

# Monthly Update on Banking System Interest Rates

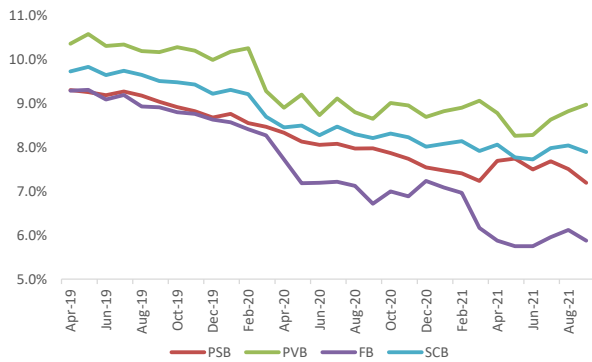
## SCB median MCLR rate rises marginally in October 2021.

November 21, 2021 | BFSI Research

### Banking interest rates have generally trended downward

The impact of Covid-19 pandemic has been rampant globally affecting the lives and livelihood negatively across the board with global economic growth being disrupted. The second wave of the pandemic which was more intense and widespread than the first was a setback for India’s fledging economic recovery. The bank credit growth has remained tepid owing to the risk aversion by both lenders and borrowers and regional lockdowns imposed by states in the earlier part of this year to curb the spread of coronavirus. However, following the relaxation in lockdown since June 2021, bank credit growth has been improving gradually. Interest rates in the banking system have generally trended lower. However, the interest rate transmission has been uneven. Furthermore, both foreign banks (FBs) and private banks (PVBs) have not passed on the policy rate cuts as aggressively as the public sector banks (PSBs).

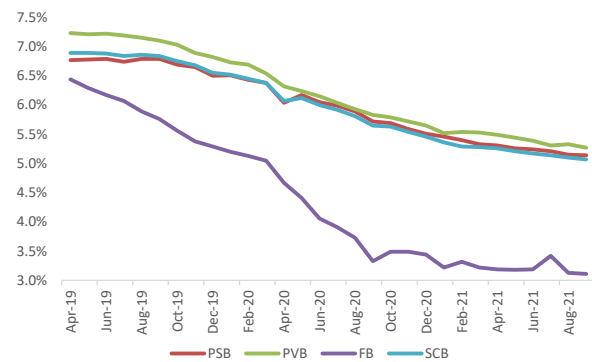
**Figure 1: WALR Fresh Loans Evolution**



Source: RBI

WALR on fresh rupee loans declined by 78 bps for PSBs, 84 bps for FBs and 32 bps for SCBs but increased by 32 bps for PVBs between September 2020 and September 2021, while the bank rate has held steady for the similar period. Decline in the WALR on outstanding loans has also continued for the same period, with the decline being 45 bps for PSBs, 72 bps for PVBs, 102 for FBs and 56 bps for SCBs. However, WALR for PVBs continues to remain higher as compared to others and has shown a somewhat rising trend in recent months.

**Figure 2: WADTDR Evolution**

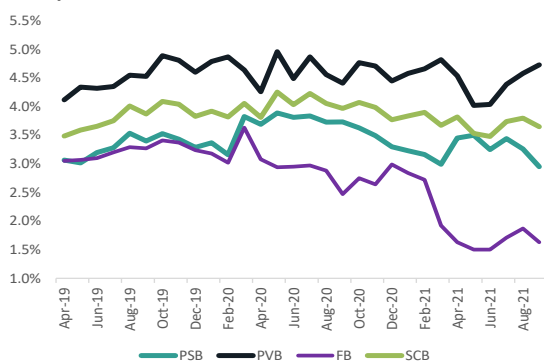


Source: RBI

As can be seen in figure 2, the WADTDR has been on a continual downtrend and has declined by 58 bps, 56 bps, 22 bps, and 58 bps for PSB, PVB, FB, and SCB, respectively, between September 2020 and September 2021, while the bank rate has held steady for the similar period. While over a two-year period, WADTDR for PVB, PSB, and SCB broadly moved in a band, while for FBs, it has fallen more significantly. However, it seems that the rates have reached a bottom.

