O/s PSB Spreads Hit 10-year Low, Fresh Spreads See Divergence

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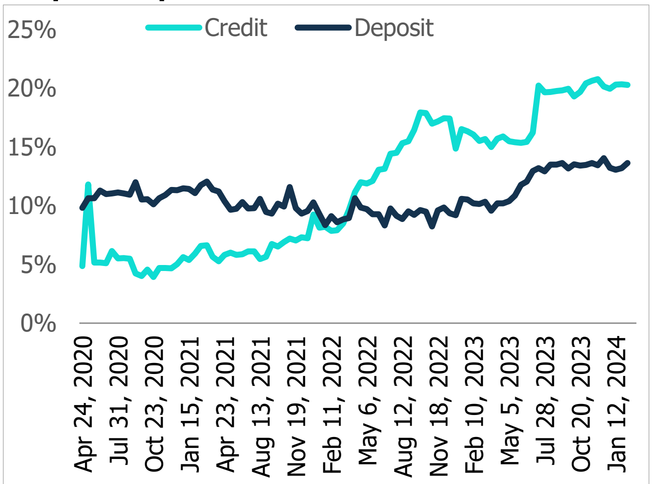
Overview

- In January 2024, the spread of SCBs between weighted average lending rate (WALR) and weighted average domestic term deposit rate (WADTDR) (the net interest rate spread) stood at 3.02% and 2.98% for Fresh and Outstanding rates, respectively in January 2024. Meanwhile, o/s spreads of PSBs hit a 10-year low at 2.34%, while PVBs continue to maintain a higher spread as compared to PSBs.
    - The WALR on outstanding rupee loans of scheduled commercial banks (SCBs) increased by 2 bps sequentially to 9.83%, while WADTDR on o/s rupee term deposits increased by 2 bps to 6.83% in January 2024. Meanwhile, the one-year median Marginal Cost of fund-based Lending Rate (MCLR) of SCBs remained flat m-o-m and stood at 8.80% as of February 2024.
    - The WALR on fresh rupee loans of SCBs increased sequentially by 13 basis points (bps) to 9.45% in January 2024, while WADTDR (Fresh) of SCBs decreased by 6 bps to 6.43% in January 2024.

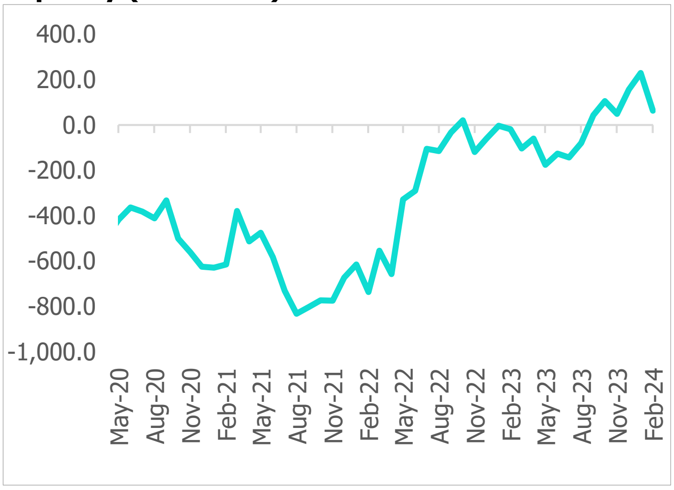
Large Gap Between Credit and Deposit Growth Persists, while Liquidity Remains in Deficit

Fig 1: Credit Growth Continues to Outpace Deposit



Source: CMIE, RBI; Note: Data post HDFC Merger in July

Fig 2: Bank System Monthly Liquidity (Rs lakh cr)



Source: RBI, CMIE

Credit offtake increased by 20.3% y-o-y for the fortnight ended February 9, 2024. It is important to note that the y-o-y figures are not directly comparable, as the data reported by the RBI as of February 9, 2024, includes the impact of the merger of HDFC with HDFC Bank. However, excluding merger growth stood at 16.3 %. The outlook for bank credit offtake remains positive for FY24, supported by factors such as economic expansion and a continued push for retail credit which has been supported by improving digitalisation. Deposits rose at 13.6% y-o-y for the fortnight (reported February 09, 2024) and without considering the merger, growth was 13.0%. Meanwhile, deposit growth is expected to improve compared to earlier periods as banks look to shore up their liability franchise and ensure that deposit growth does not constrain the credit offtake. Meanwhile, even as the liquidity continues to remain in deficit, RBI has been conducting both VRR & VRRR auctions to manage liquidity, in line with its accommodation withdrawal stance while also meeting the credit needs of the economy. (Refer to February Economic Pathway 2024).

