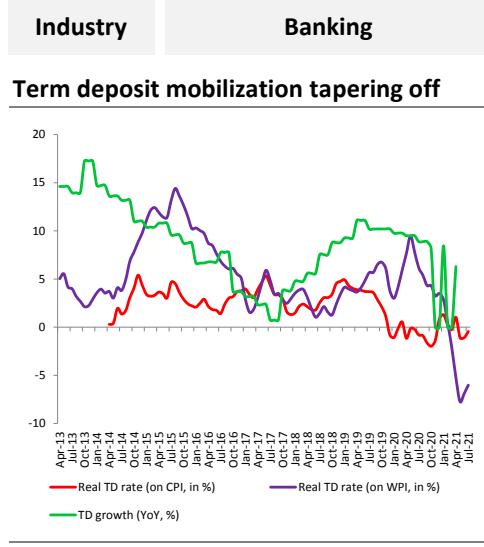


03 September 2021

SECTOR UPDATE



Banking

Private banks' spread performance improves in July'21

During July'21, the banking system's fresh loan lending rate witnessed an uptick while the weighted average term deposit rate (WATDR) declined. Banks' outstanding loans lending rate remained stable. The sectoral credit deployment data for the month indicates some building-up of credit risk by banks - reflected in the rise in fresh loan lending rates on a MoM basis especially for private banks (PVBs). Our estimation of spreads on various benchmarks reveals that PVBs performed better than public sector banks (PSBs) despite having a higher proportion of loans linked to the EBLR (external benchmark linked lending rate).

PVBs fresh loan WALR rises, resulting in an expansion in spreads over median MCLR; credit risk build-up has begun

PVBs witnessed a sharp uptick in their fresh loan weighted average lending rates (WALR) in July'21 after a contraction in 1QFY22. Incremental credit deployment during the month suggests that the banking system has started building in some credit risk & high-yielding loans, leading to a rise in fresh loans WALR. PSBs witnessed a marginal rise in their lending rates. Based on our hypothesis, PVBs gained the majority of incremental credit market share in commercial real estate (CRE), NBFCs, other personal credit and credit card receivables in July'21, leading to a sharp rise in their fresh loan WALR. PVBs' spreads over median MCLR also expanded to 39bps in July'21 from -1bps in June'21 & -18bps in May'21.

PVBs arrest a further slide in spreads over market yields

During the month, PVBs & PSBs lending rates (O/s loans WALR) remained stagnant at 9.91% & 8.67% MoM, respectively. PVBs' lending rate spreads over the 1-year AAA PSU paper yield remained stagnant at 545bps MoM and improved marginally to 620bps over the India Government 1-year generic bid yield. Overall, in the last 9 years, PVBs' spreads over these two market linked benchmarks remained much above the average spread levels of 393bps & 471bps, respectively.

Real Term deposit rate remains negative; term deposit mobilization tapers off in June'21

Scheduled Commercial Banks' (SCBs) term deposit (TD) rate was at an all-time low of 514bps in the last eight years. Real TD was -109bps during April'21-June'21 and at -45bps in July'21. TD mobilization slackened to 6.3% YoY & 1.2% QoQ in June'21 (from 8.5% YoY & 2.2% QoQ in March'21 and 9.5% YoY & 3.2% QoQ in June'20).

PVBs O/s loans WALR spread over the TD rate improved marginally to 460bps (from 453bps in June'21); it has remained in a similar range in the last 5-6 months. During the month, the spread remained stable for PSBs.

EBLR regime facilitates interest rate transmission

Over the last year (July'20-July'21), PVBs' WATDR, MCLR and WALR fell by 73bps, 57bps and 80bps, respectively. But during July'19-July'20, their WATDR, MCLR & WALR had contracted by 115bps, 63bps and 40bps, respectively (significantly lower interest rate transmission). Therefore, the EBLR regime has facilitated a better interest rate transmission.

