

# India: *Actions speak louder than words*

04<sup>th</sup> Sept 2024

## BANKING RESEARCH TEAM

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- Post the RBI Governor's discussion on financial stability in August MPC and asserting the need for banks to try innovative methods to raise deposits, there has been a lot of debate on “missing deposits”
  - *We conclude that “deposits are not missing” yet what the banks are missing is “CASA” i.e. low-cost deposits*
- In our view, the financial market participants are focused on analysing the drivers of low deposits, yet missing the direction of RBI action(s) on addressing credit excesses and lowering the credit-deposit ratio (financial stability metric)
  - *Steps to restrict bank loans to NBFCs ex HFCs, unsecured retail sub-segment, top-up loans along with proposed steps to raise LCR requirements, risk weights on project finance etc are likely to slow credit growth*
  - *RBI has been active in two-way liquidity management aligned with “withdrawal of accommodation” policy stance, driving low reserve money growth. However, periods of liquidity deficit esp. on elevated government balance with RBI, have seen liquidity injection via VRRs*
- With some of the RBI actions bearing fruit and assuming that incremental CD ratio slips to 85% in FY25 vs 95% last year, despite a strong deposit growth of 12%, credit growth is likely to see convergence at close to 12-13%.
- In a volatile world, we are not penciling in any rate cuts this year with the MPC firmly focused on the domestic food inflation vulnerable to frequent climate shocks. Additionally, relatively stronger growth providing policy space to delay start of rate cuts, with the RBI focused on financial stability especially the credit excesses.

Are we missing the wood for the trees?

Shaktikanta Das flags concerns on low deposit growth, says household savings moving from banks to MFs

Rethink needed on widening credit-deposit growth gap: Das

Banks should offer innovative products, service to garner deposits: Das

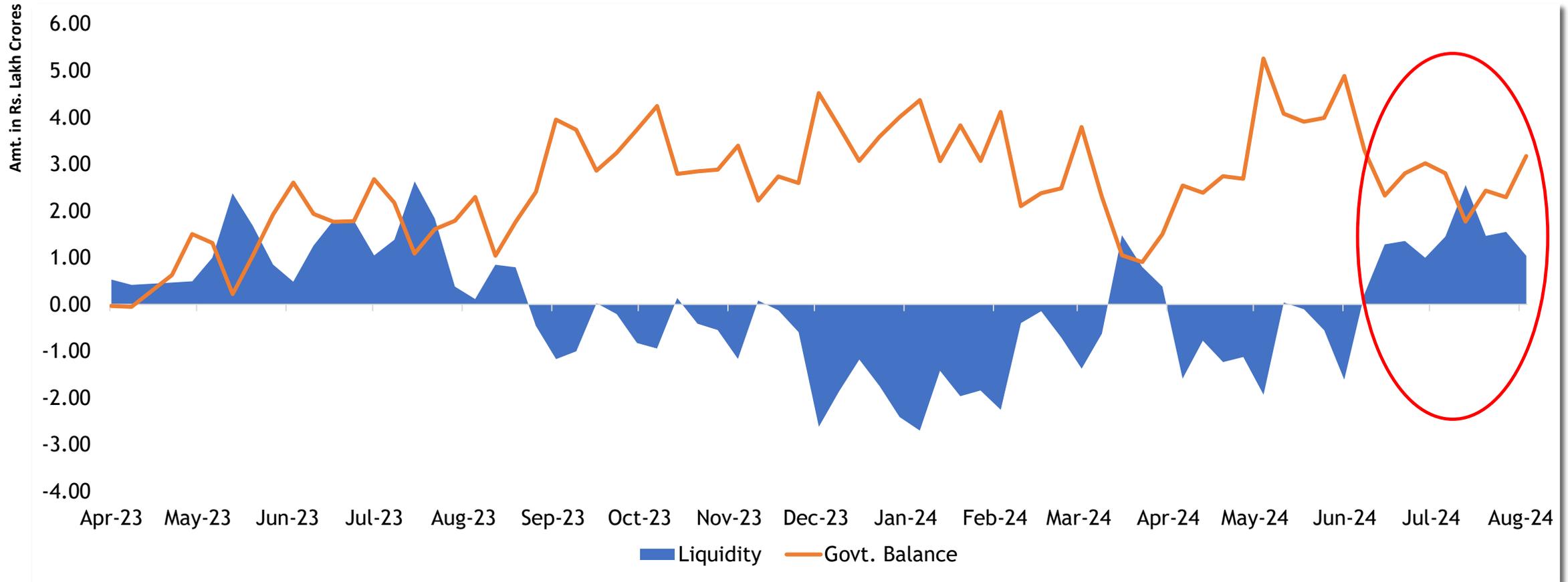
Finance Minister to banks: Innovate, focus on small deposits to plug gap with credit growth

RBI urges vigilance on home equity, top-up loans amid rapid growth

RBI tightening: Bankers blame 'high' NBFC exposure to small unsecured loans

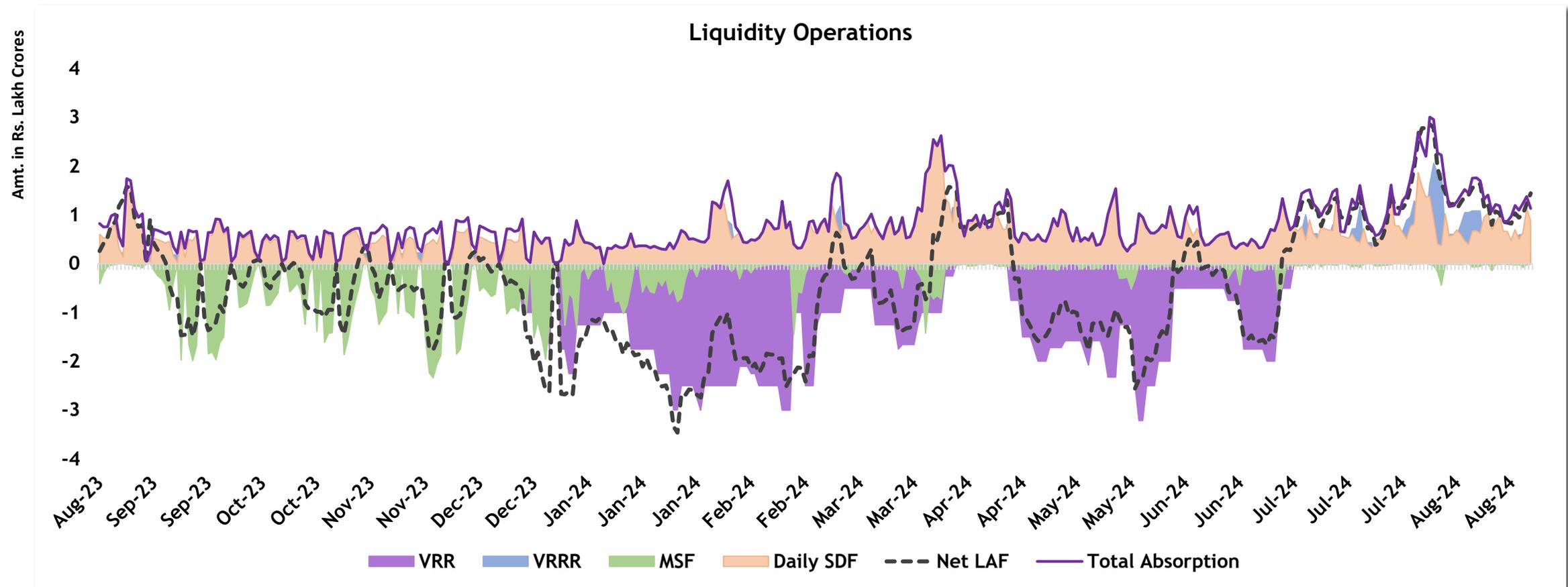
RBI's new liquidity coverage guidelines for banks could slow credit growth

RBI proposes tighter project finance rules



- After staying in deficit mode since September 2023, banking system liquidity has switched to surplus since end June 2024
- Government spending post elections and capital inflows post JP Morgan index inclusion since 28th June along with seasonal drop in currency leakage helped support liquidity dynamics

...with RBI absorbing most of it to align its liquidity stance with policy stance

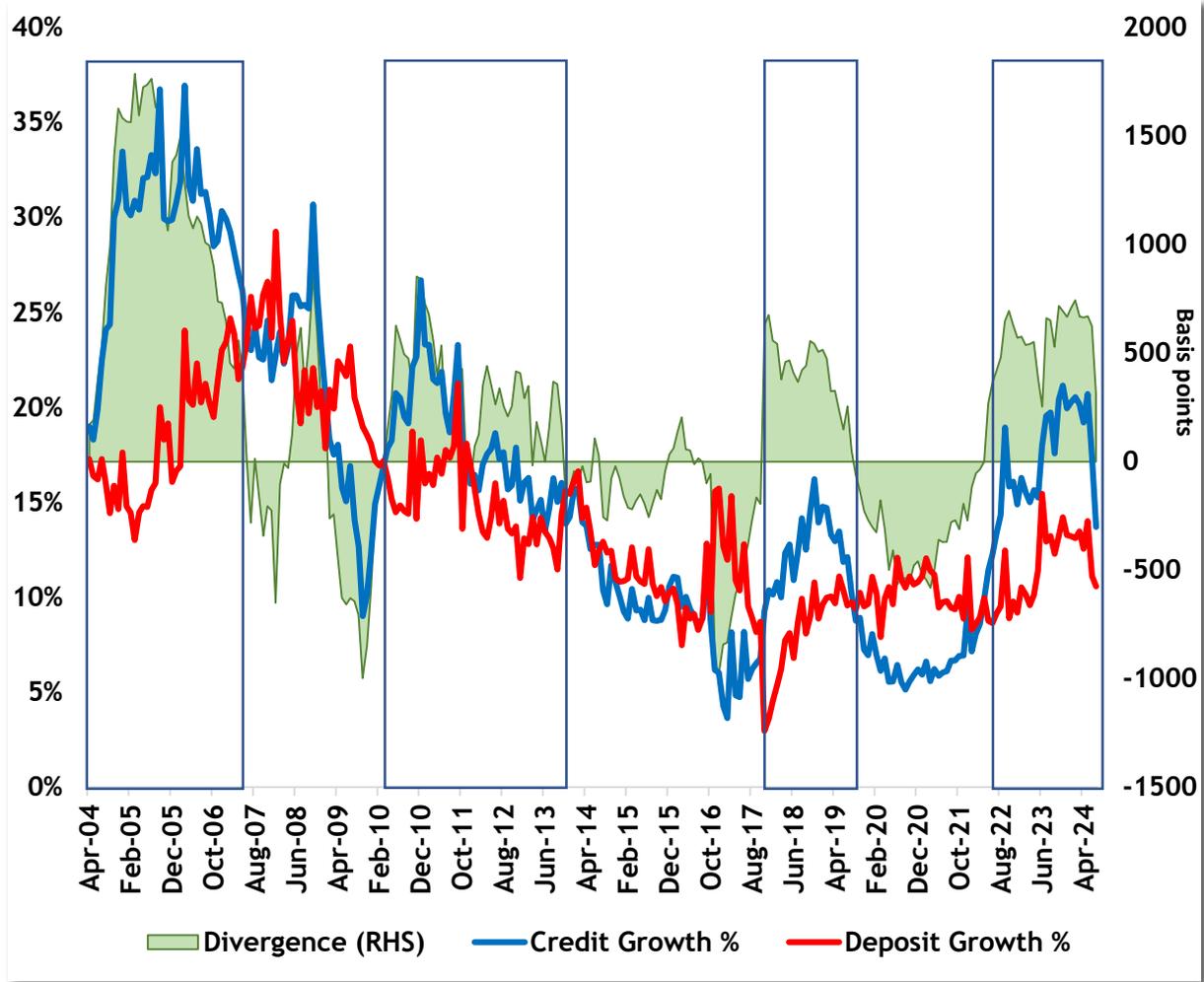


- RBI has been actively monitoring the liquidity situation to align with its “withdrawal of accommodation” policy stance. With the switch in liquidity to surplus, the central bank has largely been absorbing it via VRRRs apart from also conducting OMO sales (c.Rs 17,165 cr during July/Aug’24)
- Meanwhile, RBI has been conducting two-way fine tuning operations to ensure a minimum average liquidity balance. During periods of low liquidity especially on elevated government balance, RBI has also provided for liquidity via VRRs

