Fresh Lending Rates of Private Banks Increase Past their Mar-20 Levels

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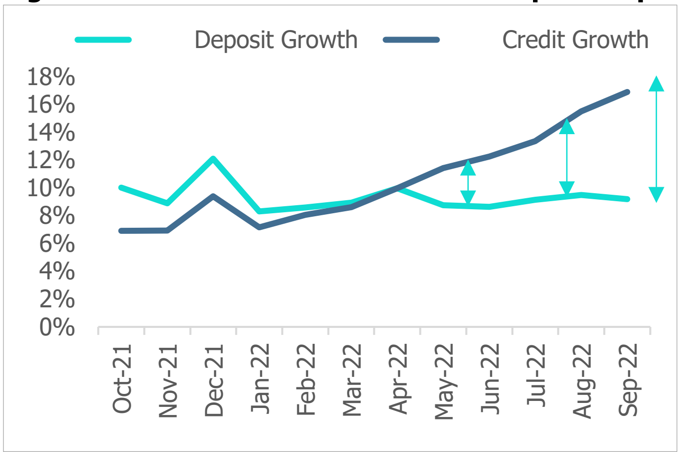
Synopsis

- Lending rates continued to grow faster compared to deposit rates.
- Private bank fresh lending rates increase past their March 2020 levels, while Public Banks are yet to reach their pre-pandemic levels.
- Private Sector Banks (PVB) and Public Sector Banks (PSB) have maintained high spreads between lending and deposit rates, with PVBs seeing higher spreads, as banks raised rates amid RBI's tightening moves.
- CareEdge expects the uptick in the deposit rate to pick up given the widening gap between credit & deposit growth and tightening liquidity conditions.

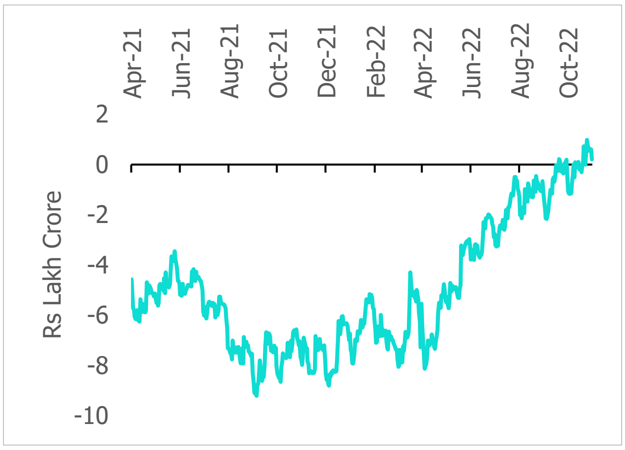
Widening Credit and Deposit Growth Gap Coupled with Lowering Liquidity Levels

Fig 1: Growth in Credit Continues to Outpace Deposit



Source: RBI

Fig 2: Banking System Liquidity Tightens



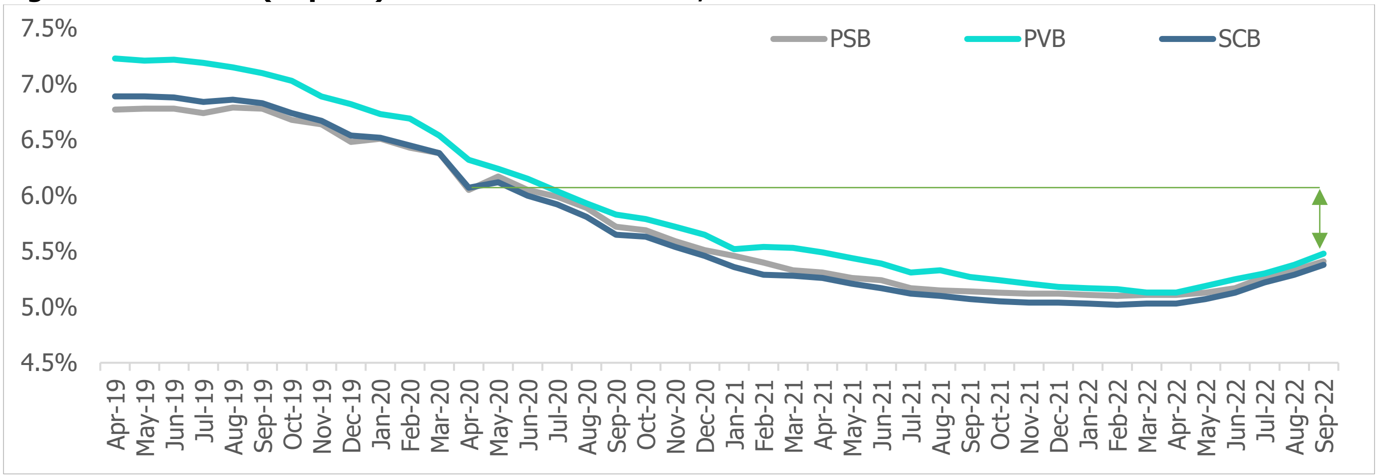
Source: RBI, CEIC

Credit demand has been recording double-digit growth driven by increased working capital requirements and demand revival. The gap between credit offtake and deposit growth is at the highest over the past 10 years (excluding the 2016 deposit growth during demonetization). Meanwhile, lower deposit mobilisation and pick-up in credit demand have pushed the credit deposit ratio to 74.2% in September 2022.