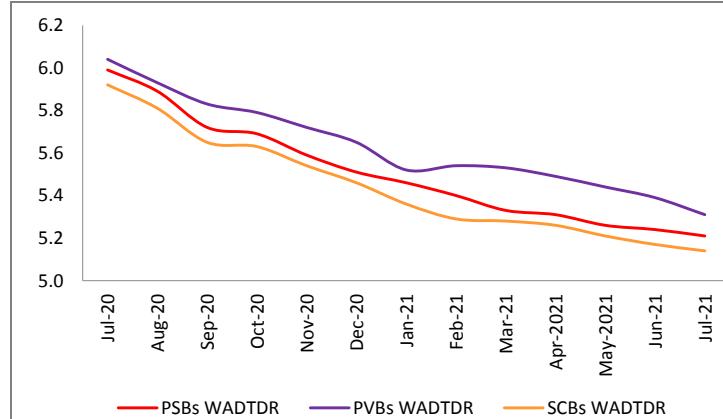
Even in the absence of a sharp contraction in MCLR (merely by 57bps on YoY), WALR contracted 80bps on a YoY basis due to the pricing of loans on the external benchmark, repo policy rates. As a result, PVBs are witnessing spread/margin compression.

While a significant portion of PVBs' mandated loans is on the EBLR [Click here](#), O/s loans WALR spreads over median MCLR (at 166bps in July'21) remain close to the 6-years mean & median spread of 172bps. On the other hand, PSBs' spreads (the difference between O/s loan WALR & median MCLR) remained stable at 137bps MoM and almost similar to the 1QFY22 spread at 139bps. PVBs' spread performance was better than PSBs during July'21.

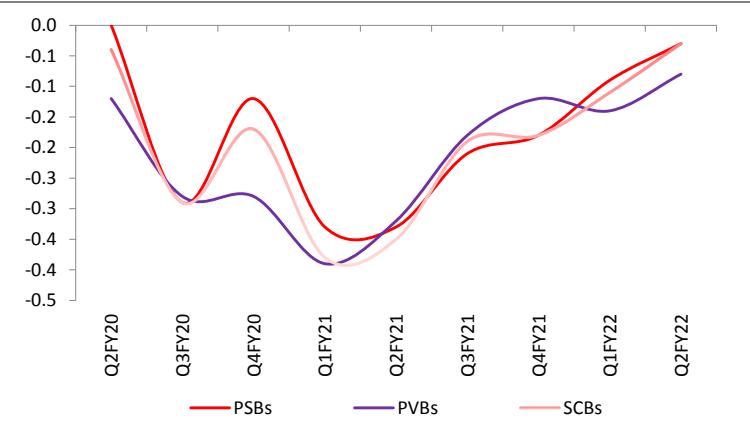
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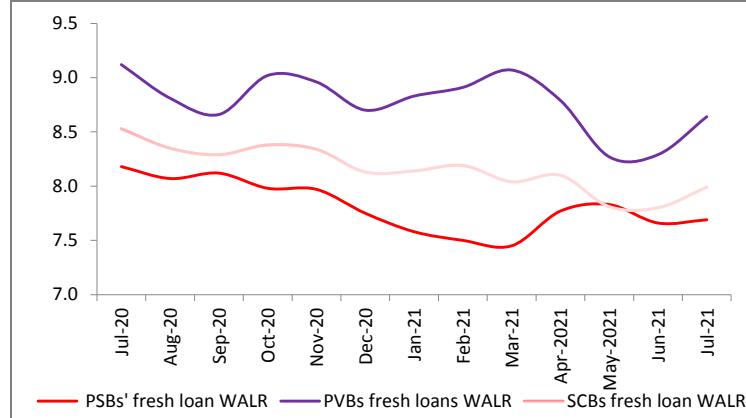
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Exhibit 1: Banks' WADTDR trajectory