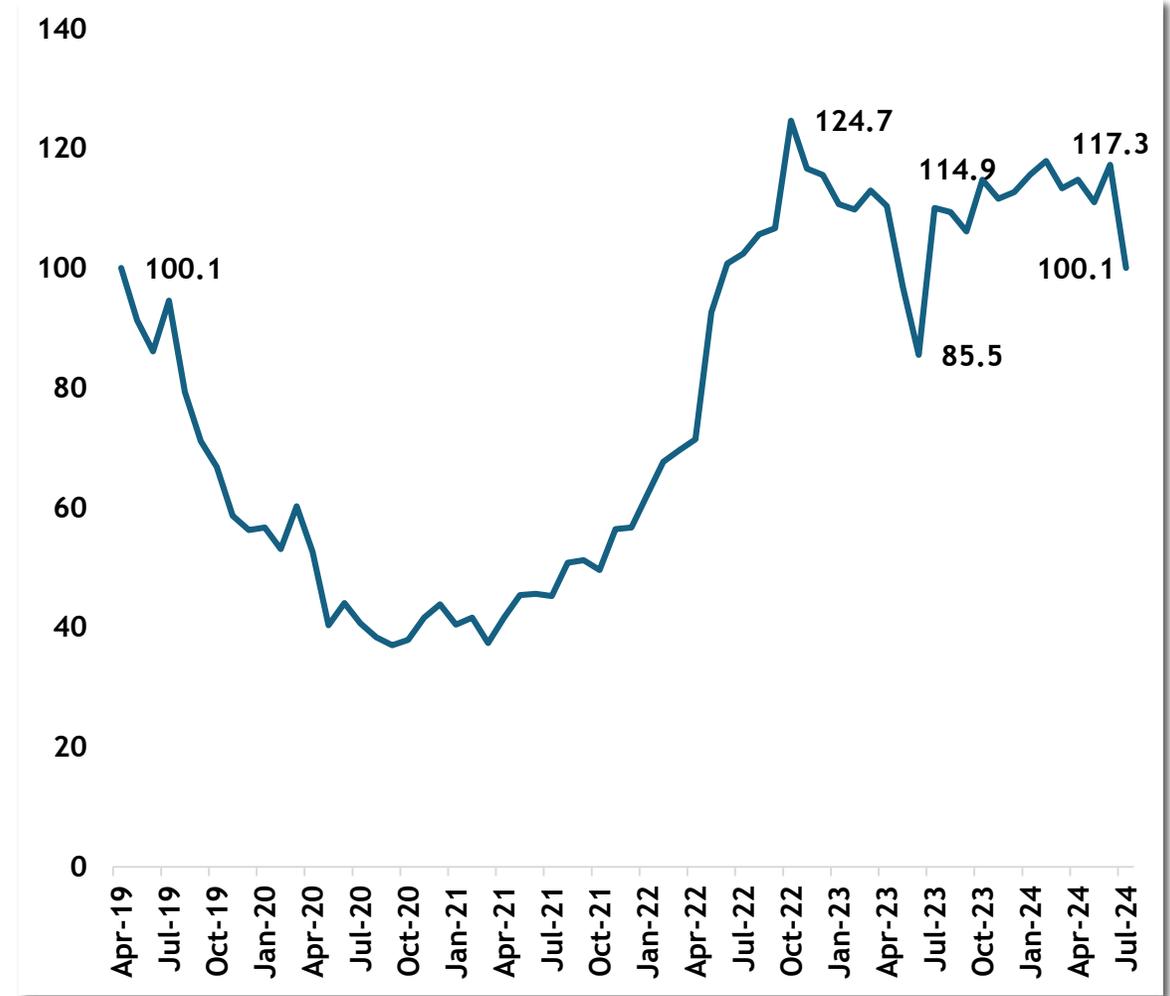
- RBI Governor spent an unforeseen close to 10 minutes in August MPC statement on “financial stability”
- As per the Governor, alternative investment avenues are becoming more attractive to retail customers and banks are facing challenges on the funding front. He asserted that:
  - *Banks may, focus more on deposit mobilisation through innovative products and service offerings and by leveraging fully on their vast branch network*
  - *Banks are taking greater recourse to short-term non-retail deposits creating ALM mismatch*
- This has a triggered a debate between economists and banking analysts on the theory of “missing deposits”
- We think that they are “missing the wood for the trees” as the bigger focus needs to be on the excessively high credit growth which the RBI wants to ease to align with the “withdrawal of accommodation” policy stance.

**C-D Ratio usually spikes during high growth phases**

### Credit & Deposit Growth – Long Term Dynamics



### Incremental CD Ratio



We agree that issue is not “missing deposits”, but credit growing much faster

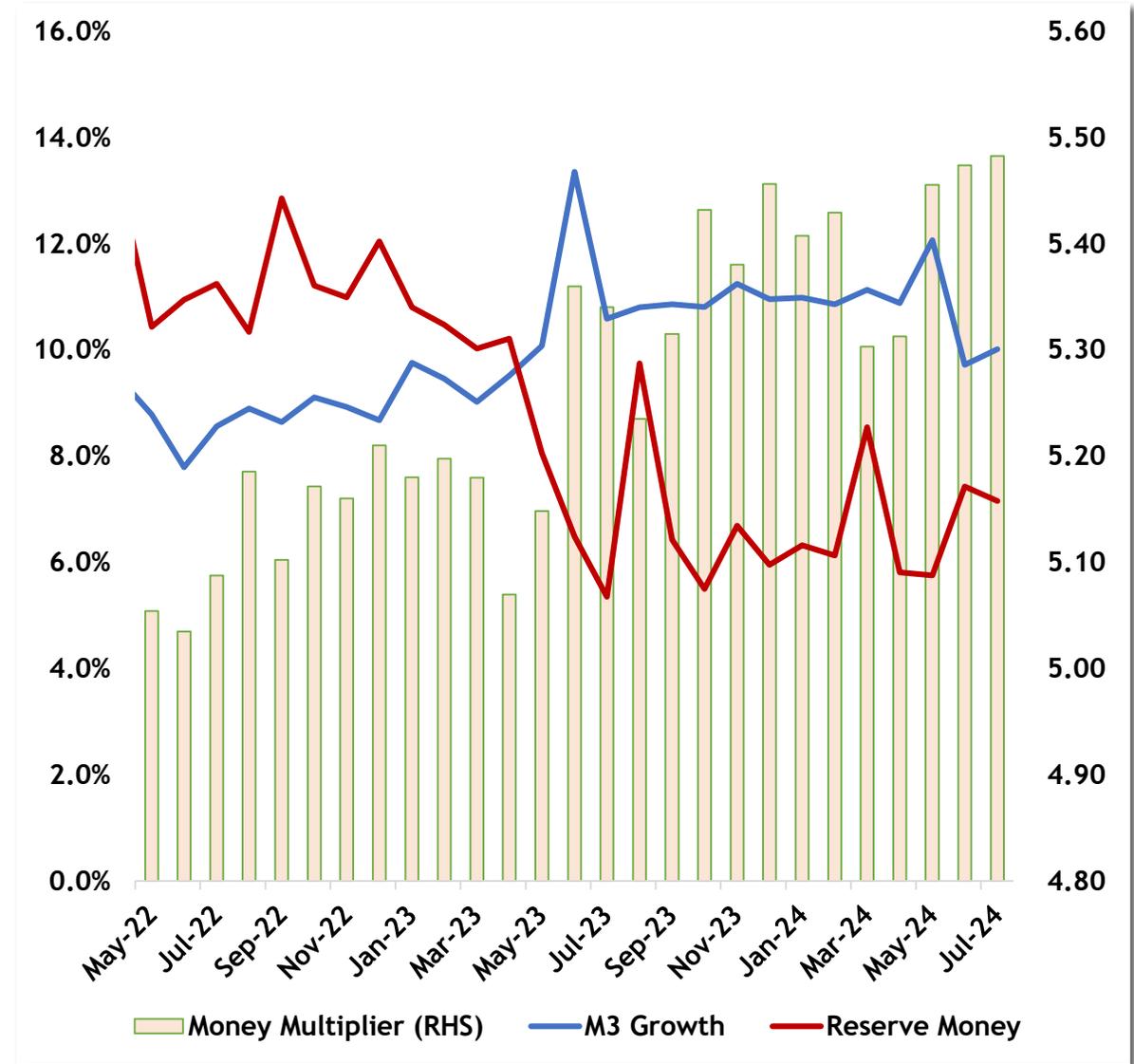
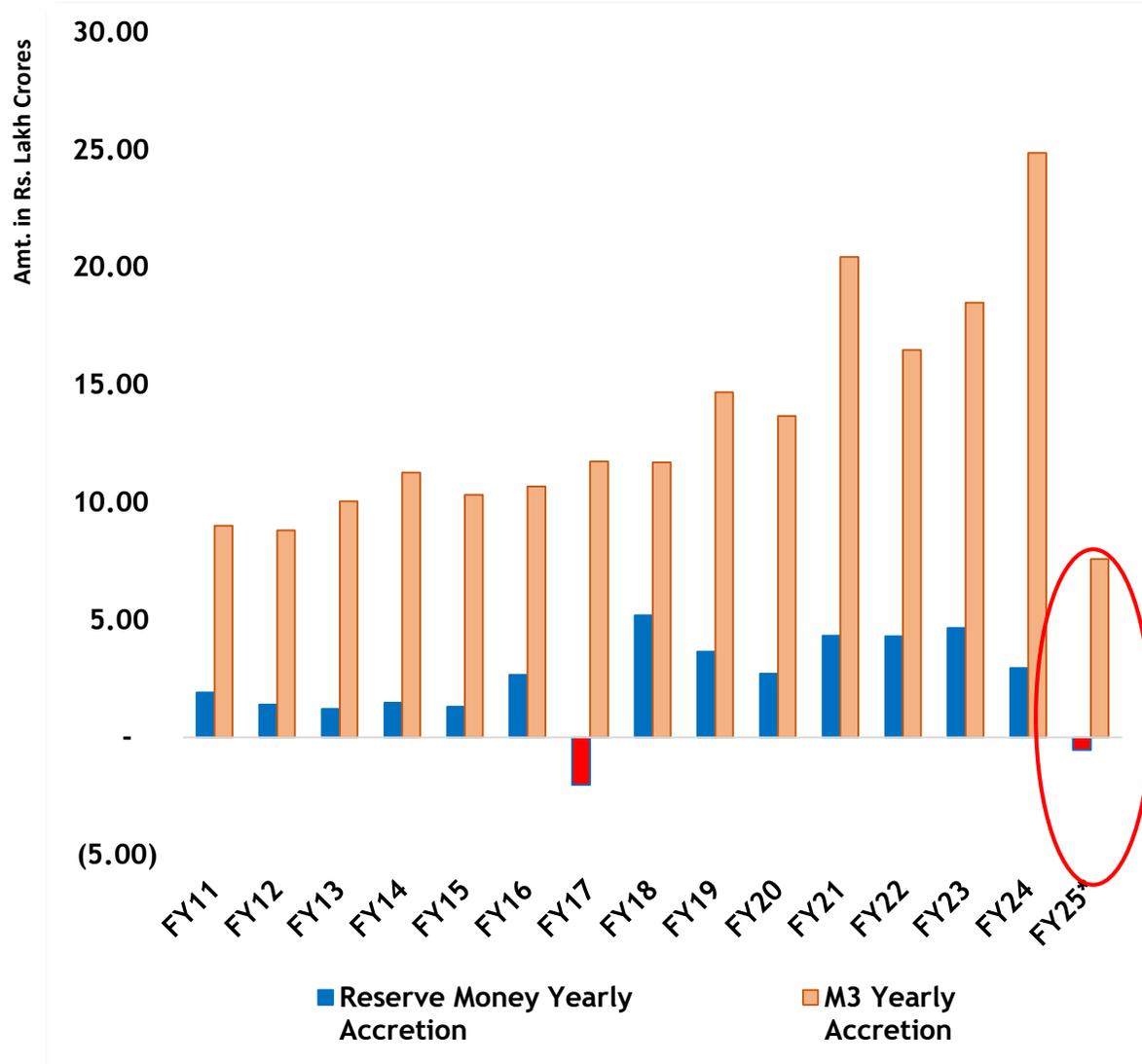
## Accretion in GDP , Credit & Deposit

