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High inflation, low interest rates hit household savings

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- Senior bankers say that despite the low rates, there seems to be no dearth of deposits

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Millions of households are staring at negative returns from their savings with inflation peaking at more than 7% in September and any further cut in key policy rates is expected to aggravate the situation.

This has created an alarming situation for households that are already facing growing financial insecurity as a result of the widespread disruptions caused by the pandemic.

While household financial savings typically refer to currency, bank deposits, debt securities,mutual funds,pension funds, insurance and investments in small savings schemes, experts said it is heavily skewed in favour of bank deposits where returns have been on a steady decline following various steps taken by the Reserve Bank of India to push liquidity into the financial system.

Adding to the woes is soaring prices, which, measured by the Consumer Price Index (CPI) was at 7.34% in September, holding for the sixth straight month above RBI's flexible target of 2-6%. Meanwhile, State Bank of India's (SBI) one-two year fixed deposit (typically used as a benchmark) offers a return of 4.9%, pushing the real rate or the inflation-adjusted return to -2.27%.

The situation has been aggravated by the abundance of liquidity in the system, experts said, leading banks to cut deposit rates in tandem with lower lending rates.

SBI, India's largest bank, lowered its term deposit rates in the one-two year bracket by 20 bps last month. Meanwhile, RBI has cut the policy repo rate by 115 bps so far this year but has opted for pauses in the last two policy meetings.

"Inflation has been above 6% for quite some time now, and term deposit rates have also come down, particularly post-pandemic," said Sameer Narang, chief economist, Bank of Baroda. That, Narang said, is because of excess liquidity, which is unlikely to change in the near term as the demand-side (in terms of credit offtake) is going to remain weak, and RBI has indicated it will continue with its accommodative stance.

Banks parked ₹5.65 trillion with RBI through its reverse repo window at a meagre return of 3.35% even as non-food credit growth languished at 5.1%.

Care Ratings said in a note on 13 October that deposit growth as on 25 September moderated as compared with the previous fortnight and indicates that with the nearing of the festive season, depositors have started spending.

“Depositors should be thankful that rates have not been further cut," said a senior economist on condition of anonymity. While one would see India Inc. up in arms when real interest rates are high, there seems to be little concern for ordinary depositors who are effectively seeing their principal erode because of negative returns, he added. This, while RBI governor Shaktikanta Das recently said the primary concern of any bank should be to protect the interest of depositors.

There are small depositors; there are middle-class depositors; there are retired people who depend on bank deposits, Das said on 16 September.

“Take the monetary policy panel meetings for instance. No one seems to be talking about how depositors are earning less every month and the entire focus is on bringing down rates for the government to borrow," the economist cited above said.