Banking Rate Tracker: Interest Rates to Continue their Upward March

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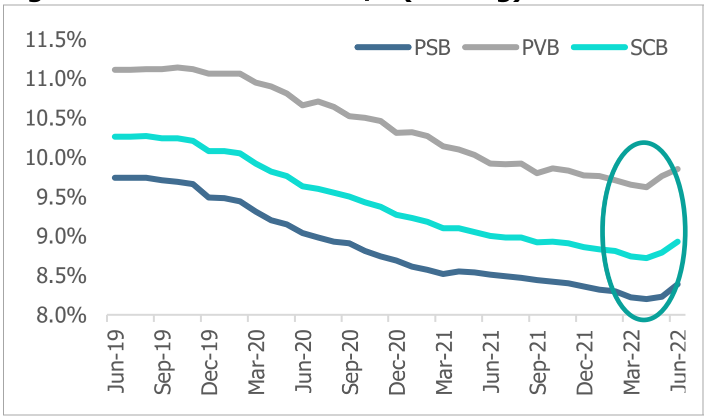
Spreads Increase, for Now

According to the published data, CareEdge has observed that in June 2022, PVBs and PSBs continue to maintain high spreads between lending and deposit rates, with PVBs seeing relatively higher spreads. Given the tightening interest rate scenario, many banks have also raised their lending and deposit rates. Lending rates on fresh loans witnessed a rise in tandem with the repo rate, however, deposit rates' rise has been slower. CareEdge anticipates that the rise in deposit rate would pick up steam given the fact that the credit growth has picked up and the liquidity is narrowing in the banking system. Further given that in today's policy meeting, RBI has raised the policy rate by 50 bps, we anticipate that the banking interest rates to continue rising in FY23.

Lending and Deposit Rates Continue Their Rise in Jun-22

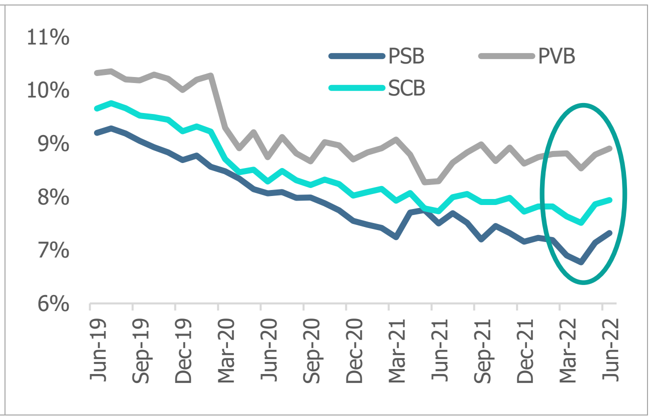
Credit offtake had shown an improving trend in the latter half of FY22, which has continued in the first four months of FY23. RBI has been working on reducing the liquidity surplus in the banking system which has been consistently reducing and is currently around the Rs 2 lakh crore mark from Rs 7 lakh crore at the beginning of 2022. Further, inflation too has been hardening for the past few months. The Russia-Ukraine conflict disrupted global supply chains, which along with high food, fuel, and commodity prices aggravated the exiting inflationary trends. Consequently, RBI increased the repo rate thrice by 40 bps to 4.40% in May 2022 and 50 bps to 4.9% in June 2022 and 50 bps to 5.4% in August and additional hikes are anticipated in the current fiscal.