### Movement of spread between lending rates and bank rate

**Figure 3: Movement of spread between WALR (fresh loans) and bank rate**

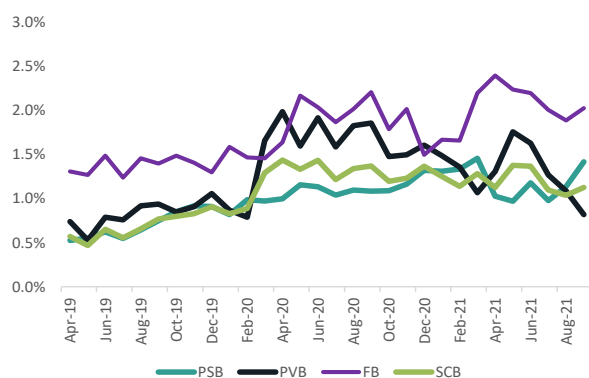


Source: RBI

WALR on fresh rupee loans declined by 78 bps for PSBs, 84 bps for FBs and 32 bps for SCBs between September 2020 and September 2021, while the WALR on fresh loans increased by 32 bps for PVBs during the same period against the bank rate which remained steady for the similar period. The data also suggests that PVBs charge the highest spread, while FBs charge the least spread.

## Movement of spread between WALR (o/s loans) and WALR (fresh loans)

**Figure 4: Movement in spread between WALR (o/s loans) and WALR (fresh loans)**

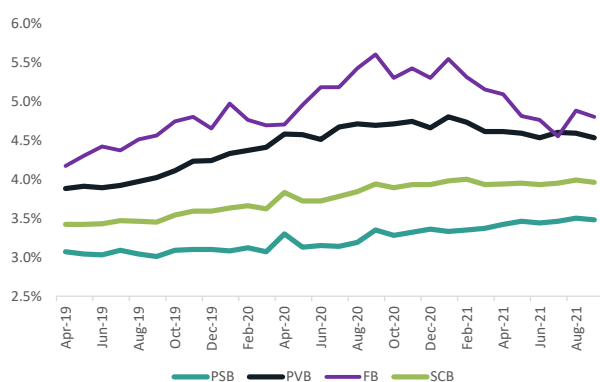


Source: RBI

The WALR for all segments has generally been on a reducing trend. In September 2021, the difference between WALR on fresh loans and WALR on outstanding loans narrowed for PVBs, while it increased for PSBs, FBs and SCBs. The average difference between the two WALRs stands at 1.2% for PSBs, 1.4% for PVBs, 2.0% for FBs and 1.2% for SCBs, for the period between September 2020 and September 2021.

## Movement in spread between lending and deposit rates

**Figure 5: Movement in spread between WALR and WADTDR**



Note: Difference between Outstanding Rupee Term Deposits and Outstanding Rupee Loans

Source: RBI, Scheduled Commercial Banks (SCBs) (All Banks)

The net interest rate spread is the difference between the average lending rate and the deposit rate. The net interest rate spread is a key determinant of a financial institution's profitability. The lending rates of FBs are generally lower than the PVBs and the PSBs; the spread for these banks is higher as FBs pay even lower rates to deposit holders when compared with PSBs and PVBs. The spread between the Weighted Average Lending Rates (WALR) on outstanding loans and Weighted Average Domestic Term Deposit Rates (WADTDR) on outstanding term deposits has been the highest for FBs, followed by PVBs, while PSBs have had the least spread. Both PSBs and PVBs pay deposit holders at similar rates, however, PVBs charge a higher WALR resulting in larger spreads. WADTDR on outstanding term deposits declined by 58 bps for PSBs, 56 bps for PVBs, 22 bps for FBs and 58 bps for SCBs between September 2020 and September 2021.

**Figure 6: Spreads at various points of time**

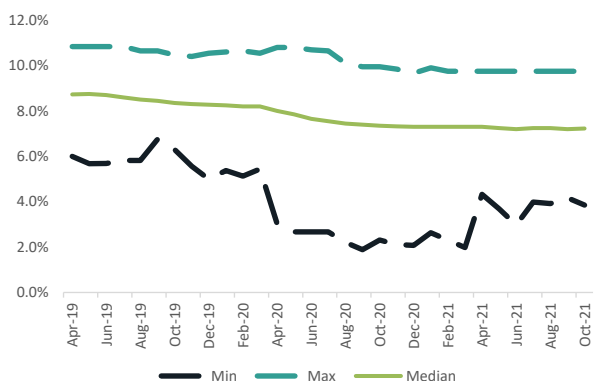
Spread between	Sep-20			Mar-21			Jun-21			Sep-21		
	PSB	PVB	SCB	PSB	PVB	SCB	PSB	PVB	SCB	PSB	PVB	SCB
WALR O/s and WADTDR	3.4%	4.7%	3.9%	3.4%	4.6%	3.9%	3.4%	4.5%	3.9%	3.5%	4.5%	4.0%
WALR O/s and Bank Rate	4.8%	6.3%	5.3%	4.5%	5.9%	5.0%	4.4%	5.7%	4.9%	4.4%	5.6%	4.8%
WALR Fresh and Bank Rate	3.7%	4.4%	4.0%	3.0%	4.8%	3.7%	3.3%	4.0%	3.5%	3.0%	4.7%	3.7%
WALR (o/s loans) and WALR (fresh loans)	1.1%	1.9%	1.4%	1.5%	1.1%	1.3%	1.2%	1.6%	1.4%	1.4%	0.8%	1.1%