Spread Compression Continues for o/s PSBs; However Fresh Spreads Rise

Figure 3: Evolution of Spreads (Outstanding)

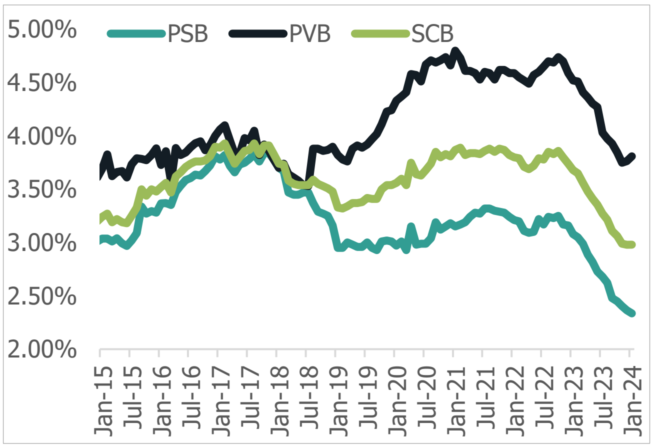
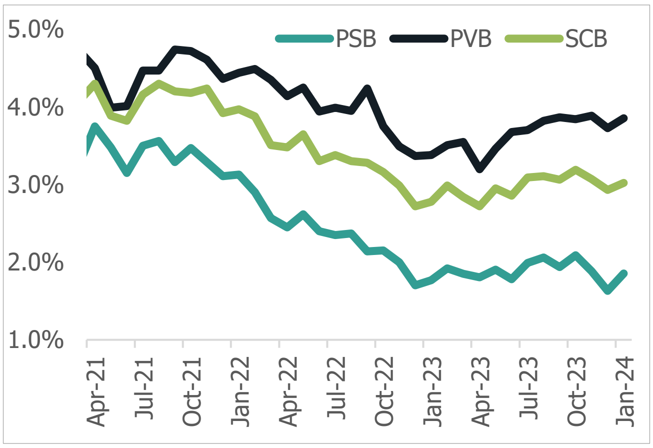


Figure 4: Evolution of Spreads (Fresh)



Source: RBI; Note: Data post HDFC Merger in July

The spread of SCBs between WALR and WADTDR (the net interest rate spread) stood at 2.98% and 3.02% for outstanding and fresh rates respectively in January 2024. We witnessed a divergence in spread trend wherein Fresh increased by 19 bps, however, o/s spreads remained flat.

- The o/s PSB spreads have been compressing over the last year touching lows post Covid and reaching 2.34% (10-year low),
- However, PVBs o/s spread saw a divergence in trend and increased by 5 bps and reached at 3.81%

The fresh SCBs spreads y-o-y increased by 19 bps, however, PSBs saw an increase of 22 bps and stood at 3.02% and 1.85% respectively. PVBs continue to maintain a higher spread given that they charge more as compared to PSBs and stand at 3.85%. The spread between outstanding WALR and WADTDR continues to be lower than the spread between fresh WALR and WADTDR.