Amt. in Lakh Crores

FY	Credit	Deposit	Incr. CD Ratio (%)
FY08	4.3	5.9	74
FY09	4.1	6.4	65
FY10	4.7	6.6	71
FY11	7	7.2	97
FY12	6.7	7	96
FY13	6.5	8.4	77
FY14	7.3	9.6	77
FY15	5.4	8.3	65
FY16	7.1	7.9	90
FY17	5.9	14.3	41
FY18	7.8	6.7	117
FY19	11.5	11.5	100
FY20	6	9.9	60
FY21	5.8	15.5	37
FY22	9.4	13.5	70
FY23	17.8	15.8	113
FY24*	27.6	24.3	113
FY24 (without merger)	22.3	23.2	96

RBI has been concerned about the sharp spike in incremental C-D ratio, a key metric for financial stability, to uncomfortably high levels (long term avg: 82-83%)

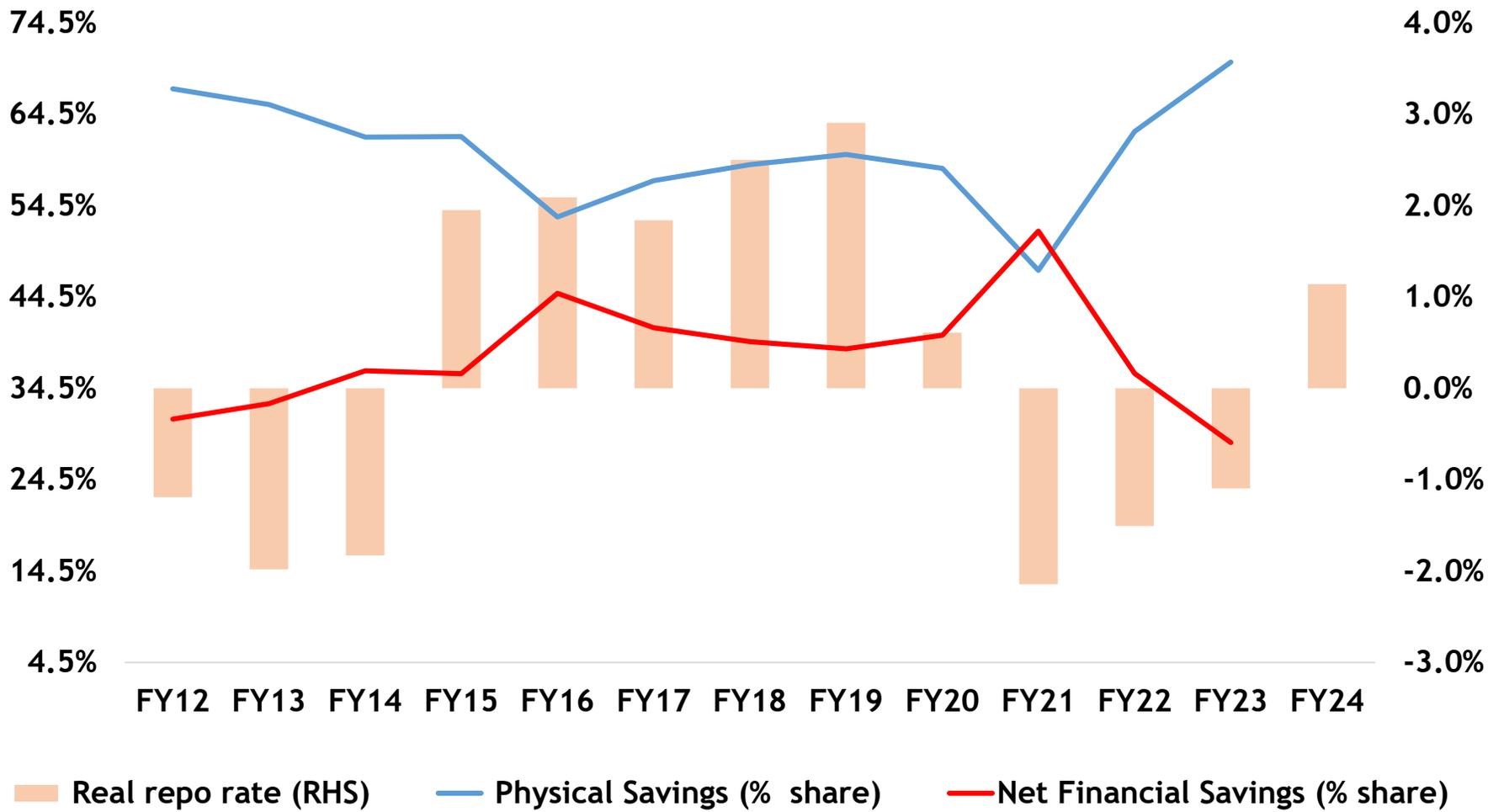
# Higher Credit Demand served by Banks via higher money multiplier even as Reserve Money growth is kept moderated



\*Data upto 23<sup>rd</sup> Aug-24; Source: RBI, CEIC, UBI Research

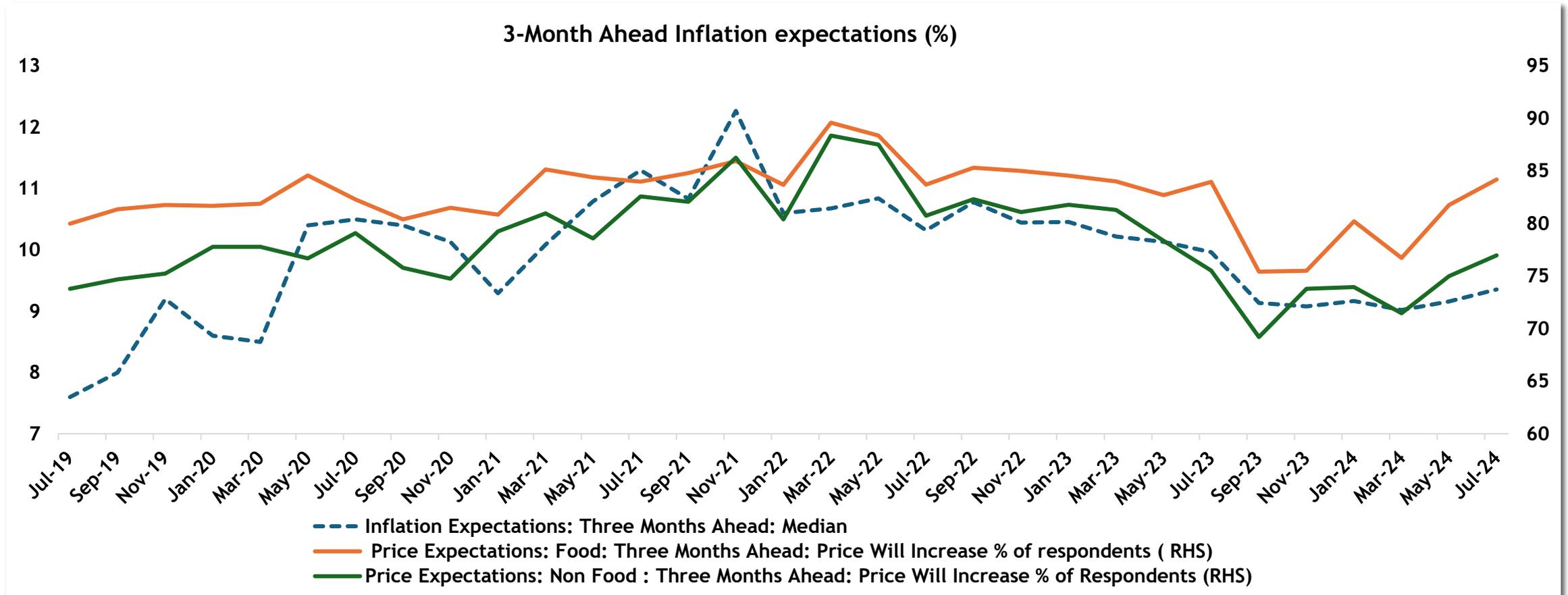
**We agree with the story  
“Deposits are not missing”**