Source: RBI, Scheduled Commercial Banks (SCBs) (All Banks)

If we study the NIMs of both PVBs and PSBs, we can see that both the groups have higher NIMs indicative that either the interest income has grown at a faster pace than the interest expense or that the interest income has fallen at a slower level than the interest expense. This is in line with the earlier charts where it can be observed that the interest rate cuts on the depositors have been sharper as compared to the rate cuts on the borrowers. Further the growth of NII has been higher in PVBs as compared to PSBs, indicative of the fact that PVBs have higher spreads vs. PSBs (evinced in Figure 6). Even though provisions have generally witnessed a fall in Q2FY22, higher NIMs are sometimes required to cover higher NPAs especially in PSBs. Any improvement in the WALR fresh loans spread over median MCLR and WALR O/s loans spread over WADTDR, would indicate an expansion in retail lending spreads and consequently any reduction in spreads would indicate pressure on NIMs.

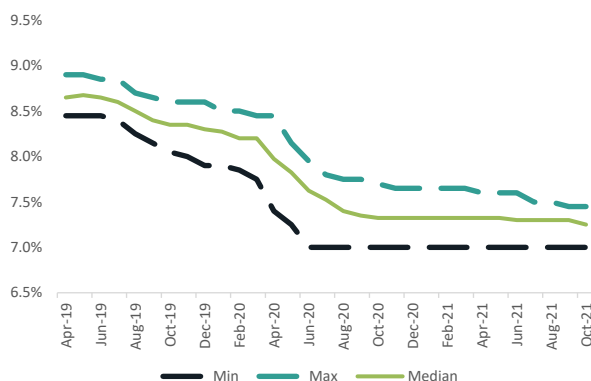
**Movement in Bank Group-wise MCLR (1 Year): PVB corridor continue to travel in a similar corridor, while PSB rates continue to travel in the narrowest corridor. Foreign Banks maintain the highest variation. SCB median rate rose marginally in October 2021.**

**Figure 7: Movement in 1 Year MCLR: Scheduled Commercial Banks**



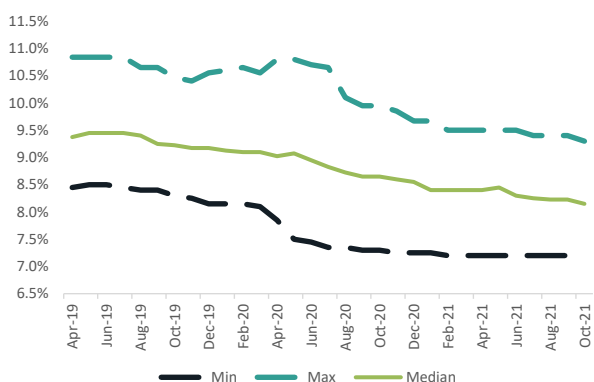
Source: RBI

**Figure 8: Movement in 1 Year MCLR: Public Sector Banks**



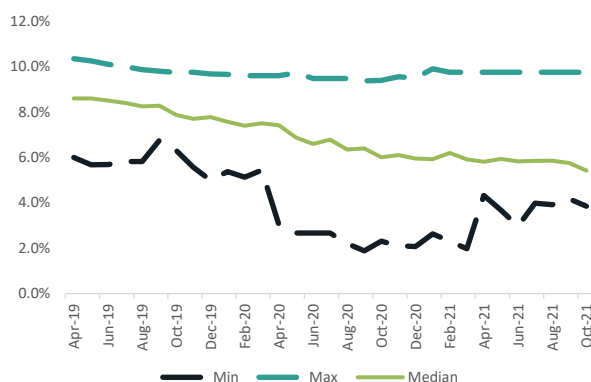
Source: RBI

**Figure 9: Movement in 1 Year MCLR: Private Sector Banks**



Source: RBI

**Figure 10: Movement in 1 Year MCLR: Foreign Banks**



Source: RBI

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