

Small savings rates remain attractive compared to bank deposits: ICRA

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Mumbai, April 5: The limited decline in small savings rates has made them relatively more attractive, compared to bank deposits, which appears to be a relief for the banking system that is flush with funds, according to credit rating agency ICRA.

Given the continuing systemic liquidity surplus, liquidity management measures and rate action by the Reserve Bank of India are likely to drive deposit rate cuts in the ongoing year, reducing the relevance of timely changes in small savings rates for policy transmission, it added.

The relative attractiveness of the small savings rates is likely to help the Government of India achieve its borrowing target from this avenue (Rs. 1 lakh crore in FY18), albeit at a higher rate than its market borrowings.

In the prevailing scenario of high inter-bank liquidity, the stickiness in small savings rates has not hindered the fall in banks' deposit rates, unlike in previous phases of tighter liquidity, said ICRA.

Interest rates on small savings schemes, which are linked to Government security (G-Sec) yields, were reduced by a limited 20 basis points (bps) for the quarter starting April 1, 2017 relative to the quarter starting April 1, 2016, far short of the decline in G-Sec rates from March 2016 to March 2017. One basis point equals one-hundredth of a percentage point.

G-Sec yields decline

“For instance, the G-Sec yields on 1-year, 5-year and 10-year bonds have declined by around 100 bps, 77 bps and 68 bps respectively, from March 2016 to March 2017.

“The considerable reduction in G-Sec yields is partly on account of the 50-bps cut in the repo rate by the central bank over the last year, as well as the rise in banks' demand for such instruments following the note ban, which has led to a sharp rise in bank deposits amid limited avenues for lending,” said ICRA. As of March 17, 2017, year-on-year (YoY) growth of bank deposits and non-food credit stood at a divergent 13 per cent and 5.1 per cent respectively, contributing to an average liquidity surplus of more than Rs. 4.3 lakh crore being absorbed by the central bank through overnight and term reverse repos in the month of March 2017.

“Compared to the 50 bps reduction in repo rate over the course of FY17, banks have cut deposit rates by a sharper extent following the aforesaid surge in liquidity.

“For instance, the 365-day median deposit rate of scheduled commercial banks has come down by 80 bps since April 2016, out of which 40 bps has been in the aftermath of demonetisation of high-denomination currency notes, which began on November 8, 2016,” the agency said.

Moreover, deposit rates over a variety of longer tenures have come down by 100-200 bps across banks during FY17.

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