Overview

The Financial Stability Report (FSR) is a half-yearly publication, with contributions from all financial sector regulators. It presents the collective assessment of the Sub Committee of the Financial Stability and Development Council on current and emerging risks to the stability of the Indian financial system.

Global Macrofinancial Risks

The global economy and the financial system remain resilient despite heightened uncertainty. Normalisation of monetary policy is underway and financial conditions remain accommodative. While near-term risks have receded, vulnerabilities such as stretched asset valuations, high public debt, prolonged geopolitical conflicts and risks from emerging technologies pose threats to financial stability in the medium term. Emerging market economies (EMEs) face challenges in preserving financial stability from global spillovers and growing uncertainty regarding trade policies and logistics disruptions.

Domestic Macrofinancial Risks

Against an uncertain global backdrop, the Indian economy is exhibiting steady growth, underpinned by solid macroeconomic fundamentals and strong domestic growth drivers. The domestic financial system is demonstrating resilience, supported by healthy balance sheets of banks and non-banks, and fortified by strong capital buffers, robust earnings and improving asset quality. Vulnerabilities in the form of stretched equity valuations, pockets of stress in the microfinance and consumer credit segments and risks from external spillovers require close monitoring.

Financial Institutions: Soundness and Resilience

The soundness of scheduled commercial banks (SCBs)[1] has been bolstered by strong profitability, lower non-performing assets and adequate capital and liquidity buffers. Return on assets (RoA) and return on equity (RoE) are at decadal highs, while gross non-performing assets (GNPA) ratio has fallen to a multi-year low.

Macro stress tests, which are not forecasts and are based on adverse hypothetical scenarios, demonstrate that most SCBs have adequate capital buffers relative to the regulatory minimum even under adverse stress scenarios. Stress tests of mutual funds and clearing corporations also attest to the resilience of these segments.

The CRAR of urban co-operative banks (UCBs) has remained robust in September 2024, while that of non-banking financial companies (NBFCs) is well above the prescribed regulatory minimum. The consolidated solvency ratio of the insurance sector also remains above the minimum threshold limit.

Network analysis indicates that the total outstanding bilateral exposures between financial institutions are expanding, with SCBs holding the largest share. A simulated contagion analysis, however, shows that losses due to failure of five banks with the maximum capacity to cause contagion would not lead to failure of any additional bank.

Regulatory Initiatives and Other Developments in the Financial Sector

Global regulatory efforts remain focused on strengthening the stability of the financial system, identifying and mitigating potential vulnerabilities,

[1] Excluding Small Finance Banks.

fostering collaboration and improving adaptability. Recent initiatives have concentrated on mitigating risks arising from technological advancements, cyber security threats and third-party dependencies. Addressing vulnerabilities in non-bank financial intermediaries and cross-border payment systems remain priorities.

Domestic regulatory initiatives continue to focus on reinforcing the safety and resilience of the financial system. Efforts have been focused on strengthening the resilience of financial intermediaries and market infrastructure, with emphasis on cyber resilience, fraud prevention and customer protection.

Assessment of Systemic Risk

In the latest round of the systemic risk survey (SRS) carried out in November 2024, respondents categorised all major risk groups in the 'medium' risk category. Majority of respondents expressed confidence in domestic financial system stability and assessed geopolitical conflicts, evolution of global growth and inflation, and capital outflows/ rupee depreciation as major near-term risks. Nearly 95 per cent of the respondents perceived 'medium' to 'limited' near-term impact of global spillovers on domestic financial stability. 60 per cent of the respondents assessed better or similar prospects for the Indian banking sector over a one-year horizon.