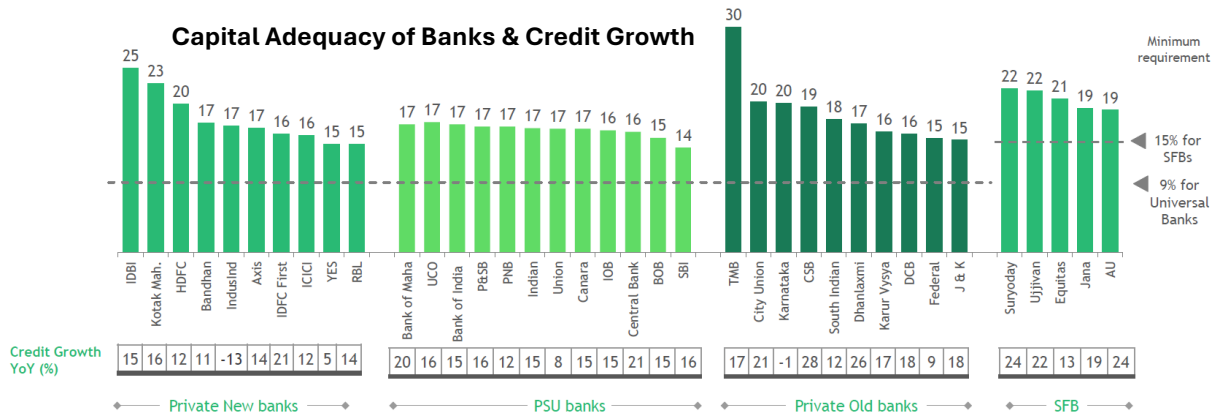


2) Cleaner Balance Sheets – Lower NPAs, increasing headroom for lending



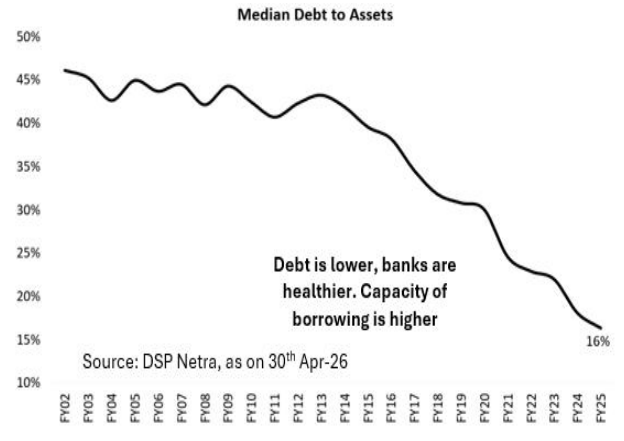
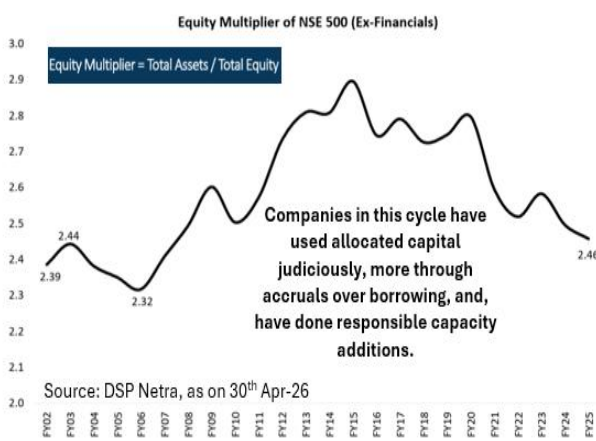
NPAs across private as well as public sector banks have declined meaningfully since FY18, there has been a major cleanup in bank balance sheets, coupled with a more credit quality focused lending and judicious borrowing on the corporate front. As consumption picks up, rates top out, infrastructure spending continues, bank balance sheets can move from repair mode to expansion mode, supporting credit growth and expansion in NIMs.

3) Capital buffers remain strong, supporting continued credit growth



Pravia Insight – Indian banks are currently very well capitalized overall, with most banks comfortably above regulatory minimum requirements. Banks have adequate room for absorbing losses, room to grow lending, and no immediate requirement to raise capital.

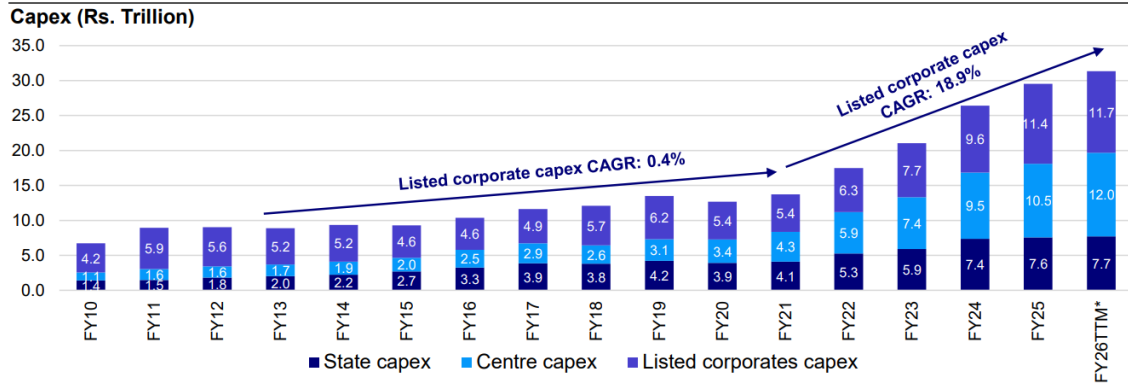
4) Corporate Balance Sheets are cleaner – giving headroom for borrowing