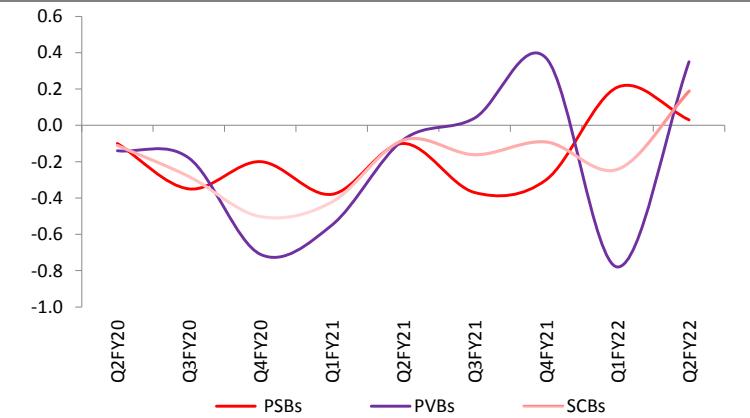
Source: Systematix Institutional Research

Exhibit 2: Quarterly changes in WADTDR

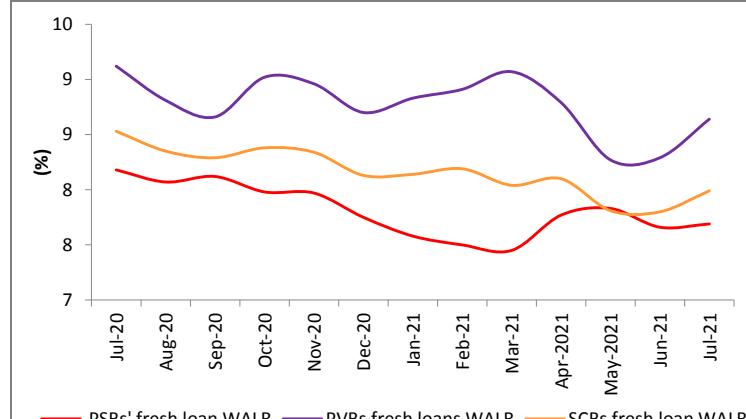
Source: Systematix Institutional Research

Exhibit 3: Banks' fresh loans WALR trajectory

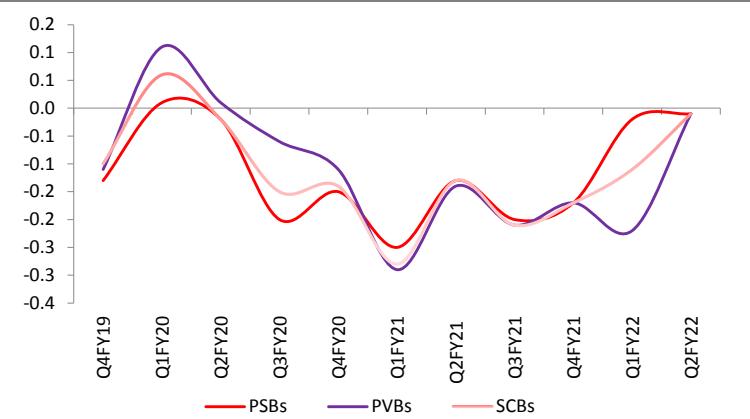
Source: Systematix Institutional Research

