

Loan growth, costly funds to weigh on bank margins

In Q4, margins of banks, especially for mid-sized lenders, were flat or slightly lower

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Interest rate margins may remain under pressure in the first half of the current financial year, as lenders continue raising funds at high costs to match soaring loan growth. In the March quarter, margins for most banks, especially the mid-sized lenders, were flat to slightly lower.

Margins compress when banks cut loan rates in line with benchmarks, but continue paying deposit interest at assured rates until they mature. Raising rates as deposits mature could help ease some of the margin pressure, but the banks are also constrained by their need to raise deposits to support loan growth.

According to Fitch Ratings, an increased share of loans to retail, agriculture and MSME customers may help margins, as these loans are priced higher. However, this will be partly offset by a gradual shift towards secured loans which are given out at lower rates as well as lower treasury gains, the ratings company said in a note on 22 April.

"There could also be moderate downside risks if liquidity is tighter than we expect due to the RBI's efforts to contain rupee volatility," it said. ICICI Bank, Axis Bank and Bank of Maharashtra which focus on higher-yielding segments and keep funding costs in check will enjoy higher margins, Fitch added.

At India's largest private sector banks HDFC Bank and ICICI Bank, margins were 8-9 basis points (bps) lower annually, but were up 2-3 bps on quarter. The prime reason: accelerated reduction in lending rates while deposit costs remained elevated. Both banks have said that while the outlook on margins is uncertain, they are likely to be "range-bound".

Between February and December 2025, the Reserve Bank of India cut the repo rate by a total of 125 bps. Banks in India bring down interest rates in line with benchmark rates such as the repo, driving an industry-wide reduction in loan rates, even as deposit rates are raised only for fresh deposits and renewals,

Margin squeeze

Strong loan growth and high deposit costs are likely to keep bank margins under pressure despite rate cuts.

Bank	Net interest margin (%) in Q4 FY26	Q-o-q change (pp)	Y-o-y change (pp)
HDFC Bank	3.4	0	-0.1 ↓
ICICI Bank	4.3	0	-0.1 ↓
Axis Bank	3.6	0	-0.4 ↓
Union Bank	2.6	-0.1 ↓	-0.2 ↓
Indian Bank	3.2	-0.1 ↓	-0.1 ↓
Federal Bank	3.7	0.6 ↑	0.6 ↑
Kotak Bank	4.7	0.1 ↑	-0.3 ↓
IDBI Bank	4.2	0.6 ↑	-0.8 ↓
Central Bank	3.1	0.1 ↑	-0.3 ↓
IDFC First	5.9	0.2 ↑	0
UCO Bank	3	-0.1 ↓	0
Yes Bank	2.7	0.1 ↑	0.2 ↑
IndusInd Bank	3.4	-0.1 ↓	1.1 ↑
Bandhan Bank	6.2	0.2 ↑	-0.5 ↓
Punjab & Sind Bank	2.5	-0.1 ↓	-0.7 ↓
RBL Bank	4.4	-0.2 ↓	-0.5 ↓

pp: percentage points

Source: Banks' Q4 investor presentations

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which come with a lag. The higher transmission in lending rates is reflected in the fact that banks' average outstanding loan rates fell to 8.99% in March, down 7 bps on quarter and 78 bps on year. In comparison, average rates on outstanding deposits declined to 6.62%, 6 bps

hiked rates on term deposits even in April. So, there is going to be a pressure on the deposit rates. Accordingly, there are a lot of these moving parts, which give some kind of lack of clarity on margins. But there is more downward side pressure," said Anil Gupta, senior vice president and co-group head, financial sector ratings, Icria Ltd.

RBI expects policy rate to remain "low for long", signalling lower lending rates for banks amid high funding costs. While loan growth was robust in H2 FY26, it was largely led by lower-yielding secured retail, SME and corporate loans, while

higher yielding loans such as credit cards saw a slowdown. The need to mobilize deposits to match this pace of loan growth, especially in lower yielding segments, could ensure that margins remain under pressure, experts said.

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COST PRESSURE

HIGHER share of retail, small-business and agriculture loans are likely to support lenders' margins

RISING competition for deposits and rising term deposit rates continue to push up funding cost

LOAN rates fell to 8.99%, while deposit rates declined to 6.62%, reflecting transmission lag

lower on quarter and 49 bps lower on year, as per latest RBI data.

"NIMs (net interest margins) will get supported by a rise in the share of personal loans which have been growing well. But the risk is from elevated competition for deposits and deposit rate hike. Some institutions have