

Banking Interest Rates: PSB Term Deposit Rates bottom out

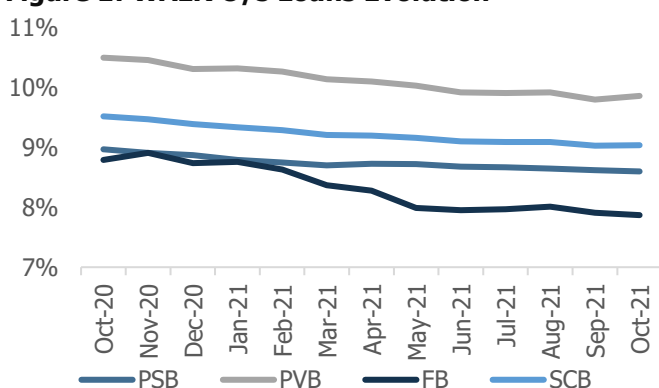
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Banking interest rates have generally trended downward

The impact of Covid-19 pandemic has affected lives and livelihood negatively across the board with global economic growth being disrupted. Consequently, the bank credit growth was tepid, 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) and the overall scheduled commercial banks (SCBs).

Movement in lending rates (Weighted Average Lending Rate - WALR)

Figure 1: WALR O/s Loans Evolution



Interest rate transmission continued between October 2020 and October 2021 as WALR on outstanding loans continued, while the bank rate has held steady for the similar period. The figure 2 below captures the quantum of this change. On a m-o-m basis, PSBs and PVBs have followed contrasting pathways in October 2021 wherein WALR (on O/s loans) of PSBs declined by 2 bps, while of PVBs increased by 6 bps.

Source: RBI

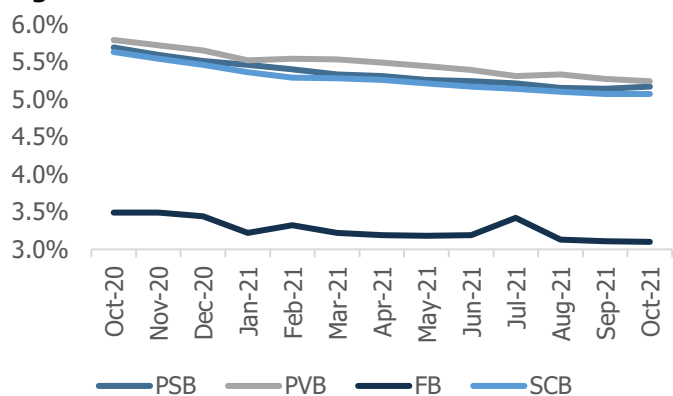
Figure 2: Decline in WALR over the last 12 months (October 2020 to October 2021)

	Outstanding loans
PSBs	37 bps
PVBs	64 bps
FBs	92 bps
SCBs	48 bps

For SCBs, the difference between the median MCLR and WALR o/s loans has generally been on a declining trend. If we study the spread between the 10-year Gsec yield and the lending rates, PVBs have a higher spread compared to PSBs. WALR for PVBs continues to remain higher as compared to others. Further, with a reduction in WADTDR indicates increase in spreads.

Movement in deposit rates Weighted Average Domestic Term Deposit Rates (WADTDR)

Figure 3: WADTDR Evolution

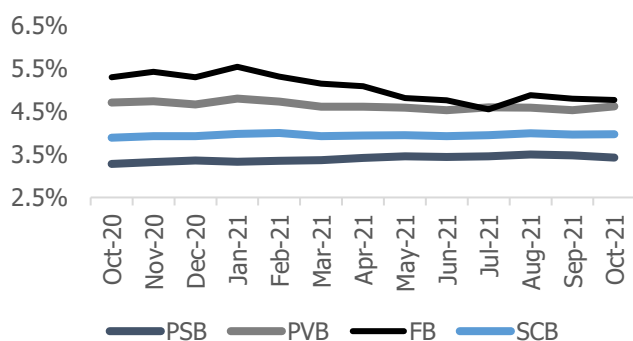


Source: RBI

As can be seen in figure 4, the WADTDR has been on a continual downtrend and has declined by 52 bps, 55 bps, 39 bps, and 56 bps for PSB, PVB, FB, and SCB, respectively, between October 2020 and October 2021, while the bank rate has held steady for the similar period. However, it seems that the rates have reached a bottom as the PSB rates increased on a m-o-m basis by 3 bps, while SCB rates held steady and PVB and FB rates increased by 3 bps and 1 bps, respectively. Further the rates for FBs continue to be significantly lower than the other categories.