Outstanding Business: Deposit and Lending Rates Rise

Fig 5: Evolution of WALR O/s (Lending) Rate

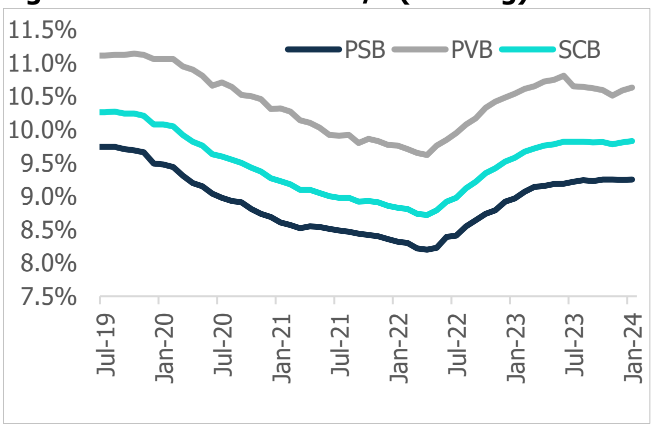
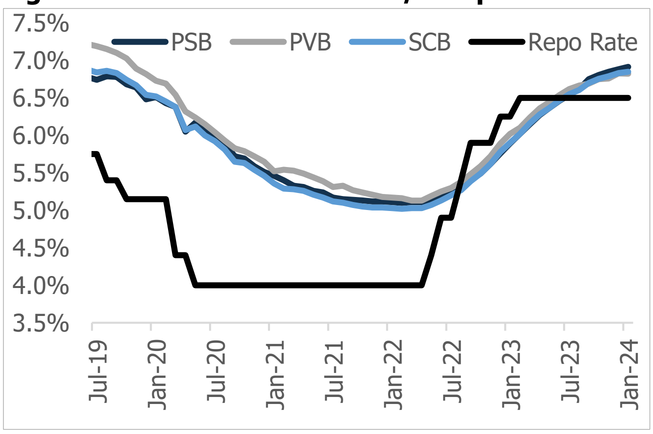


Fig 6: Evolution of WADTDR O/s Deposit Rate



Source: RBI, Note: Data post HDFC Merger in July

WALR on outstanding rates increased by 2 bps on m-o-m basis and stood at 9.83% for SCBs. PSBs remained flat at 9.25%, whereas PVBs saw an increase of 4 bps. One of the reasons for the current slower trajectory of the PVB rates over the last few months has been the merger between HDFC and HDFC Bank where housing finance assets have impacted the lending rates. If this impact is ignored, then the rates would have been higher by 2 bps for SCBs and 3 bps for PVBs. O/s lending rates have been moving below pre-pandemic for the last few months. Meanwhile, outstanding deposit rates saw a m-o-m uptick by 3 bps and 2 bps for PSBs and SCBs respectively. Whereas PVBs saw a marginal decline of 1 bps O/s WADTDR continue to remain above their pre-pandemic levels (compared with March 2020).

Fig 7: Movement in 1-Year MCLR (Median)

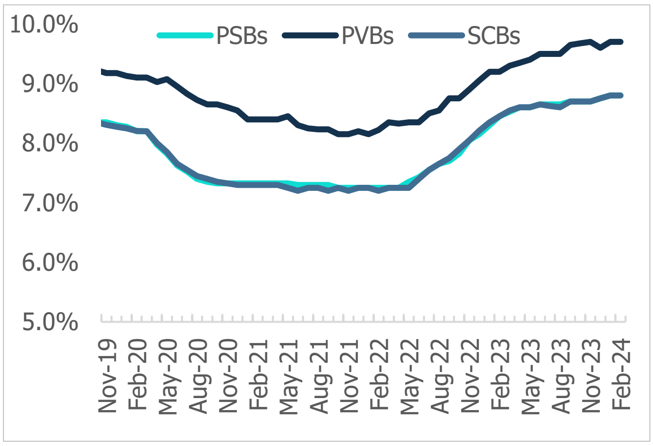
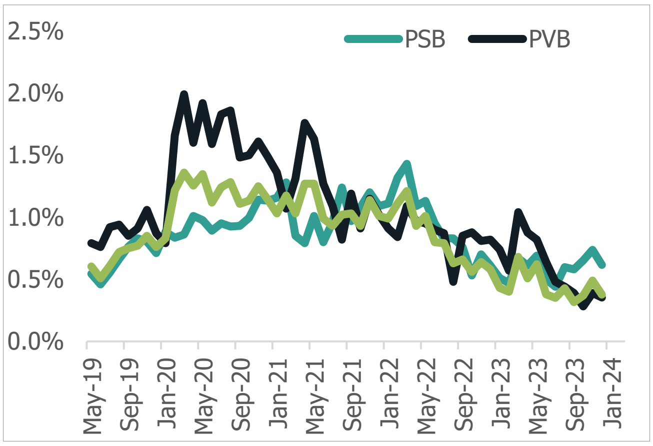