Exhibit 4: Quarterly changes in fresh loans WALR

Source: Systematix Institutional Research

Exhibit 5: Banks' outstanding loans WALR trajectory

Source: Systematix Institutional Research

Exhibit 6: Quarterly changes in O/s loans WALR

Source: Systematix Institutional Research

Exhibit 7: Trend in spread of PSBs fresh loans & o/s loans WALR and 5-year G-sec

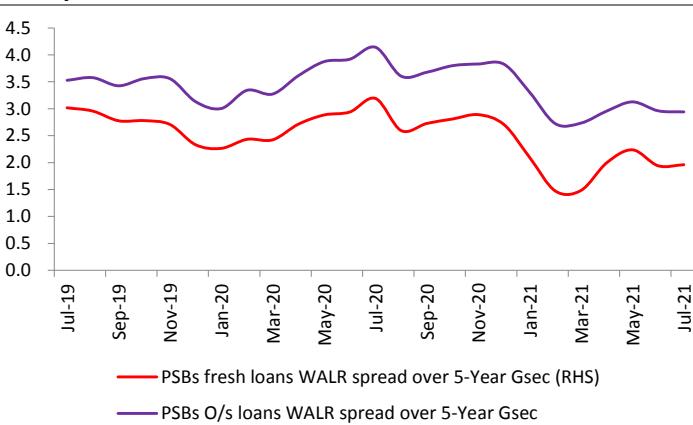


Exhibit 8: Trend in spread of PVBs fresh loans & o/s loans WALR and 5-year G-sec

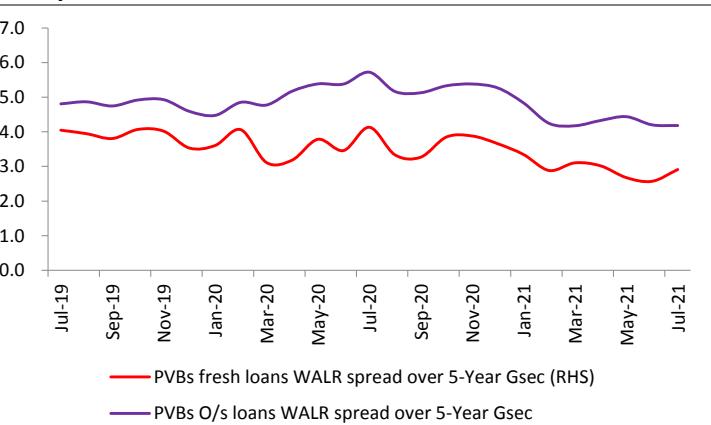


Exhibit 9: Movement in 5-year G-Sec yield and PSBs & PVBs fresh loans WALR

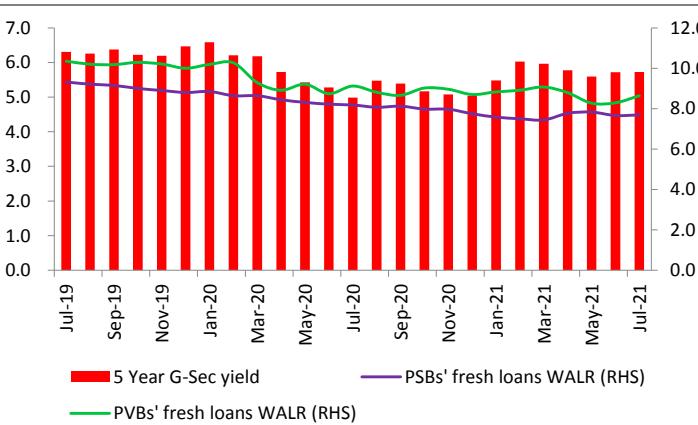


Exhibit 10: Movement in PSBs & PVBs fresh loans (over median MCLR)

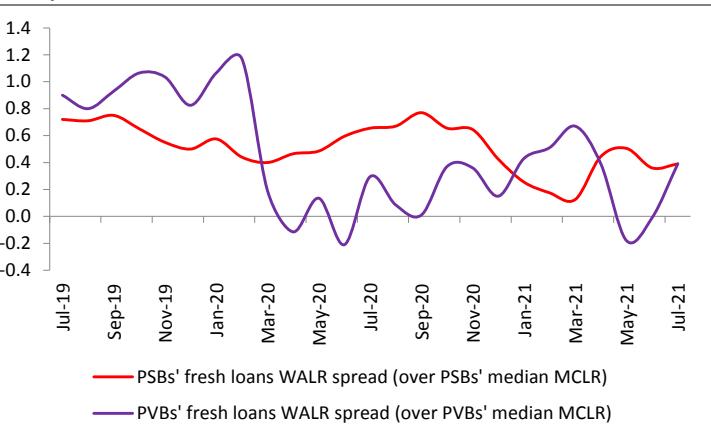


Exhibit 11: Trend in credit spread (over 1-year liquid AAA PSU yield)

