(BN) First Savings Drop Since 1999 Limits Rate-Cut Room: India C redit

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By Jeanette Rodrigues

Jan. 16 (Bloomberg) -- Bank deposits in India fell for the first time in at least 14 years as investors sought higher returns in gold or bonds, limiting lenders' ability to reduce interest rates as the central bank eases monetary policy.

Deposits declined 0.4 percent to 64.8 trillion rupees ($1.2 trillion) in the quarter ended Dec. 28 from the preceding three months, the first drop in Reserve Bank of India data going back to at least March 1999. State Bank of India, the nation's biggest lender, pays 7.50 percent on six-month deposits, while inflation averaged 7.54 percent last year. Gold futures advanced 13 percent in 2012, while rupee-denominated debt returned 10.6 percent, HSBC Holdings Plc indexes show.

"There are fewer incentives for savers as the returns are not favorable compared with other assets, especially gold," N. Srinivasan Venkatesh, Mumbai-based head of treasury at state-run IDBI Bank Ltd., said in a Jan. 14 telephone interview. "If deposit growth stays sluggish, monetary transmission will become weak and make it difficult for bank rates to come down."

Bets the central bank will cut borrowing costs this month helped drive the BSE India Sensitive Index of stocks above 20,000 for the first time in two years yesterday. Inflation in Asia's third-largest economy remains the fastest among the four largest emerging markets, stoked by bottlenecks and a 6.2 percent drop in the rupee in the past 12 months.

'Inflation Sticky'

"Inflation remains sticky," Harihar Krishnamoorthy, Mumbai-based treasurer at the Indian unit of FirstRand Ltd., South Africa's second-largest financial services provider, wrote in a Jan. 11 e-mail. "Thus it's unclear whether there could be space for larger policy cuts, especially in the light of deposit growth lagging advances in the banking sector."

While gains in the benchmark wholesale price Index slowed for the third straight month to 7.18 percent in December, official data showed Jan. 14, they have exceeded 7 percent since December 2009. Consumer prices accelerated for the third month in December to 10.56 percent, compared with increases of 5.84 percent in Brazil, 6.6 percent in Russia and 2.5 percent in China.

RBI Governor Duvvuri Subbarao said yesterday inflation remains "quite high" and policy makers lack room for stimulus measures. Economic growth remains a concern, and India will be lucky if gross domestic product expands 5.5 percent in the year to March 31, he told management students in the northern Indian city of Lucknow. That would be the slowest pace in a decade.

The central bank will lower its benchmark repurchase rate by 25 basis points, or 0.25 percentage point, to 7.75 percent at its Jan. 29 policy review, nine of 11 analysts said in a Bloomberg News survey last week.

Credit-Deposit Ratio

Venkatesh of IDBI, which had 2.1 trillion rupees of deposits as of March 31, said a 50 basis point repurchase-rate cut may translate into a 10 basis-point drop in banks' lending rates, because lower savings are contributing to a cash squeeze.

The so-called credit-deposit ratio rose to a nine-month high of 77.61 as of Dec. 28, central bank data show, indicating loan growth is outstripping savings. A slowdown in government spending has also contributed to the crunch, according to IndusInd Bank Ltd.

India had a cash surplus of 1.3 trillion rupees earlier this month after the finance ministry clamped down on allocations to other ministries, according to a government official with knowledge of the matter. A 33 percent spending cap on government projects will be enforced in the quarter ending March, the ministry said in a statement yesterday.

'Last Resort'

"Bank deposits are now the investments of last resort due to the low yield," J. Moses Harding, executive vice president at IndusInd Bank in Mumbai, said in a Jan. 14 telephone interview. "Deposit growth should stay sluggish for the next few months, but things should look up when the new fiscal year starts and the government resumes spending."

The drop in deposits has left banks with less cash to invest in sovereign bonds, even as individual investors pump money into debt. Lenders cut holdings of the notes by 73 billion rupees, or 0.4 percent, last quarter, the first decrease since the three months through December 2010, RBI data show.

The yield on benchmark 10-year government bonds slid 52 basis points in 2012 as local asset managers investing in debt took in 724 billion rupees in the first nine months of the fiscal year that began April 1, compared with outflows of 59.3 billion rupees a year earlier, data from the Association of Mutual Funds in India show. The increase was 229 billion rupees in the October-December period.

Gold Purchases

The 10-year yield has fallen 18 basis points this month.
The rate rose four basis points to 7.87 percent today, according to data compiled by Bloomberg. The rupee weakened 0.3 percent to
54.7925 per dollar today and gold futures rose 0.2 percent today to 30,917 rupees per 10 grams. The contracts touched a record
32,464 rupees on Nov. 26.

The value of gold bars and coins purchased by Indians rose
8 percent to $4.6 billion in the quarter ended Sept. 30 from a year earlier, the latest data from the World Gold Council shows.

The cost of insuring using five-year credit-default swaps the debt of government-controlled State Bank, considered a proxy for the sovereign by some investors, slid 21 basis points this year to 205 on Jan. 15, according to data provider CMA, which is owned by McGraw-Hill Cos. The swaps, which fell 169 basis points in 2012, pay the buyer face value in exchange for the underlying securities or the cash equivalent should a borrower fail to adhere to its debt agreements.

"We are seeing low deposit growth as inflation is still elevated and there is heavy gold buying," Indranil Pan, chief economist at Kotak Mahindra Bank Ltd. in Mumbai, said in a Jan.
14 telephone interview. "The RBI may not be able to cut rates too drastically given the need to mobilize deposits."

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