Fig 8: WALR o/s vs WALR Fresh



sSource: RBI, Note: Data post HDFC Merger in July

Fig 9: MCLR Rates (in %) Remained Broadly Flat on a m-o-m basis

Banks	Feb-23	Mar-23	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	Nov-23	Dec-23	Jan-24	Feb-24	YoY
	Public Sector Banks													
BoB	8.55	8.55	8.6	8.6	8.65	8.65	8.65	8.70	8.70	8.75	8.75	8.80	8.80	0.25
BoI	8.40	8.50	8.6	8.6	8.65	8.65	8.7	8.70	8.70	8.75	8.80	8.80	8.80	0.4
BoM	8.40	8.40	8.5	8.5	8.5	8.5	8.60	8.60	8.70	8.70	8.70	8.70	8.80	0.4
Canara	8.50	8.60	8.65	8.65	8.65	8.65	8.70	8.70	8.70	8.75	8.75	8.80	8.85	0.35
CBI	8.15	8.45	8.45	8.45	8.6	8.6	8.60	8.60	8.65	8.70	8.70	8.70	8.75	0.6
Indian	8.45	8.55	8.6	8.6	8.65	8.65	8.65	8.70	8.70	8.75	8.75	8.80	8.85	0.4
IOB	8.45	8.60	8.6	8.65	8.65	8.65	8.70	8.70	8.70	8.70	8.75	8.80	8.80	0.35
PSB	8.50	8.60	8.65	8.65	8.65	8.70	8.90	8.90	8.90	8.95	8.95	8.95	8.95	0.45
PNB	8.40	8.50	8.5	8.5	8.6	8.60	8.60	8.65	8.65	8.65	8.65	8.70	8.80	0.4
SBI	8.50	8.50	8.5	8.5	8.5	8.55	8.55	8.55	8.55	8.55	8.65	8.65	8.65	0.15
UCO	8.35	8.50	8.6	8.6	8.65	8.65	8.65	8.70	8.70	8.70	8.75	8.75	8.80	0.45
UBI	8.65	8.65	8.65	8.65	8.65	8.65	8.65	8.70	8.70	8.70	8.80	8.80	8.90	0.25
	Private Sector Banks													
HDFC	8.90	8.95	8.95	9.05	9.05	9.05	9.10	9.15	9.20	9.20	9.20	9.20	9.30	0.4
ICICI.	8.65	8.75	8.75	8.75	8.85	8.85	8.90	8.95	8.95	9.00	9.00	9.00	9.10	0.45
Axis	8.90	8.95	8.95	9.10	9.10	9.1	9.15	9.15	9.15	9.20	9.25	9.25	9.30	0.4
IndusInd	10.05	10.15	10.20	10.20	10.20	10.25	10.25	10.30	10.30	10.35	10.25	10.25	10.40	0.35
Kotak	9.00	9.05	9.10	9.20	9.20	9.25	9.30	9.30	9.35	9.35	9.35	9.35	9.45	0.45
Yes.	9.90	10.10	10.15	10.00	10.05	10.15	10.15	10.25	10.25	10.40	10.50	10.50	10.50	0.6

Source: RBI, Note: Data post HDFC Merger in July

On a m-o-m basis in February 2024, 1-Year median MCLR of PVBs and SCBs increased by 7 bps and 5 bps respectively, while PSBs remained flat. Meanwhile when we compare pre-pandemic levels, MCLR median for SCBs is above 50 bps (compared with March 20), whereas we saw a divergence in trend, o/s WALR dropped by 8 bps since a large part of the lending has moved to external benchmark linked rates.