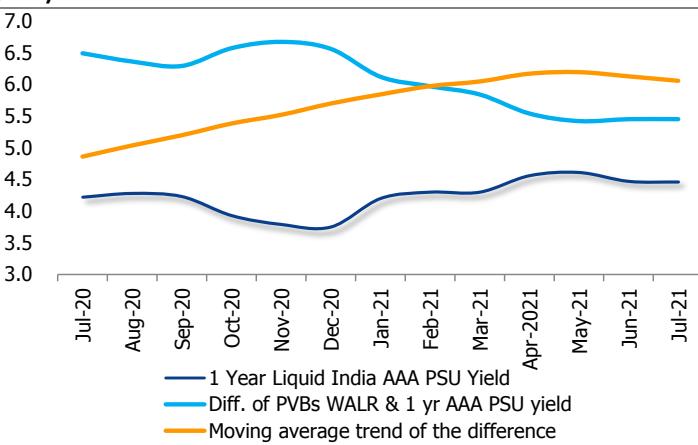


Exhibit 12: Trend in spread of PVB's WALR & 1-year India government bond generic bid yield

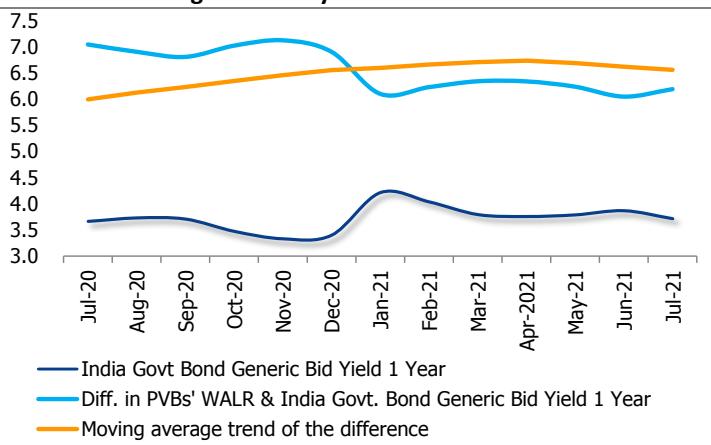
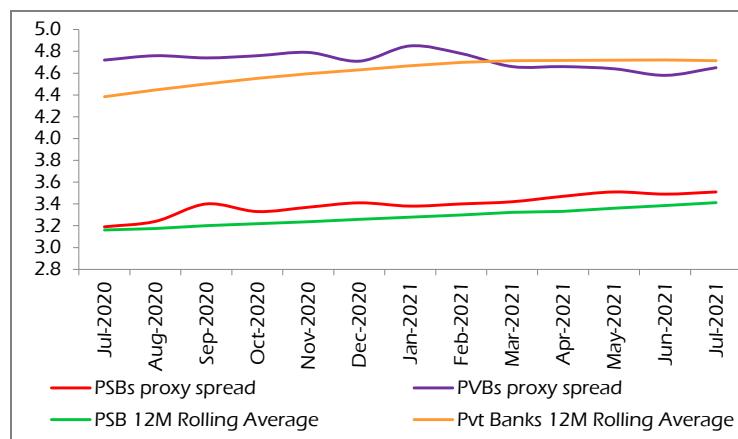
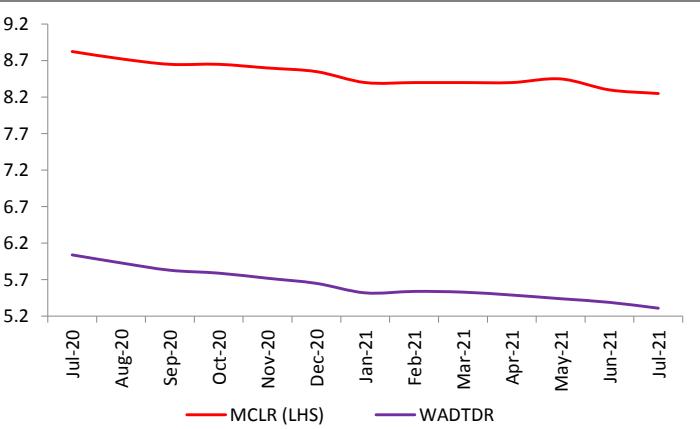
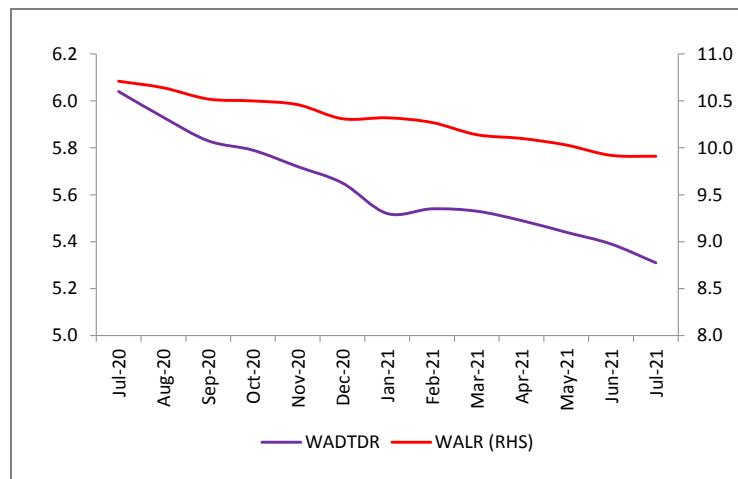