# Shift in households' investment preferences has been linked to low deposit growth



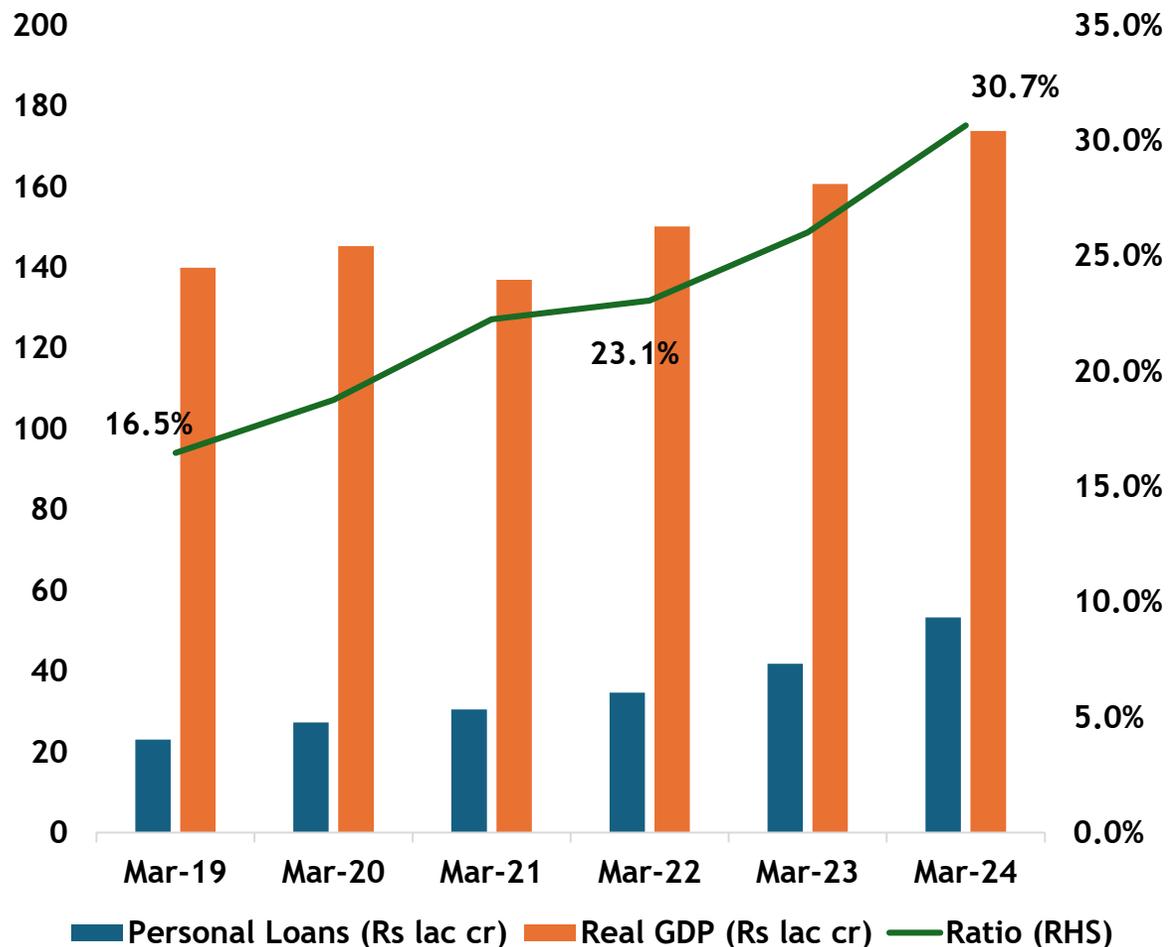
Interestingly, the share of physical savings in total household savings at 70% is similar to taper tantrum period which also saw a loud call for higher real rates. Similar research seen from RBI on higher potential growth and (perceived) inflation

# Persistence of elevated (food) inflation expectation has led to “hunt for yield” among households

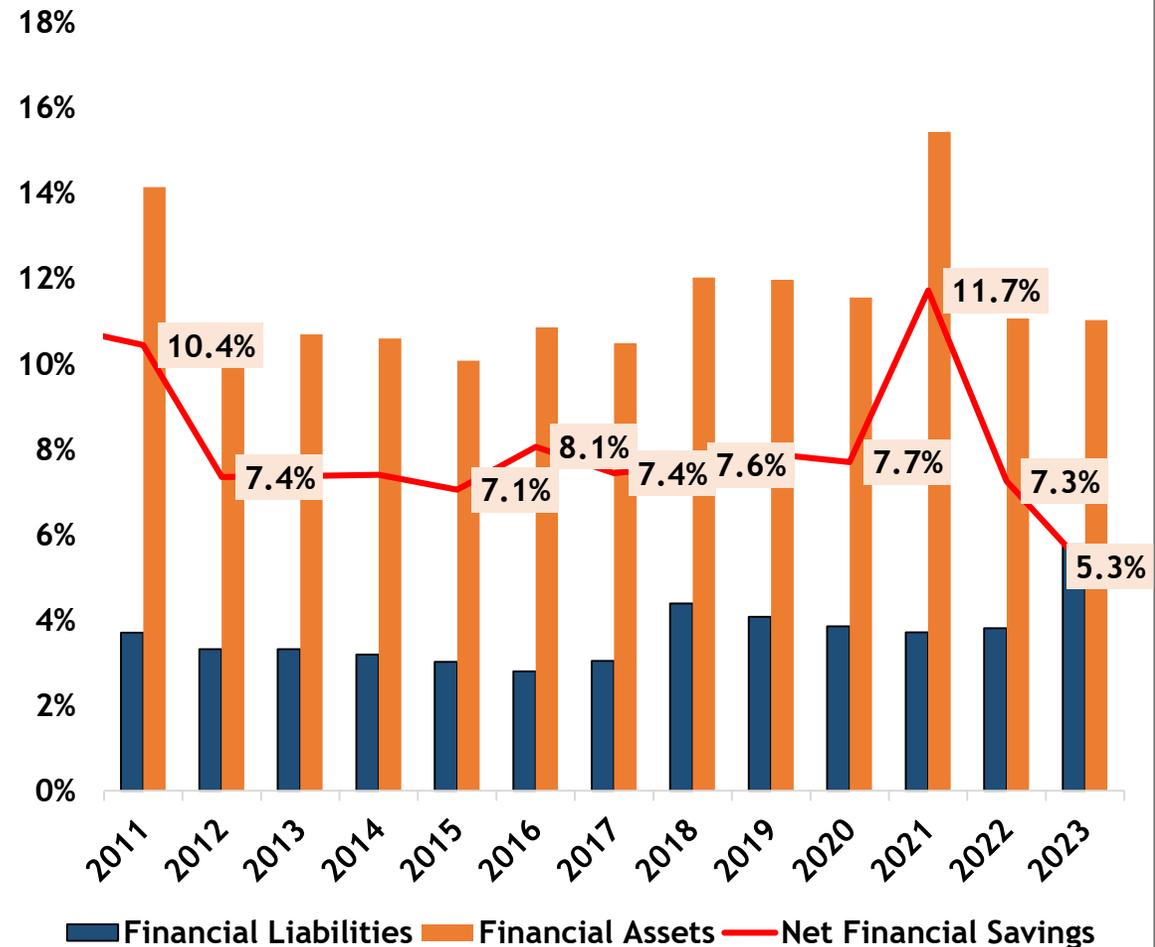


- We agree with the RBI Governor’s statement in August MPC, “With this high share of food in the consumption basket, food inflation pressures cannot be ignored. Further, the public at large understands inflation more in terms of food inflation than the other components of headline inflation. Therefore, we cannot and should not become complacent merely because core inflation has fallen considerably.”
- Historical RBI analysis shows, that 65% of inflation expectations are driven by petrol/diesel and vegetable prices. With the former broadly unchanged since May-2022, the volatility in vegetable prices has likely kept inflation expectations elevated and driven the hunt for yield by households.

Household leverage levels have spiked, personal loans from banks up 2x from FY20-24



Household financial savings have slipped to 47 year lows in FY23 (% of GDP)



However, we see a rise in household savings in FY24 as seen in spike in bank deposits...

### Ownership wise Accretion in Total Deposit

Amt. in Rs. Lakh Crore

Total Deposit	FY20	FY21	FY22	FY23	FY24	Q1 FY25*
General Government Sector	-0.07	1.63	2.06	1.61	2.99	-0.96
Corporations	2.78	3.36	5.89	5.31	7.14	-0.49
House Holds	7.59	11.51	7.58	9.74	14.10 <sup>#</sup>	2.41
Others	1.02	0.20	0.21	0.97	1.56	0.40

<sup>#</sup> Partly affected by withdrawal of Rs.2,000 notes

\*Q1 FY25 Data is without RRBs and increment from Mar-24 to Jun-24; Source: RBI, UBI Research

...primarily in term deposits

### Absolute Increase in Term deposits of individuals

Amt. in Rs. Lakh Crore

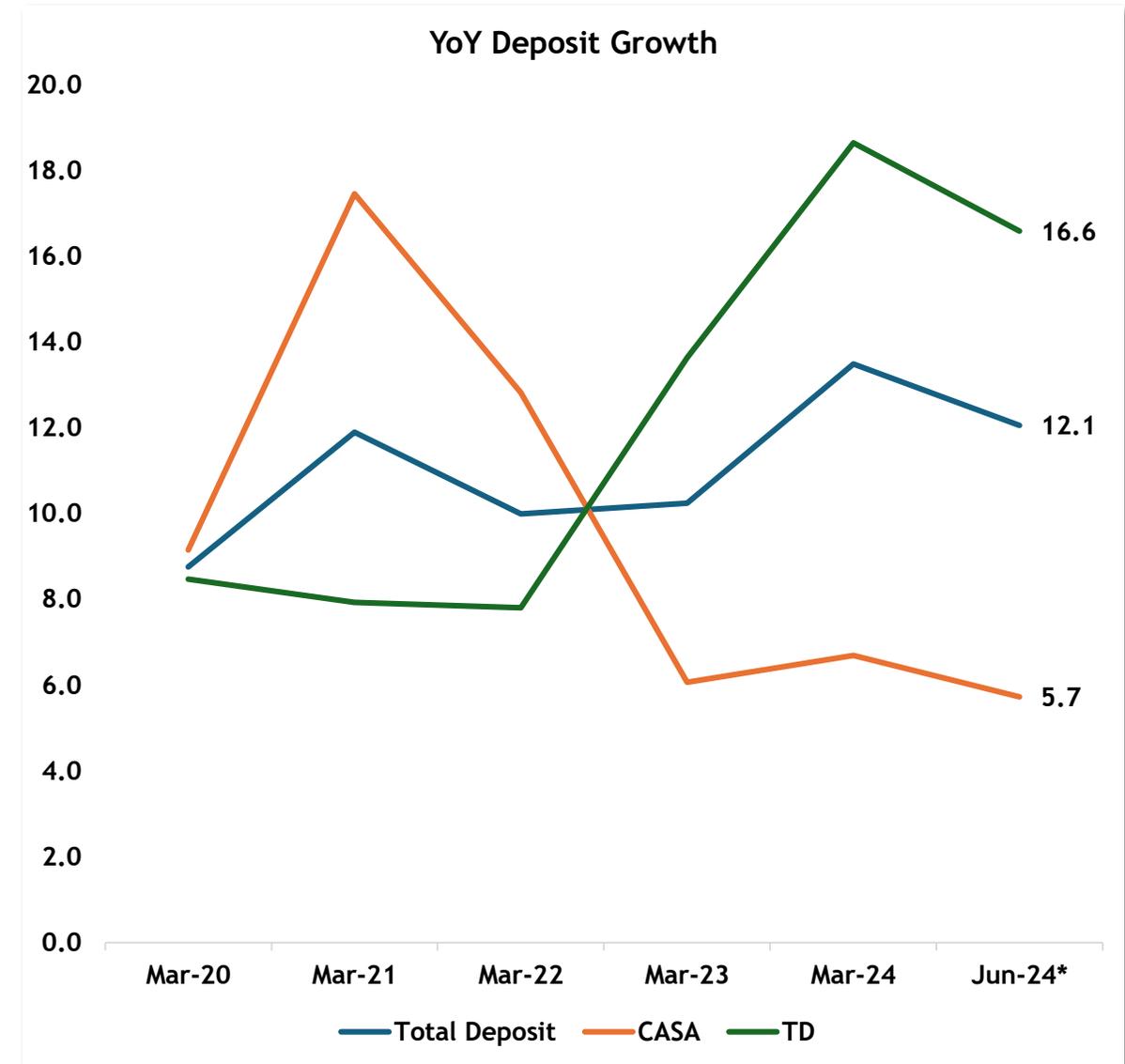
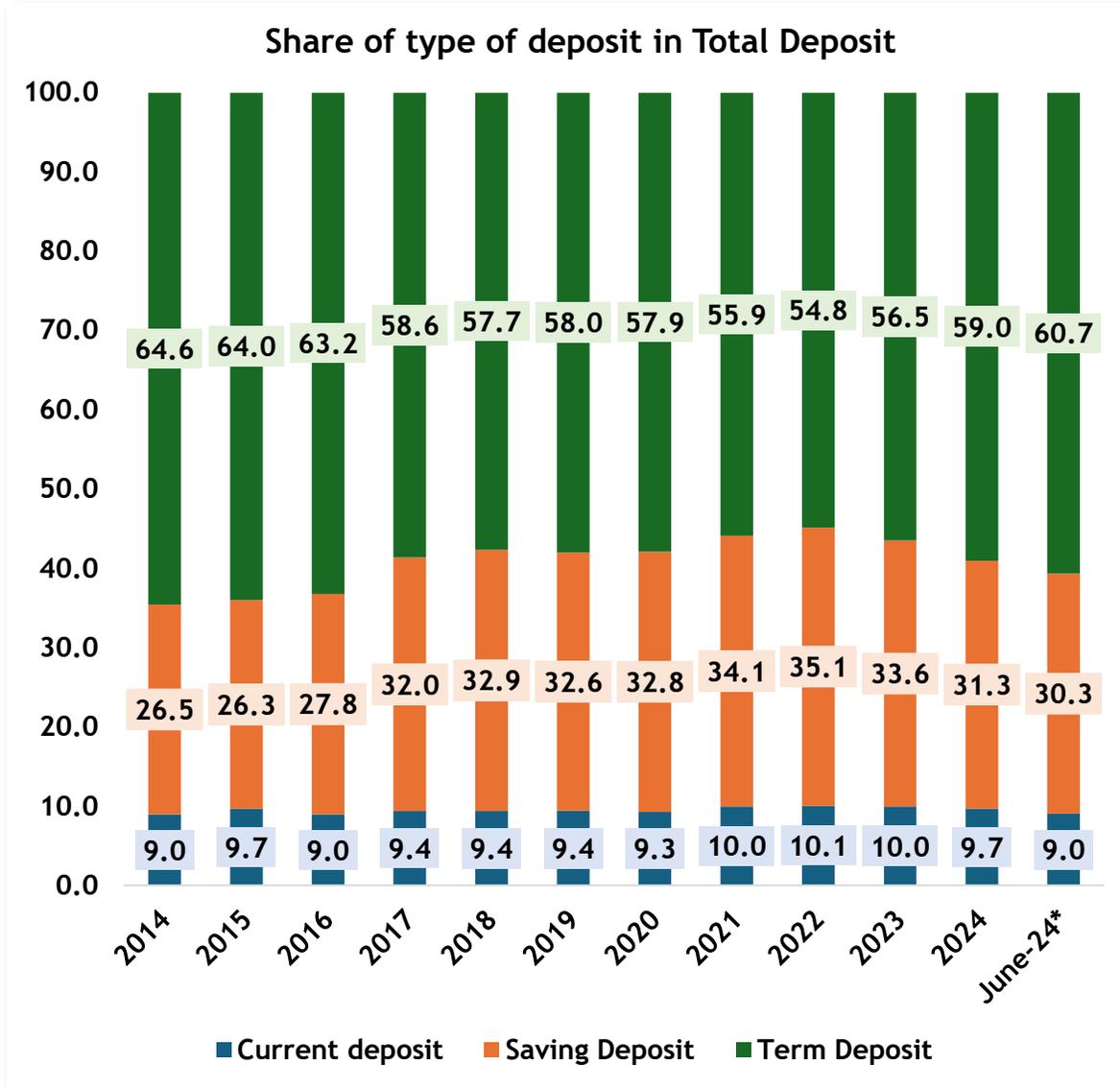
	FY20	FY21	FY22	FY23	FY24
Less than 1 Crore	3.33	2.9	2.61	4.54	7.89
Above 1 Crore	0.57	0.41	-1.12	0.57	0.76
Total	3.9	3.31	1.49	5.11	8.65