The banking system liquidity surplus has narrowed from Rs 6.3 lakh crore at the start of FY23. The liquidity conditions are expected to tighten further with a pick-up in government expenditure, strong credit growth and a higher Balance of Payment deficit. These tightening liquidity conditions have pushed the short-term interest rates higher. The weighted average call money rate has risen from 3.25% at the start of FY23 to 6.21% by end-October 2022.

Deposit Rates Anticipated to Rise Faster vs. Previous Months

Figure 3: WADTDR (Deposit) Rates Continue to Rise, Remain Below Pre-Pandemic Levels



Source: RBI

Deposit rates for PSBs, PVBs and SCBs too witnessed a rise by 8 bps, 10 bps, and 9 bps m-o-m respectively, in September 2022, however, they continue to be lower than their pre-pandemic levels (as of March 2020) by around 100 bps, indicating the distance the deposit rates have yet to traverse to reach their pre-pandemic levels, let alone move past the same.

Banks have raised lending rates in-line with an increase in repo rates over the last few months. However, an increase in deposit rates is much lower than the rise in lending yields. Banks maintain significant levels of investments in G-Secs which can be used to fund credit growth, the focus on deposits is also likely to increase going further. As competitive intensity picks up on the liability side, a sharper increase in deposit rates is anticipated, thus driving an increase in funding costs.

Lending Rate (WALR/ MCLR) to Continue Rising Reflecting the Rise in the Repo Rate

Figure 4: Evolution of WALR O/s (Lending) Loans

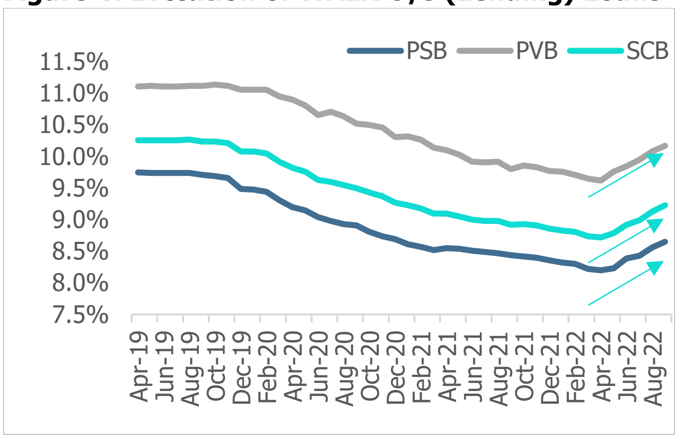
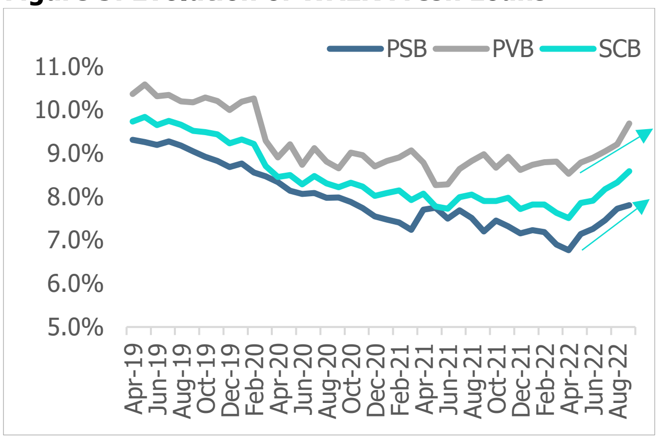
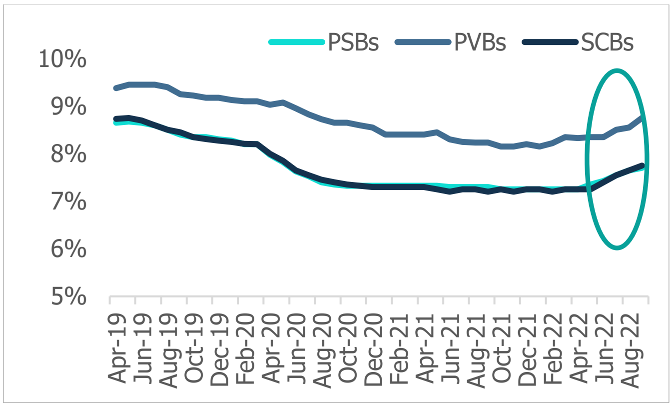


