

## India: Banks

Equity Research

### RBI de-regulates rates on non-resident deposits; limited impact

#### News

Reserve Bank of India (RBI) has de-regulated interest rates on non-resident (external) rupee (NRE) deposits and ordinary non-resident (NRO) accounts. The interest rates offered on non-resident (NR) deposits by the banks cannot be higher than those offered on comparable INR deposits. The revised rates will be applicable on new and renewed deposits. Currently, premature withdrawal is allowed, but no interest is payable on NRE deposits withdrawn before 12 months (15 days for NRO deposits). According to RBI, given the current environment of a shortage in dollar funding and sharp currency depreciation, the de-regulation provides flexibility to banks in mobilizing NR deposits.

#### Analysis

The current differential between the INR term deposits and NRE deposits (LIBOR/Swap +275bp) in the 1-3 year category is 450-575bp industry-wide. We believe the interest rates on NRE deposits can potentially move up by 200-300bp due to a) greater demand for foreign exchange deposits, and b) the lower rates relative to even wholesale deposits. However, given the moderating credit growth, we expect rational behavior by banks on interest rates offered on NR deposits.

#### Implications

NR deposits account for 4.5% of total deposits in the system; therefore, we do not believe the impact on margins for banks would be material, except for those that have a higher proportion of NR deposits such as Federal Bank, which has c.7% market share in total NRE deposits in India. Federal Bank traditionally has had a higher proportion of NR deposits due to its significant presence in Kerala, a state with a relatively higher NRI population vs. other states in the country. Federal Bank has c.14% of its deposit mix in NRE deposits as of 2QFY12. Assuming 50% of NRE deposits get re-priced, given the revised rates will be applicable to new and renewed deposits, at a 200bp higher interest rate we estimate the impact on Federal Bank's FY13E NIM would be 8-10bp and approx. 2-4% on NII and PAT, respectively. Given attractive valuations and best-in-class operating matrix, we maintain our target price and estimates on Federal Bank.

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Rs.	Ticker	Rating	Price (16-Dec)	12-m TP	Up/downside potential (%)
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BOI	BOI.BO	Sell	310	280	-10%
OBC	ORBC.BO	Neutral	242	290	20%
PNB	PNBK.BO	Buy	832	1130	36%
SBI	SBI.BO	Neutral	1680	1920	14%
Union Bank	UNBK.BO	Sell	188	190	1%
<b>Private Banks</b>					
Axis Bank	AXBK.BO	Buy	900	1230	37%
Federal Bank	FED.BO	Buy	375	470	25%
HDFC Bank	HDBK.BO	Neutral	416	520	25%
ICICI Bank	ICBK.BO	Buy	676	950	41%
IndusInd	INBK.BO	Buy*	252	350	39%
Kotak Mahindra	KTKM.BO	Sell	481	470	-2%
Yes Bank	YESB.BO	Buy	257	350	36%

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Source: Datastream, Goldman Sachs Research estimates.

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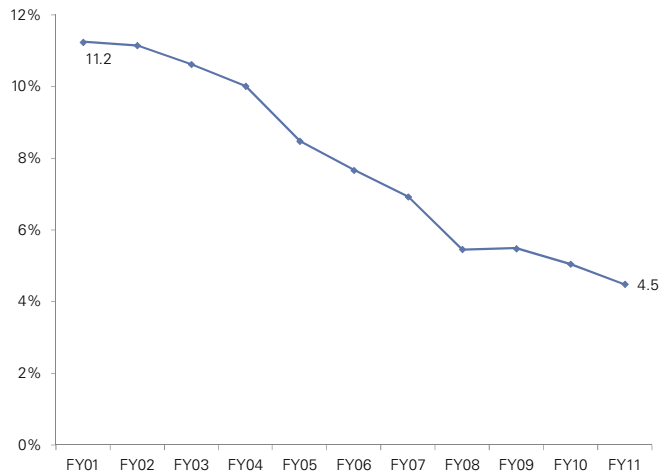
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**Exhibit 1: NR deposit share has been on the decline in the last decade; currently NR deposits comprise 4.5% of total system deposits**

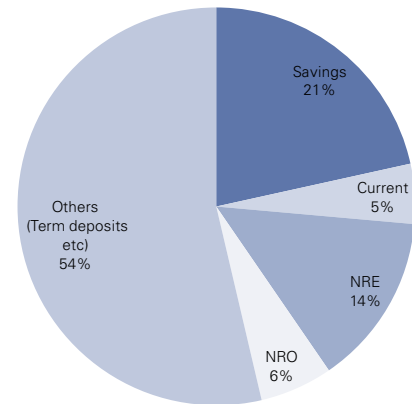
Non-resident deposits as % of total deposits



Source: Reserve Bank of India.

**Exhibit 2: 14% of Federal Bank's deposit base is comprised of NRE deposits**

Federal bank deposit mix as of 2QFY12



Source: Company data.

**Exhibit 3: Current differential between domestic and NRE term deposits is over 500bp**

Existing rates on domestic and NRE deposits offered by State Bank of India

Period	Domestic term deposit rates		
	NRE rupee deposit rates	< INR10 mn	> INR 10 mn
1 Year to less than 2 years	3.82%	9.25%	9.00%
2 years to less than 3 years	3.51%	9.25%	8.75%
3 years to 5 years	3.64%	9.25%	8.75%
3 years to 10 years	na	9.25%	8.75%

Source: State Bank of India.

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