

# Despite RBI's rate cut, deposit and lending rates are unlikely to come down in a hurry

Radhika Merwin | Updated on February 07, 2019 Published on February 07, 2019



Given the modest deposit growth, banks may not cut deposit rates significantly. Whether PSU banks will be nudged to cut rates needs to be seen

Despite concern over the fiscal deficit and sticky core inflation, the RBI chose to surprise markets and cut its key policy repo rate -- at which banks borrow short-term funds from the RBI -- by 25 basis points to 6.25 per cent. The last rate cut by the RBI was in August 2017, when CPI inflation was 3.2 per cent, and within that, food inflation was at 1.96 per cent (inflation had moved up to 5.2 per cent by December that year).

While the rate cut and the reversal of stance to neutral suggests that there could be more cuts in the coming year, banks may not be in a hurry to trim deposits, and in turn lending rates. For one, credit has been growing at a faster pace than deposits, exerting pressure on banks' funding resources. Hence, a cut in deposit rates will be measured, and vary from bank to bank.

Two, despite deposit rates moving up for all banks in the last one year, the hikes have been more aggressive in private sector banks, given the higher traction in their loans. Given that credit growth is likely to further inch up for private banks, they will be wary about cutting deposit rates in a hurry.

Deposit rates for public sector banks are already significantly lower than most private sector banks. This gives them less leeway to trim rates. But whether the Centre nudges PSU banks to make the first move and pass the repo rate cut to borrowers, needs to be seen.

## Sharper moves in private banks

Deposit rates for most PSU banks have gone up by 45-50 bps on an average across tenures in the last one year. In contrast, private banks have hiked deposit rates by 75-100 bps over the past year. This is because credit growth for private sector banks has been healthy at 14-15 per cent, while deposits have been growing at single-digits. Hence, private banks have been increasing deposit rates more aggressively (broadly) than public sector banks to fund their credit growth.

With this trend likely to continue, the RBI's rate cut on Thursday may not see private banks trimming deposit rates in a hurry. Hence, lending rates, too, may not come down sharply. Data suggests that while private banks have hiked benchmark MCLR lending rates by 60-100 bps in the past year, public sector banks have increased their lending rates by a lower 40-50 bps (SBI though has hiked by 60 bps). There is unlikely to be any sharp fall in these lending rates.

While public sector banks continue to grow loans at a slower pace than private sector banks, and possibly have relatively lower pressure on funding resources, they may not tinker with deposit rates much. This is because the rates they offer are already significantly lower than that offered by private sector banks, leaving them little leeway to cut deposit rates. SBI, for instance, offers 6.8 per cent on a 2-3 year deposit, while HDFC Bank offers 7.4 per cent for the same deposits, while Axis Bank and ICICI Bank offer 7.5 per cent.

Hence, theoretically, sharp cuts are unlikely unless PSU banks are nudged to toe the RBI's line and transmit rate cuts to borrowers. At a system level, since the December 2017 quarter, the credit-deposit ratio has been on the rise. Now, at 76-77 per cent levels, a high credit ratio reflects the pressure on banks' resources -- deploying around Rs 76 or Rs 78 out of every Rs 100 deposit as loans. In such a scenario, the RBI's rate cuts may take time to be transmitted to the end-borrower.

Published on February 07, 2019



Save 61% on BusinessLine e-Paper  
Now at just ₹ ~~2,100~~ ₹ 799\* per year [SIGN UP](#)

[banking](#)   [monetary policy](#)   [interest rate](#)

[RBI and other central banks](#)

0

COMMENTS

Next Story

[IRDAI imposes Rs 9 lakh fine on United India Insurance for violations](#)

**You May Like**

Sponsored Links by Taboola

<b>Get a Machine Learning ... UpGrad &amp; IIITB</b>	<b>11 Month PG Diploma in Busines... Amity University Online</b>	<b>Everything You Need to Know... BloombergQuint</b>	<b>Coming to 12 cities across Ind... Squareyards</b>
--	--	--	--

**In Money & Banking**