Figure 5: Evolution of WALR Fresh Loans



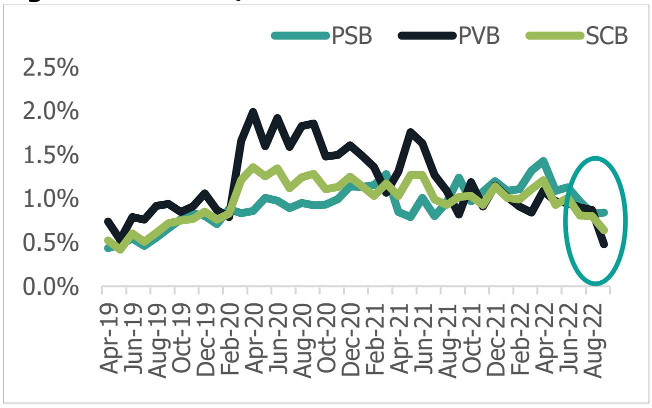
Source: RBI

Figure 6: Movement in 1-Year MCLR (Median)



Source: RBI

Figure 7: WALR o/s Loans vs WALR Fresh Loans



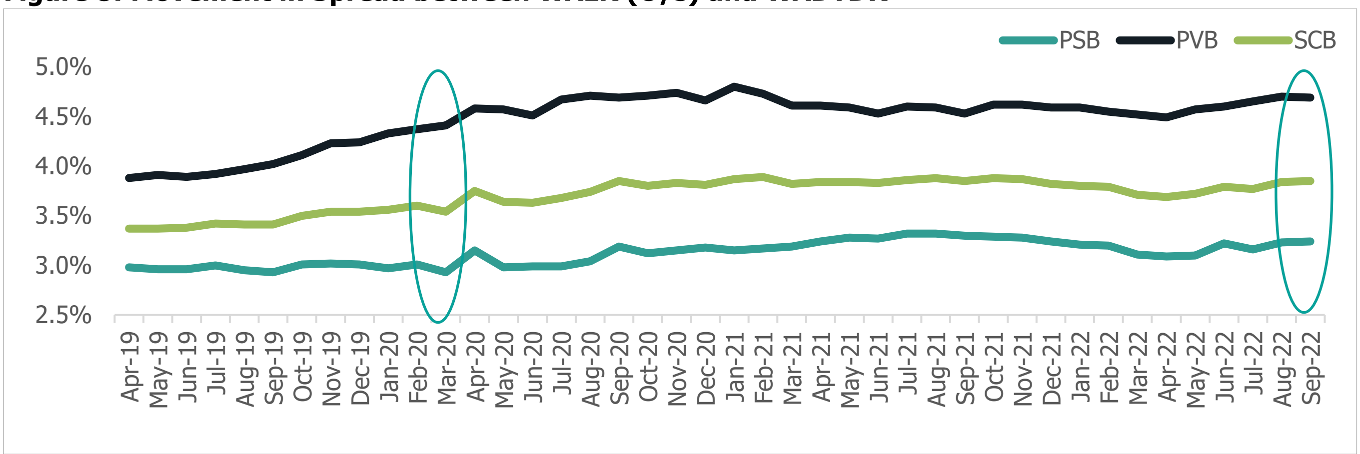
Source: RBI

Weighted Average Lending Rate (WALR) on fresh loans continues to reflect the rising interest rate cycle faster as it increased for PSBs, PVBs and SCBs by 8 bps, 48 bps, and 26 bps m-o-m, respectively. Private Bank Fresh Lending Rates Increase Past their Mar-20 levels, while Public Banks have yet to reach their pre-pandemic levels. The spread between WALR O/s loans and WALR fresh loans for PSBs and PVBs narrowed on a m-o-m, respectively, in September 2022 due to a higher rise of WALR on fresh loans as compared to WALR on O/s loans.

On a m-o-m basis given the tightening interest rate scenario, the 1-year median MCLR of SCBs increased by 15 bps from 7.75% in September 2022 to 7.90%t in October 2022 (lower than the 8.25% in March 2020).

Rate hikes and expectations for further rises have prompted banks to raise rates. The rising policy rate also has had a faster impact on the lending rate of fresh loans as new loans are being priced at newer rates, while older loans are re-priced based on repricing dates for specific loans. Consequently, the spread between WALR O/s loans and WALR fresh loans is narrowing in the near term and is expected to stabilise over the medium term.

Figure 8: Movement in Spread between WALR (O/s) and WADTDR



Source: RBI

Spread of SCBs between WALR (O/s) and WADTDR (the net interest rate spread) stood at 3.85% in September. The spread for PSBs as well as SCBs widened by 1 bps, while the PVB spread narrowed by 1bps in September 2022 due to a higher rise in lending rates as compared to deposit rates. On a y-o-y basis, PSB spread narrowed, PVB spreads rose, while the spreads of both PSB and PVBs have continued to remain elevated compared to the pre-pandemic levels. PVBs continue to maintain a higher spread given that they charge more as compared to PSBs while paying out at a similar rate.

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