Fig 1: Evolution of WALR O/s (lending) Loans



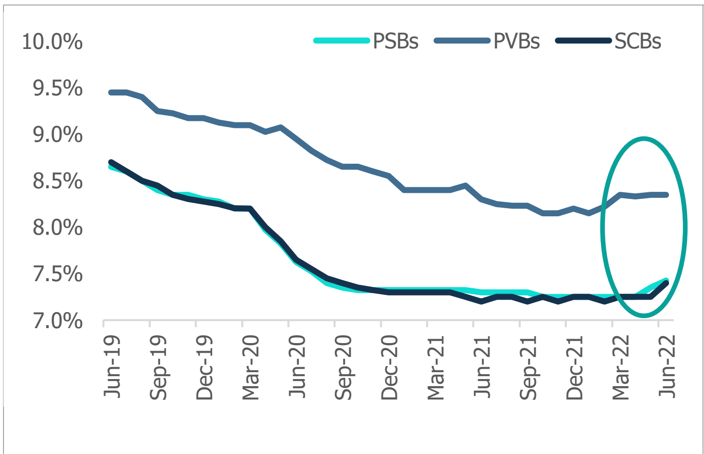
Source: RBI

Fig 2: Evolution of WALR Fresh Loans



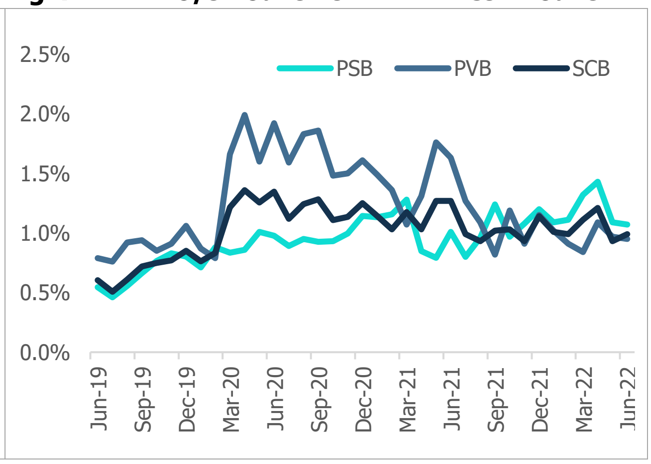
Source: RBI

Fig 3: Movement in 1 Year MCLR (Median)



Source: RBI

Fig 4: WALR o/s Loans vs WALR Fresh Loans

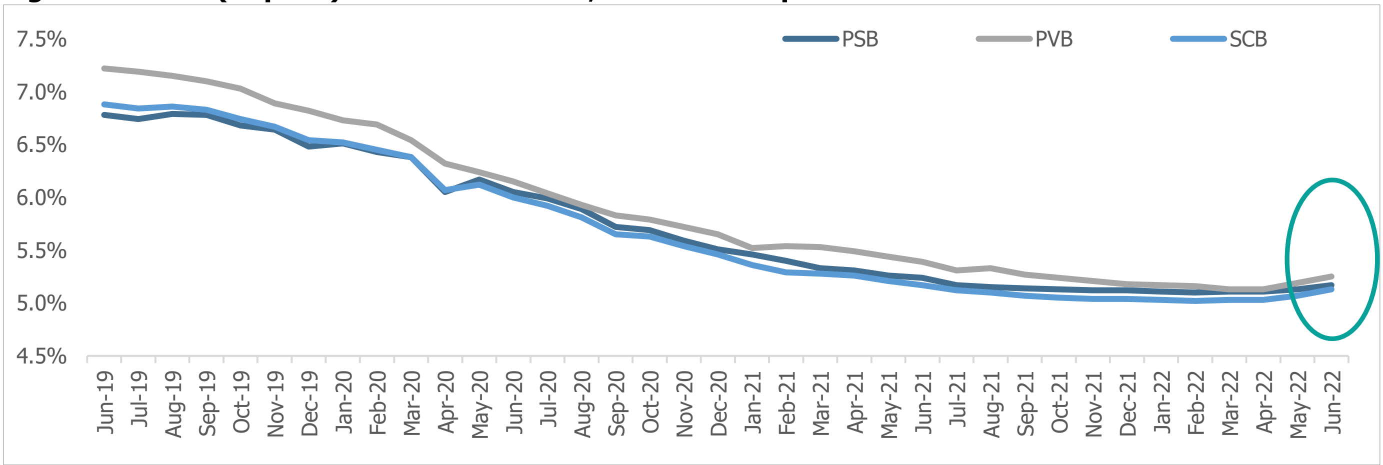


Source: RBI

- In June 2022, WALR on O/s loans for PSBs, PVBs, and SCBs increased by 16 bps, 9 bps, and 14 bps, m-o-m, respectively, passing on the policy rate hike.
- Meanwhile, WALR on fresh loans incorporated the rising interest rates faster as it increased for PSBs, PVBs and SCBs by 18 bps, 11 bps, and 8 bps m-o-m, respectively.
- The spread between WALR O/s loans and WALR fresh loans for PSBs and PVBs narrowed on a m-o-m, respectively, in June 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 median MCLR of PSBs and SCBs increased by 8 bps and 15 bps, respectively to 7.43% and 7.40%, while PVB's median MCLR remained constant at 8.35%, in June 2022.

Expectations of further policy rate hikes are also prompting certain banks to proactively raise rates. The rising policy rate 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 likely to narrow in the near term and then stabilise over the medium term.