5) Focus on Infrastructure and Private Capex – accelerating rapidly

Metric	FY14	FY25
Railways electrification	33.00%	97.00%
Road - National highway length	91,287 KM	146,150 KM
Metro operational length	248 KM (5 cities)	1,013 KM (23 cities)
No of airports	74	163
Ports turnaround time	~93 hrs	~49 hrs
Defence exports	< USD 0.2 billion/year	~USD 2.8 billion/year
Rural homes with tap water conn	32 million	153 million
Oil & Gas pipeline	~15,845 KM	~34,233 KM
Data usage/subscriber/month	61 MB	24 GB





Investment Implication: Nifty Bank Index

The Nifty Bank index is an index tracking the performance of the largest public and private sector banks in India.

It comprises of 14 banks, across the private and public domain, weighted on a free-float market capitalisation basis, inherently assigning a higher weight to larger banks in the portfolio.

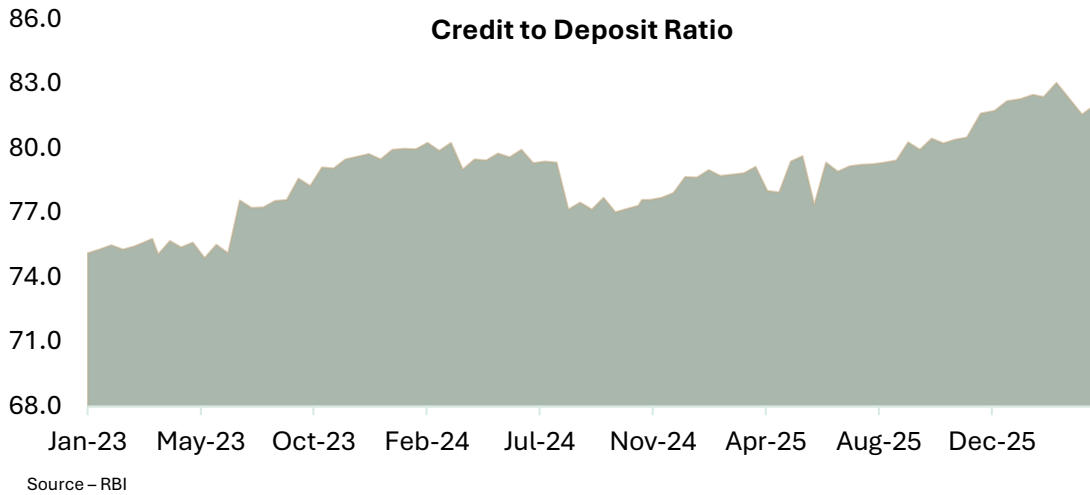
Index Constituents

Stock Name	Weight %	PE TTM	PB TTM
HDFC Bank	19.00	15.90	2.07
ICICI Bank	14.11	16.82	2.51
Axis Bank	10.01	15.03	1.85
State Bank of India	9.94	12.04	1.58
Kotak Bank	9.73	19.41	2.09
The Federal Bank	6.18	16.66	1.83
IndusInd Bank	4.80	82.70	1.13
AU Small Finance Bank	4.49	29.48	3.97
Bank Of Baroda	4.45	7.14	0.83
Canara Bank	4.06	6.66	1.04
IDFC First Bank	3.80	37.47	1.30
Punjab National Bank	3.38	6.76	0.82
Union Bank	3.09	6.47	0.95
Yes Bank	2.95	20.21	1.41

As on 31st March 2026



Risks to the thesis



- ▶ The credit-deposit (CD) ratio measures the amount lent for every rupee deposited in the bank, it currently stands at ~82% indicating that credit growth is outpacing the deposit growth.
- ▶ When the CD ratio becomes too high, banks compete for deposits to fund loans, thereby creating pressures on NIMs, and lowers the liquidity cushion.
- ▶ Increase in financialization of savings, is causing incremental savings to pool into equities over bank deposits, this continues to remain a structural risk for banks.



Conclusion – The Lending Sector Allocation

Indian banks are at an interesting juncture currently due to –

- ▶ **Valuation De-rating** – P/B below historical average
- ▶ **Fundamentals Improving** – lower NPAs
- ▶ **Stronger Bank Balance sheets** – high capital adequacy
- ▶ **Increasing infrastructure spending**, and private capex
- ▶ **Cleaner corporate balance sheets** – headroom for borrowing
- ▶ Interest Rates **peak out**

These factors make banks a good allocation with a plausible re-rating of the universe.

We view the banking sector as a tactical allocation opportunity, supported by improving fundamentals, **attractive valuations**, and **an accelerating infrastructure and capex cycle**. However, as valuations begin to re-rate and the risk-reward moderates, **we would look to rotate capital back into the primary beneficiaries of the infrastructure upcycle**, rather than participating indirectly through banks.

Our preferred exposure to the sector is through a combination of the Nifty Bank Index in the mutual fund universe. We recommend a lumpsum allocation with an 18 to 24 months investment horizon.

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