

Financial conditions show healthy rise in Q1: survey

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Banks, financial institutions expect cost of funds to fall, liquidity index to rise



Mumbai, August 7:

A survey of banks and financial institutions has pointed to a healthy improvement in the country's financial conditions in April-June quarter, with its index rising to 61.1 from 47.8 in the previous quarter.

This is owing to strong expectations of leading banks and financial institutions regarding reduction in the cost of funds, comfortable liquidity position and better external financial linkages, revealed the survey, which is jointly conducted by the Confederation of Indian Industry (CII) and the Indian Banks' Association (IBA). The overall economic activity is also signalling improvement, albeit moderately.

The CII-IBA Financial Conditions Index comprises four sub-indices — cost of funds, funding liquidity index, external financial linkages, and economic activity. A total of 41 major banks and financial institutions with total assets of more than Rs. 72 lakh crore (as of March 2016), participated in the survey.

“The directional change in the performance of the Financial Conditions Index augurs well for the Indian financial sector as well as for the real sectors of the economy,” said Chandrajit Banerjee, Director-General, CII. “We are certain that traversing the external headwinds, the government and the RBI would continue to focus on the twin objectives of maintaining financial stability and enhancing economic growth,” he added.

Cheaper funds

Among the sub-indices, the Cost of Funds Index witnessed the maximum improvement to reach at 71.2 in the first quarter of the current fiscal, from 44.8 in the previous quarter. Most banks and financial institutions expect the overall cost of funds to decline in the current quarter.

The respondents expect the Marginal Cost Lending Rate (MCLR) and the short-term interest rates (the interbank call rate and the 3-month bank certificate of deposit rate) to decline.

Further, most participants of the survey expect the long-term interest rate (yield on 10-year government bonds) and the Corporate Bond Spread (between top-rated 10-year corporate bonds and government bonds) to improve in the first quarter, easing the overall cost of funds.

The Funding Liquidity Index stood at 67.5, the second-highest value among the sub-indices, recording a significant improvement from the previous quarter (45.7). The number is significantly higher than the 50-mark, pointing to a strong expectation of improvement in the funding of liquidity.

Rupee and forex positions

The External Financial Linkages Index is at 54.5 as against 36.0 in the previous quarter. The Indian financial sector remained unperturbed from the effects of the US Fed interest rate as most banks and financial institutions expect net capital inflows from FIIs to increase in the current quarter.

However, the rupee will depreciate against the US dollar and the country's foreign exchange reserves are poised to rise, the survey observed. Further, most respondents expect mobilisation by Indian companies through global equity and debt markets is unlikely to change significantly during the current quarter.

Economic activity suffers

At 51.6, the Economic Activity Index witnessed a deterioration from 64.6 in the previous quarter. The deterioration, on a quarter-on-quarter basis, was led by the performance of the Consumer Price Index (inflation), which was expected to fall.

Further, most respondents expected the Non-Food Bank Credit in the current quarter to deteriorate. However, they foresee an improvement in the growth rate of real GDP, whereas no significant change was expected in asset prices (stock and housing market) vis-à-vis the previous quarter.

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