### Absolute Increase in Term deposits of other than individuals

Amt. in Rs. Lakh Crore

	FY20	FY21	FY22	FY23	FY24
Less than 1 Crore	1.31	0.63	0.16	0.31	0.83
Above 1 Crore	0.34	2.82	5.57	6.2	8.71
Total	1.65	3.44	5.73	6.5	9.55

Hence, the issue is not “missing deposits” but “missing CASA”

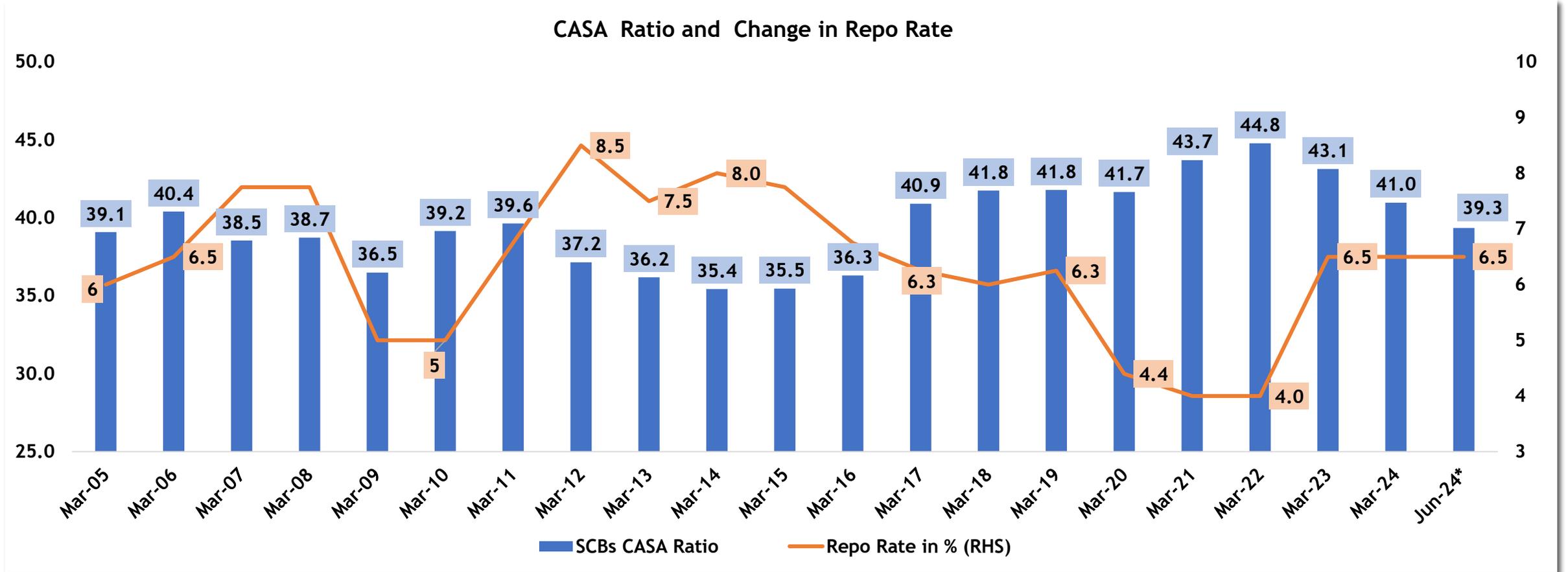


\*Q1 FY25 Data is without RRBs and increment from Mar-24 to Jun-24; Source: RBI, UBI Research

## Absolute Increase in Total deposits by type

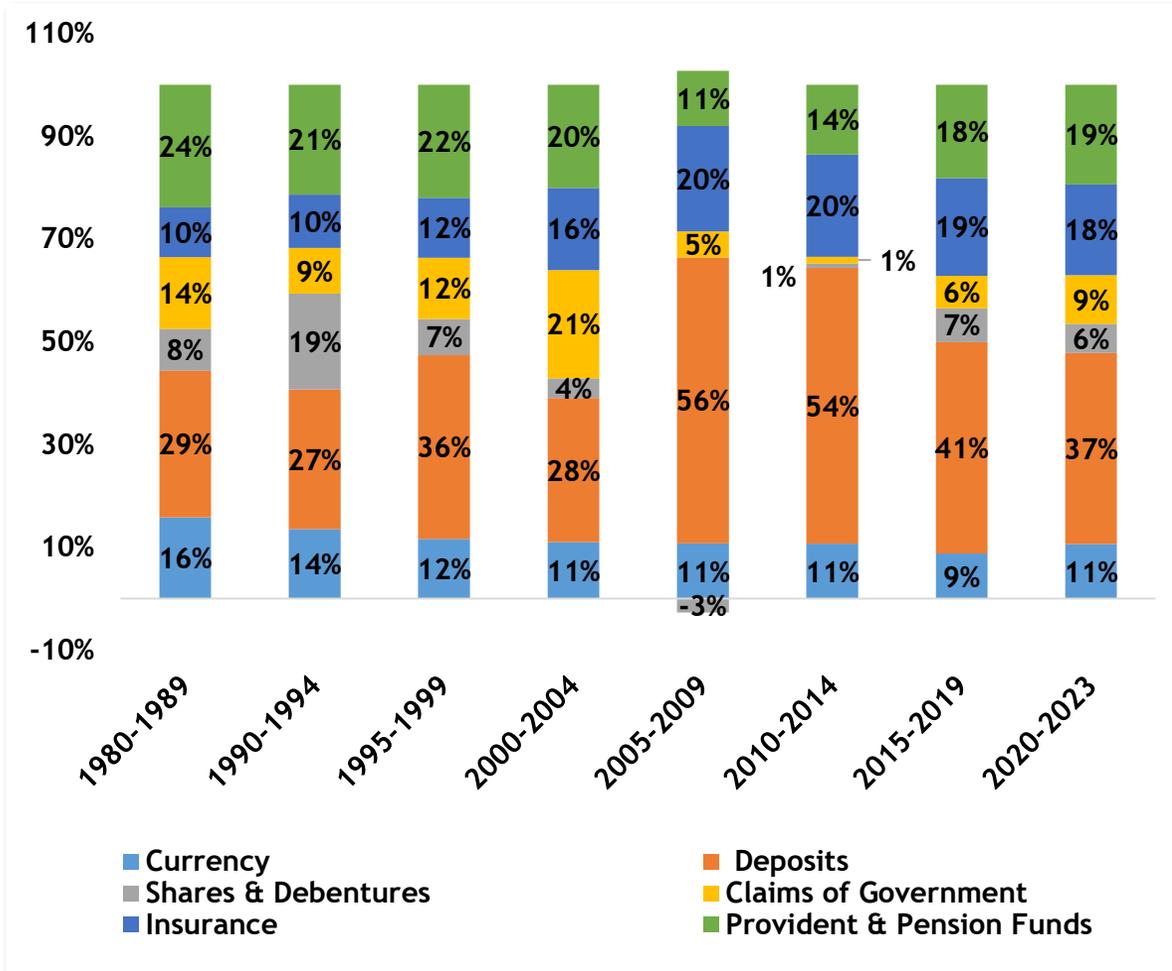
Amount in Rs. Lakh Crore	FY22	FY23	FY24	Q1 FY23*	Q1 FY24*	Q1 FY25*
CASA	8.7	4.8	5.5	-1.1	-0.9	-1.8
Term Deposit	6.9	12.6	19.6	1.07	4.8	3.3
Total Deposit	15.7	17.3	25.1	-0.04	3.8	1.6