Fresh Rates Remain Volatile, Lending sees a Sequential Drop, whereas Deposit Increases Marginally

Fig 10: Evolution of WALR Fresh Loans

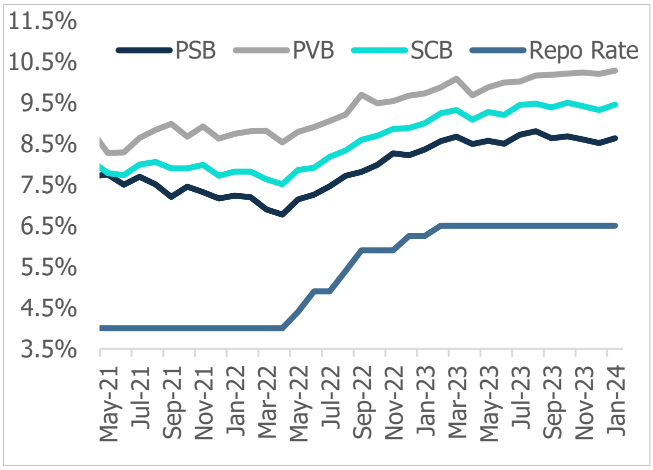
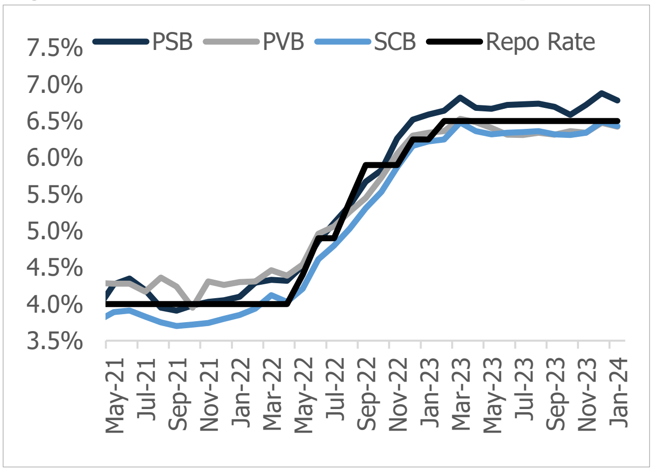


Fig 11: Evolution of WADTDR Fresh Deposits



Source: RBI, Note: Data post HDFC Merger in July

WALR on fresh loans on m-o-m basis saw an increase across bank types wherein PVBs and SCBs increased by 12 and 13 bps respectively, whereas PVBs grew by 8 bps. On the other hand, fresh deposit rates saw a downtick m-o-m across bank types by 10 bps, 5 bps and 6 bps for PSBs, PVBs and SCBs, respectively in January 2024. When compared to April 2022, (prior to commencing of rate hikes in May 2022) repo rate increased by 250 bps to 6.5% as of January 2024, Fresh WALR and WADTDR have increased by 194 bps and 240 bps to 9.45% and 6.43% as of January 2024 from April 2022. Meanwhile, the Short-term Weighted Average Call Rate (WACR) stood at 6.71% as of February 16, 2024, compared to 6.36% on February 17, 2023, due to liquidity and pressure on short-term rates.

Conclusion

In January 2024, there has been pressure on o/s spreads due to growing competition amongst banks. However fresh spreads have broadly increased., Spreads between the outstanding WALR and WADTDR have been hovering below pre-pandemic levels since June 2023, which is exerting pressure on NIMs. Notably, the spread between the outstanding lending and deposit rates has narrowed compared to the spread between the fresh lending and deposit rates.

Furthermore, with RBI turning the heat on unsecured lending products leading to banks turning cautious on high-yield products such as unsecured personal loans, lending rates could also witness some pressure. Further, with yields on capital market offerings remaining elevated, interest rates on deposits are likely to increase in the current period. Additionally, as the Credit to Deposit ratio remains elevated, growth in the liability franchise would play a significant role in sustaining loan growth. The competition for deposits is likely to remain intense resulting in a rise in funding costs in the coming periods as CASA share remains under pressure.

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