Fig 5: WADTDR (Deposit) Rates Bottom Out, Commence Upward March

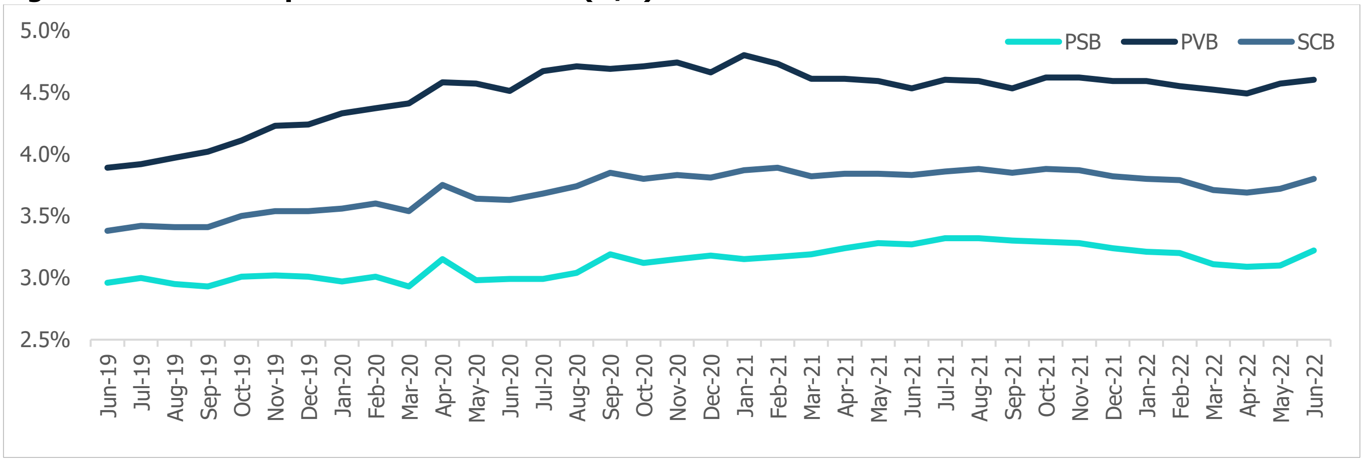


Source: RBI

- Deposit rates for PSBs, PVBs and SCBs too witnessed a rise by 4 bps, 6 bps, and 6 bps m-o-m respectively, in June 2022.

The rise in deposit rates, has been slower than the increase in repo rate. Generally, the repricing of liabilities usually happens after a lag, compared to the repricing of assets, also because fixed deposits generally do not have floating rates. Going forward, reducing liquidity and rising credit offtake are anticipated to create demand for deposits, which could prompt banks to further raise rates. Selectively, banks have already been raising rates across certain tenures and categories.

Fig 6: Movement in Spread between WALR (O/s) and WADTDR

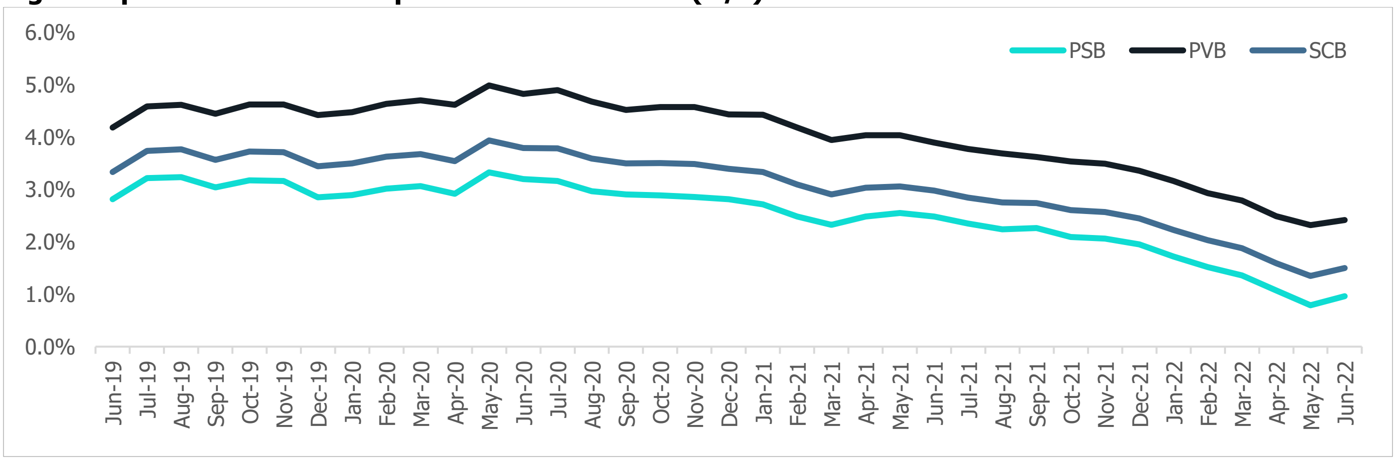


Source: RBI

- SCB's spread between WALR (O/s) and WADTDR (the net interest rate spread) stood at 3.8% in June 2022. The spread for PSBs, PVBs and SCBs increased by 12 bps, 3 bps and 8 bps m-o-m, respectively in June 2022 due to a higher rise in lending rates as compared to deposit rates.

The spread which had generally been contracting for the last 1 year, has reported a second consecutive month of increase. PVBs continue to maintain a higher spread given that they charge more as compared to PSBs, while paying out at a similar rate.

Fig 7: Blip in Contraction of Spread between WALR (O/s) and 10-Year G-Sec



Source: RBI

- The spread between the 10-year G-sec yield and the lending rates for SCBs came in at 1.5% in June 2022 rising by 15 bps m-o-m whereas PSBs and PVBs rose by 17 bps and 10 bps, respectively in the same period.

The spread has been contracting due to rising yields in the capital market. However, in June 2022, the spread increased as banks raised rates and yields moderated a bit. The elevated yields on G-sec bonds are encouraging corporate borrowers to shift borrowings to the banking system from the capital market.

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