Exhibit 13: Movement in PSBs & PVBs proxy spreads

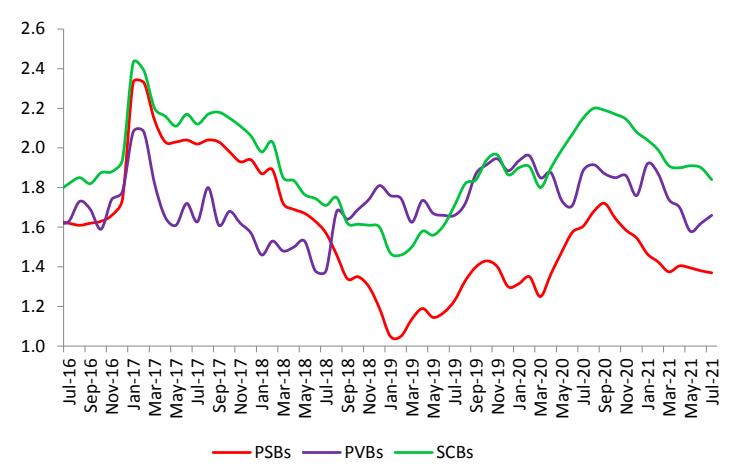
Source: Systematix Institutional Research

Exhibit 14: PVBs' movement in WADTDR & median MCLR (in %); fall in WADTDR reflects in lower MCLR

Source: Systematix Institutional Research

Exhibit 15: PVBs' difference between WALR & WADTDR (in %); slower transmission as WALR contracts gradually

Source: Systematix Institutional Research

Exhibit 16: SCBs, PSBs & PVBs difference between WALR & median MCLR (in %); softening of spreads (over MCLR) witnessed across banks

Source: Systematix Institutional Research

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