Sharp drop in CASA during Q1 FY25

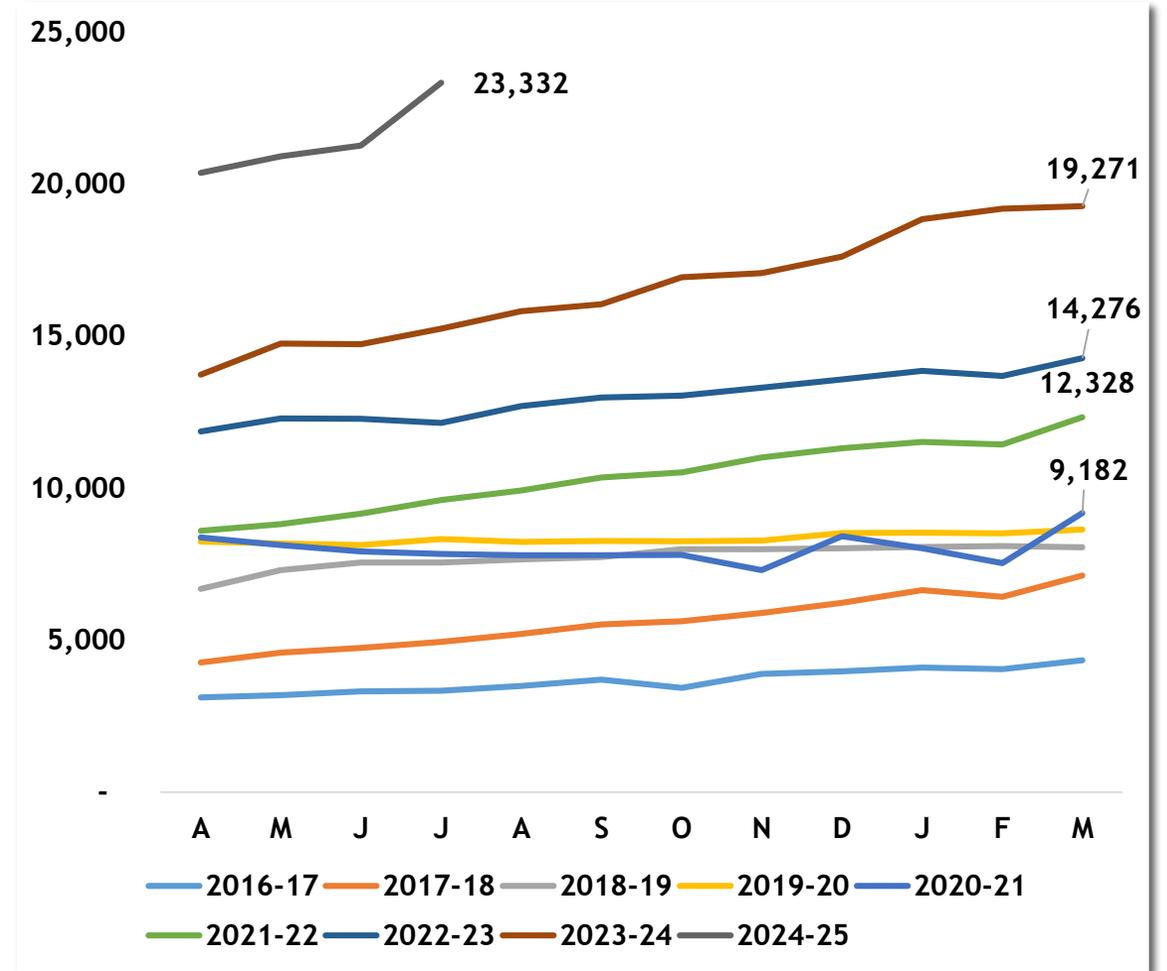


- Historically, CASA ratio across Bank groups drops during rising Repo Rate cycle & faces upward pressure during Repo rate cut cycle.
- The shift of Household financial savings away from bank deposits toward equities, MFs, Insurance & other wealth management products likely to keep CASA under pressure.

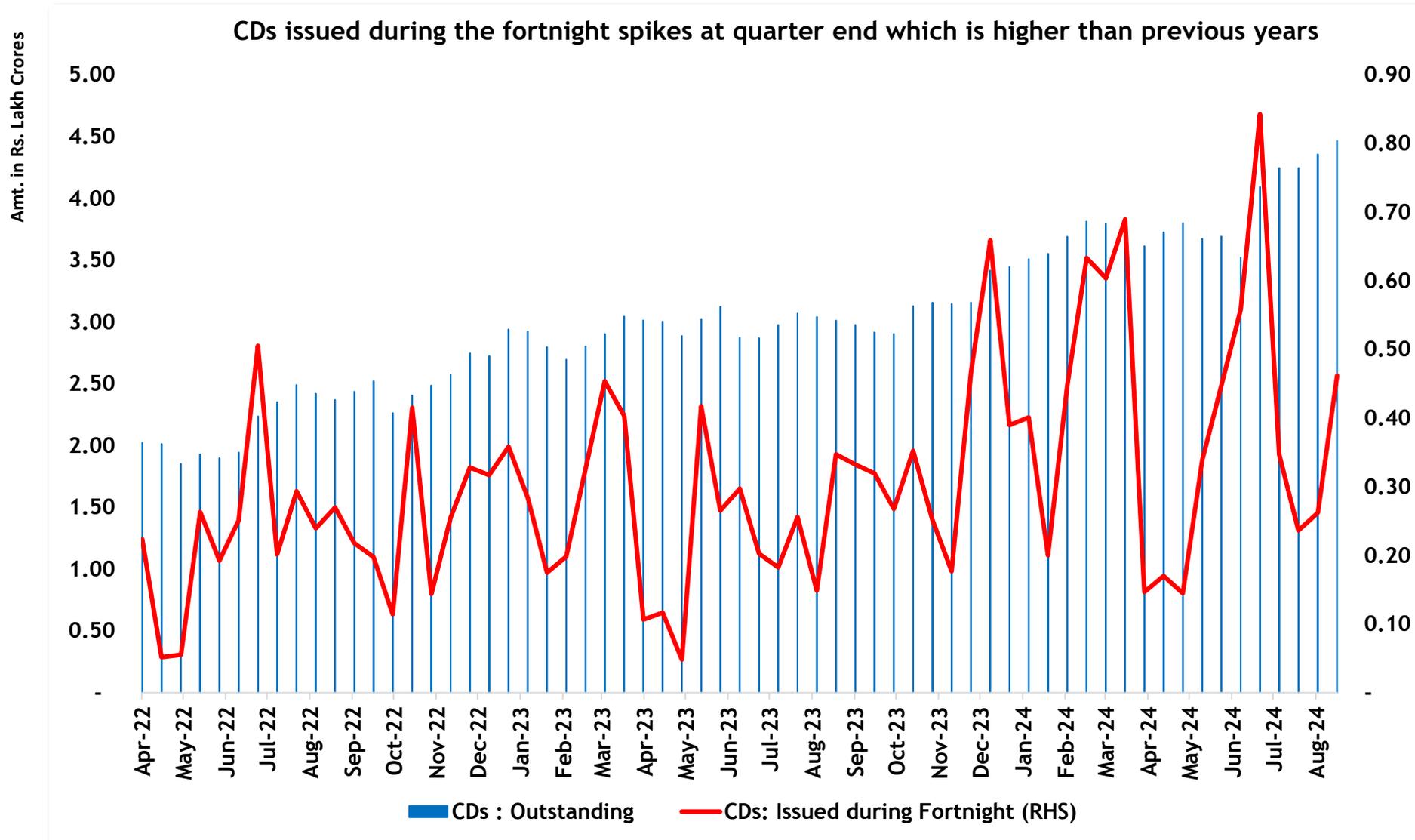
## Share of bank deposits in Household financial savings on a downtrend



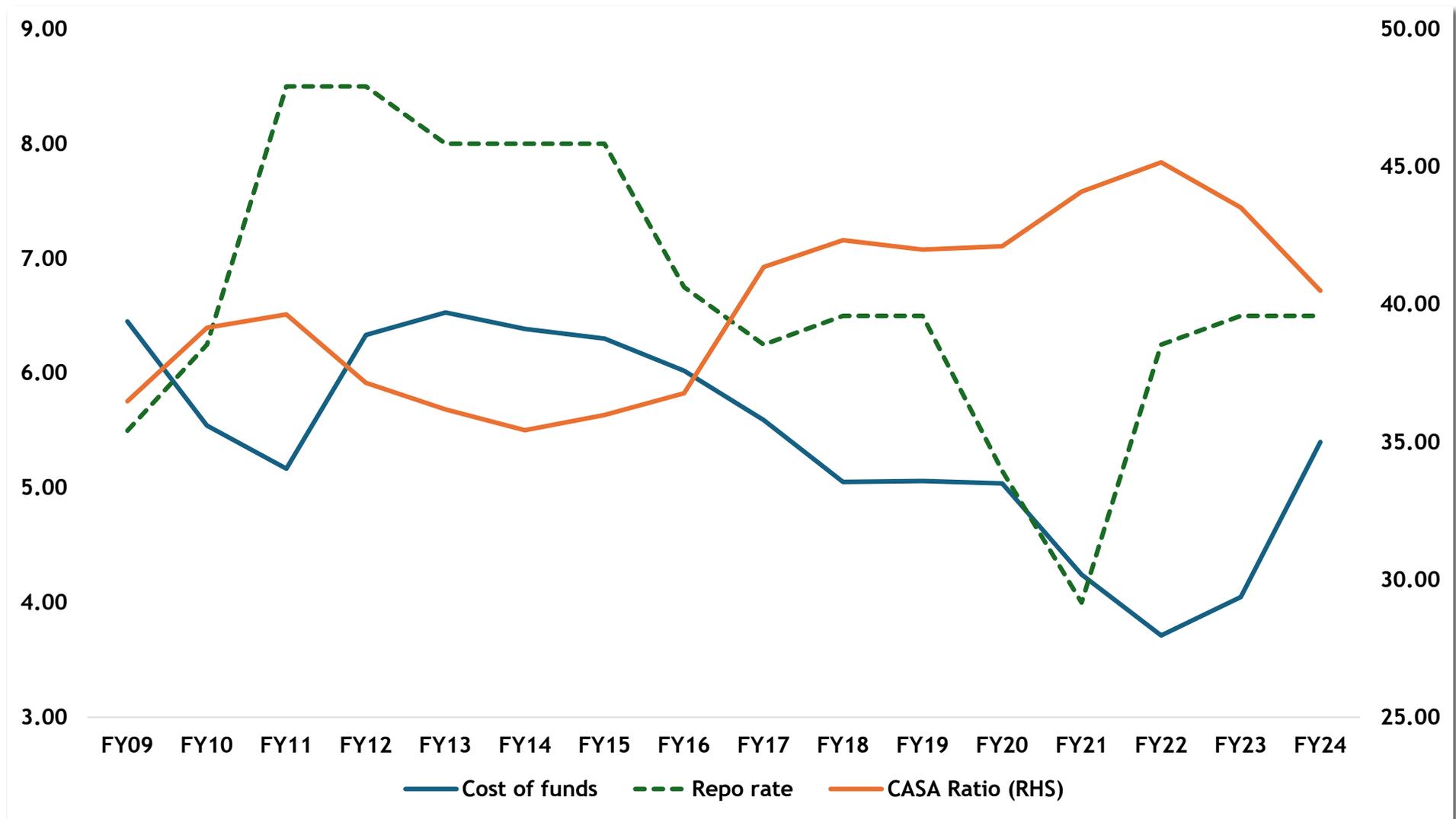
## Mutual Funds has seen record flows clocked in FY25 (Rs. Crore)