Movement in spread between lending and deposit rates

Figure 4: 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 WALR on outstanding loans and 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. The spread between O/s loan lending rate over WADTDR has remained generally unchanged on a m-o-m basis.

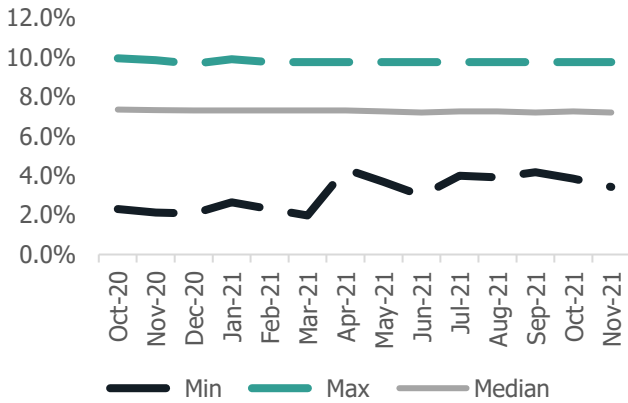
Concluding remarks

If we study the spreads of both PVBs and PSBs, we can see that both the groups have high spreads with PVBs continuing to have relatively higher spreads. However, there are early signs that the term deposit rates have bottomed out and may rise. Consequently, WALR may also witness some pressure as any decrease in the WALR O/s loans spread over WADTDR, would indicate pressure on NIMs and any improvement in spreads would indicate an expansion in the retail lending spreads.

Annexure

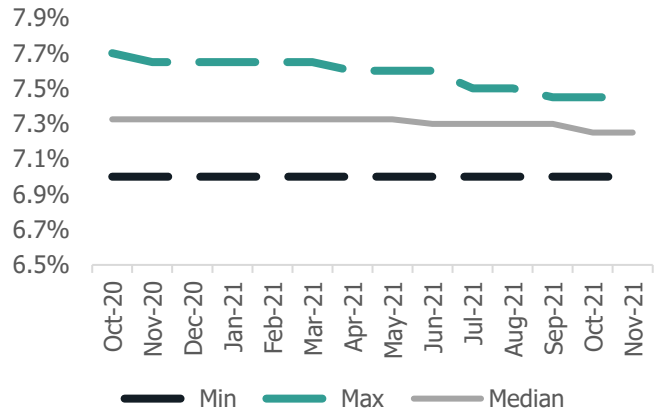
Movement in Bank Group-wise MCLR (1 Year): PVB continue to travel in a similar corridor, while PSB rates continue to travel in the narrowest corridor. Foreign Banks maintain the highest variation.

Figure 5: Movement in 1 Year MCLR: Scheduled Commercial Banks



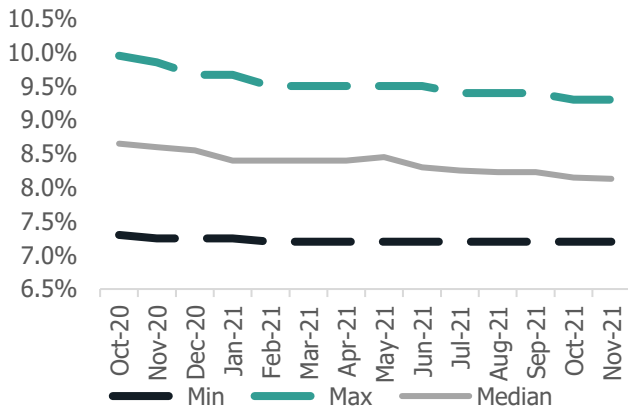
Source: RBI

Figure 6: Movement in 1 Year MCLR: Public Sector Banks



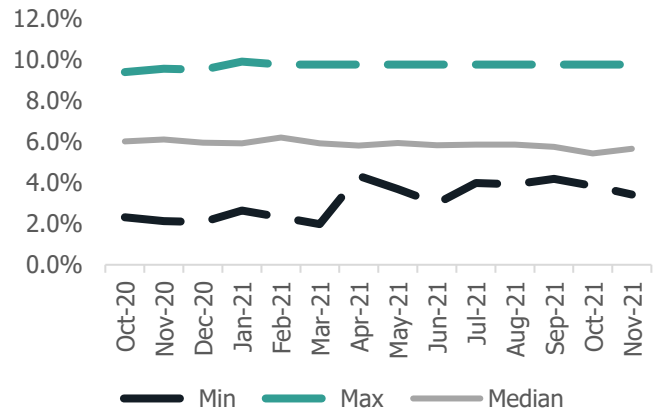
Source: RBI

Figure 7: Movement in 1 Year MCLR: Private Sector Banks



Source: RBI

Figure 8: Movement in 1 Year MCLR: Foreign Banks



Source: RBI

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