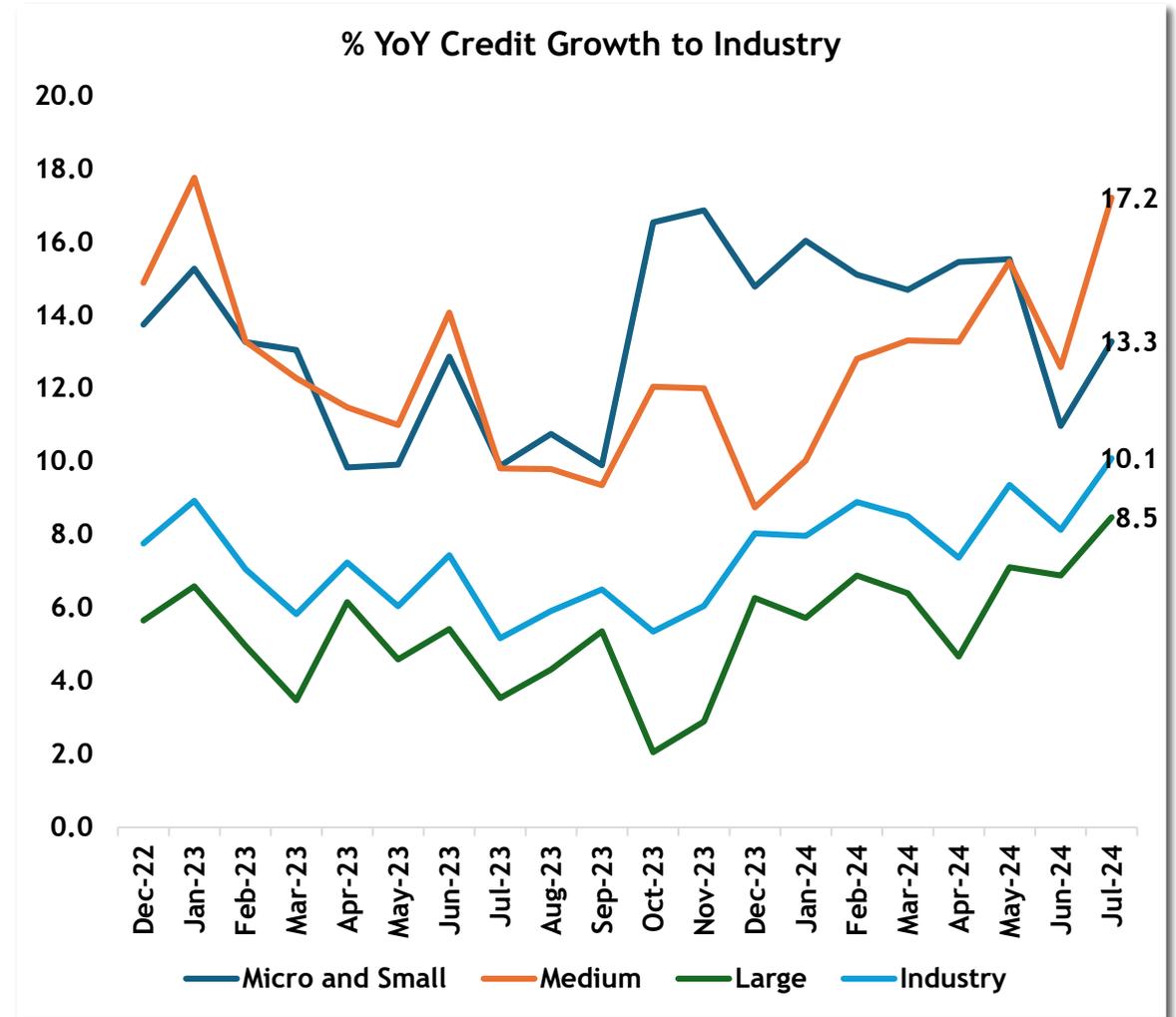
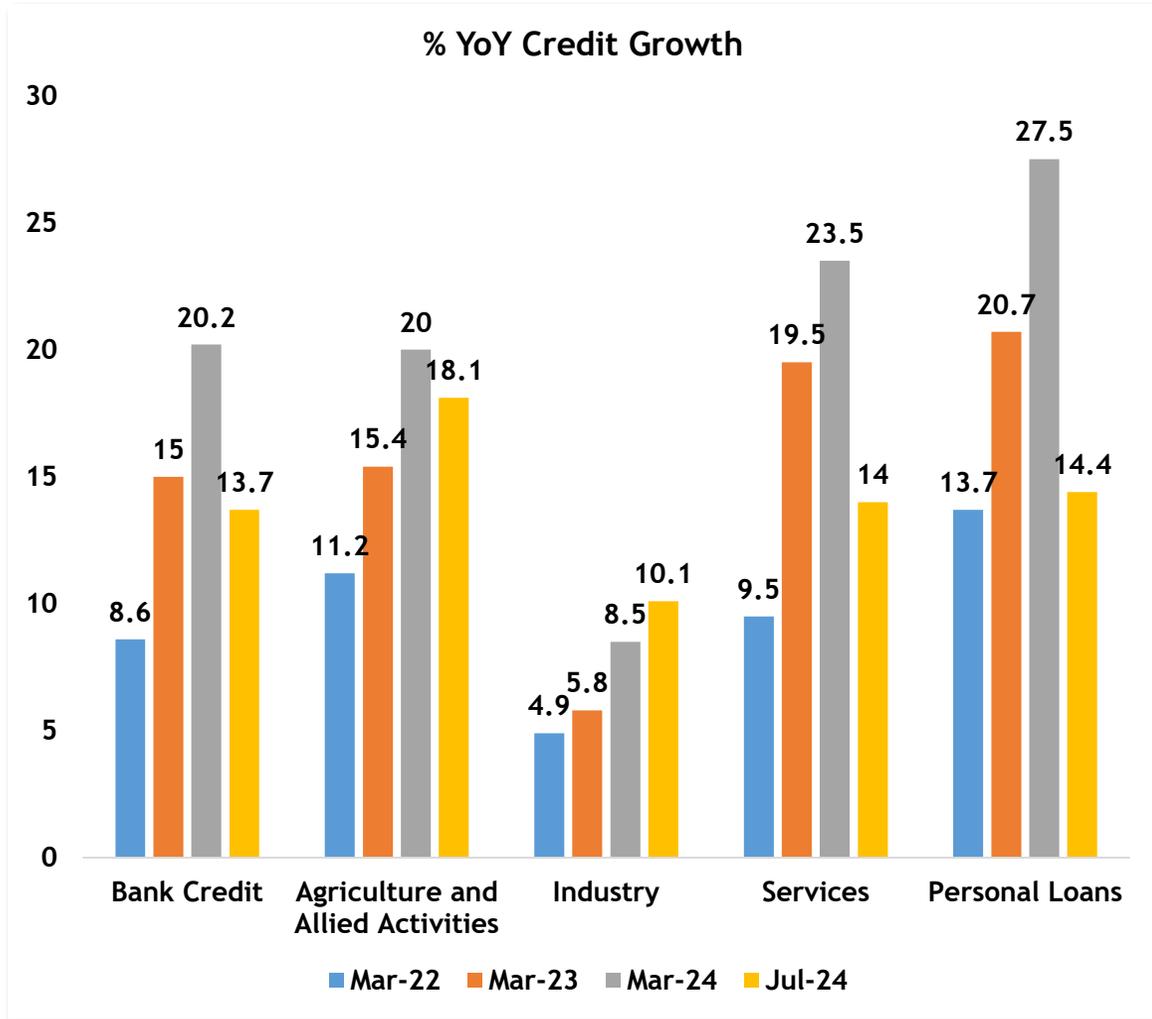
Data for 2024-25 is up to July-24; Source: RBI, CEIC, AMFI, UBI Research



# Cost of deposits trending higher on falling CASA ratio



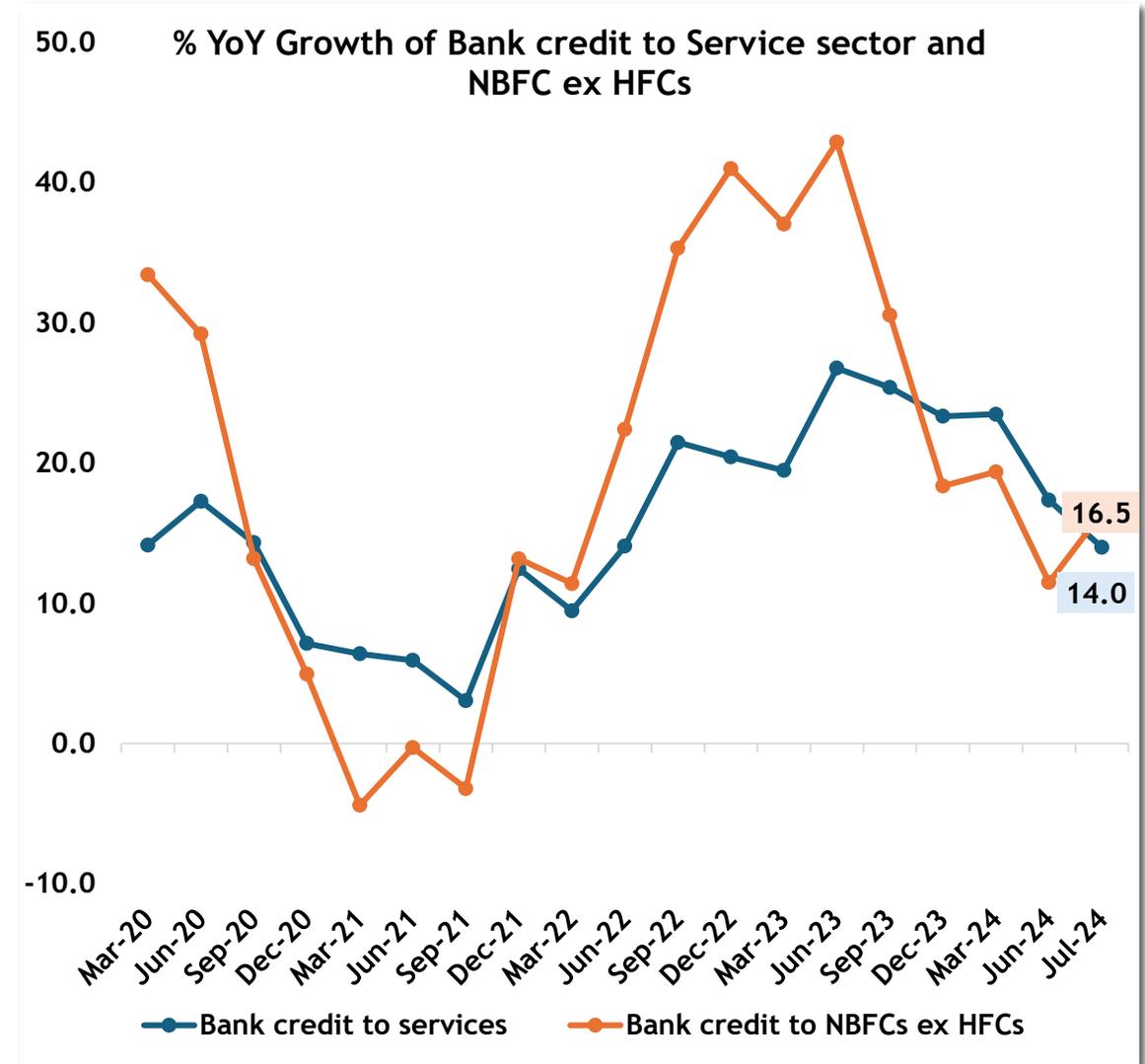
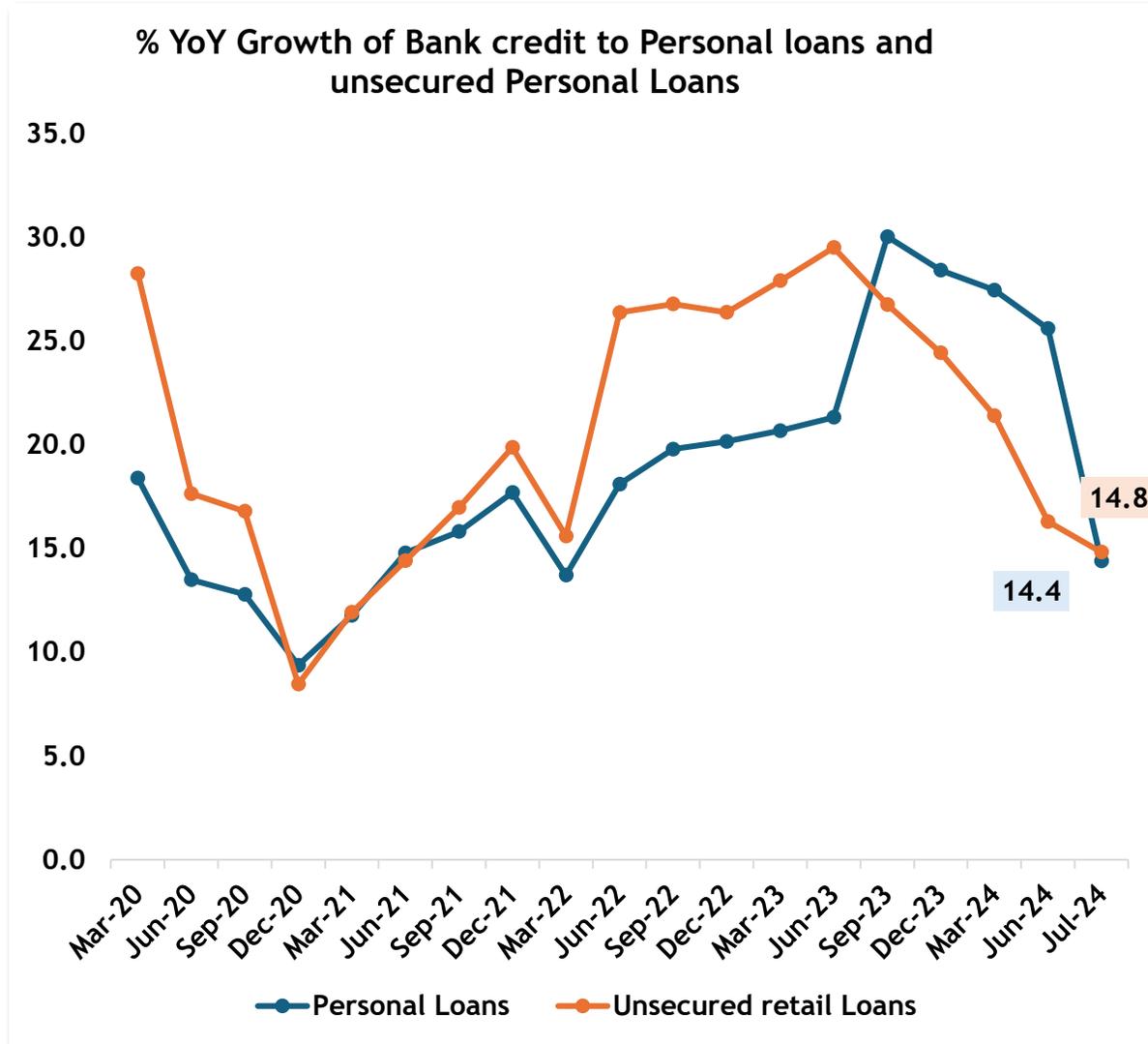
**Credit story - where the real action is residing**

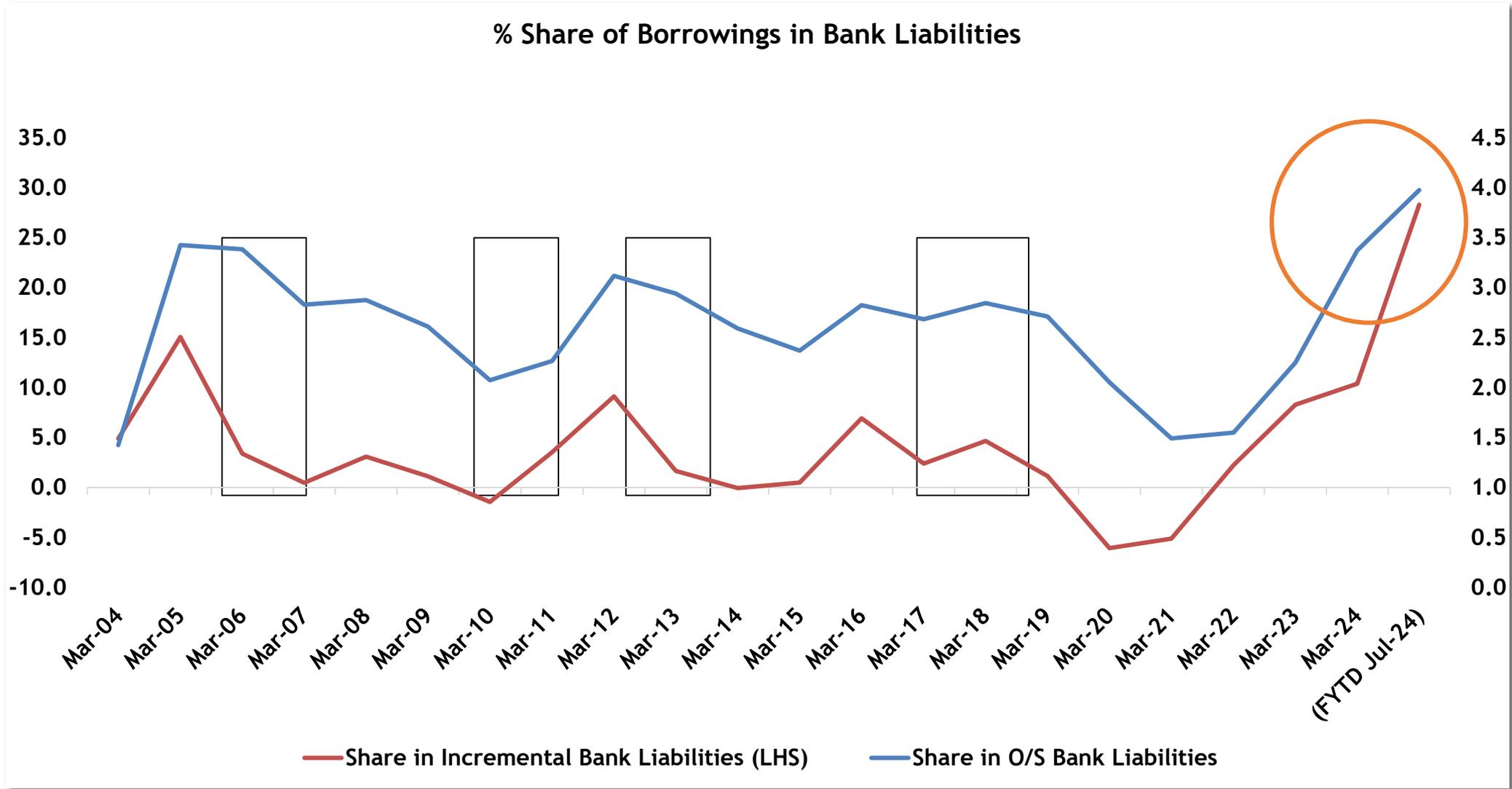


- While the RBI Governor may have shifted market focus towards deposits, the central bank has been taking consistent steps towards lowering the C-D ratio via cooling the credit momentum in the economy, as enlisted in the table below:

Period	RBI action
<a href="#">Nov-2023</a>	Increased regulatory requirements for unsecured retail and NBFC ex HFC loans
<a href="#">Mar-2024</a>	RBI directs JM Financial to stop financing against shares, debentures
<a href="#">Mar-2024</a>	RBI orders immediate ban on IIFL Finance from sanctioning, disbursing gold loans
<a href="#">June-2024</a>	Bank Boards asked to assess “persisting gap between credit and deposit growth rates ”
<a href="#">May-2024</a>	RBI proposes tighter project finance rules
<a href="#">July-2024</a>	LCR requirements proposed to be raised esp. on retail deposits
<a href="#">Aug-2024</a>	Governor mentioned about concerns around “top up” home and gold loans

# Bank Credit growth to unsecured retail & NBFCs ex HFCs has slipped in FY25 with RBI steps bearing fruit





Transmission in this cycle is lagging in market rates forcing banks to keep lending rates low

(in bps)	Repo rate	10yr G sec	5yr AAA rated Corp bond	WADTDR o/s deposits	WALR fresh Rupee Loans	WALR o/s loans	1 yr median MCLR
April 2012 to May 2013	-125	-71	-84			-44	
Sep 2013 to Jan 2014	75	58	23	-6		-1	
Jan 2015 to Aug 17	-200	-134	-148	-199	-203	-136	
Jun 2018 to Aug 2018	50	-11	-7	6	27	7	22
Feb 2019 to May 2020	-250	-161	-217	-91	-166	-61	-115
May 2022 till date	250	<b>-20</b>	<b>76</b>	189	189	117	<b>165</b>

# C-D growth convergence likely to be achieved in FY25 via fall in credit growth

Identifying Period				Credit Growth			Deposit Growth		
Start Month	End Month	Number of Months	Average growth gap: Credit Deposit (bps)	Peak of credit growth during that period (y-o-y percent)	credit growth after 12 Months after end month (y-o-y percent)	Change in Credit Growth (bps)	Deposit growth in the month when credit growth peaked (y-o-y percent)	Deposit growth after 12 Months after end month (y-o-y percent)	Change in Deposit Growth (bps)
Apr-04	Jun-07	39	1071	36	26	-961	20	22	232
Apr-10	Oct-13	43	332	24	11	-1382	17	11	-555
Nov-17	Aug-19	22	432	15	6	-958	9	11	173
Apr-22	May-24	26	408	17			13		

- Episodes of credit deposit growth divergence have happened in the past. This cycle is exacerbated due to the merger of non-bank in Bank.
- Average duration of these episodes would last for 22-43 months according to RBI Financial Stability Report (FSR) for June 2024.
- As per previous cycles, the CD ratio is near to its peak and convergence will start through fall in the credit growth.

Year	Incremental CD ratio	Deposit	Credit	Incremental deposit	Incremental credit
Unit		% y/y		Rs. Lakh cr	
FY22	69.7	8.9	8.6	13.5	9.4
FY23	113.0	9.6	15.0	15.8	17.8
FY24*	95.9	12.9	16.3	23.2	22.3
FY25 (F)	85.0	12.0	12.0-13.0	24.6	20.9

Our assumptions in line with RBI's stance

What would be the optimal credit growth for the system for FY25?

Assuming deposit growth remains steady at 12% while incremental loan to deposit ratio eases to 85% from around 95% last year, credit growth would likely slip to 12.0-13.0% in FY 25 from 16% last year.

\*excluding HDFC merger effect; Source: RBI, UBI Research

# Thank You !

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