Banks See Worst Deposit Crunch in 20 Years

Source: LM

Why in News?

A recently released report revealed that despite **robust** credit growth, Indian banks faced difficulty in garnering deposits in 2023-24, resulting in the **highest credit-deposit ratio** in at least **two decades.**

What is the Deposit Crunch?

- **About:**
  - **Indian banks** are grappling with a severe deposit cash crunch that has not been witnessed in the past two decades.
  - Currently standing at 80%, the credit-deposit ratio is at its **highest** since 2015.
    - The **CD ratio** indicates how much of a bank's deposit base is being **utilized for loans.**
- **Deposit Cash Crunch:**
  - A deposit cash crunch occurs when banks have **insufficient funds** on hand to lend to their customers.
  - As a result, businesses face challenges in operating smoothly, and employees may experience delays in receiving their salaries.
  - This **ripple effect** can disrupt economic stability and financial well-being.
- **Reasons for the Deposit Crunch:**
  - Investors are increasingly pursuing high-return, **equity-linked products** due to strong market performance and growing financial awareness, presenting banks with the **dual challenge of attracting deposits and supporting credit growth.**
  - A portion of mobilised deposits is also set aside for regulatory requirements such as **cash reserve ratio (CRR)** and **statutory liquidity ratio (SLR)**, reducing lendable funds and intensifying competition for deposits.
  - In recent quarters, banks used their surplus **SLR holdings to boost credit growth amid slower deposit growth,** but as SLR buffers shrink, they face the challenge of balancing deposit rate hikes with profitability.
  - Banks raised deposit rates last fiscal to attract retail deposits amidst rising competition, alternative investment options, and a **shift toward real assets.**
  - The **merger** of **HDFC and HDFC Bank** resulted in the incorporation of HDFC's loans and deposits into the banking system, contributing to the overall figures.
- **Implications:**
  - A high CD ratio **increases a bank's dependence** on costly, large deposits, which may not be from its core depositors, potentially leading to **liquidity risks** due to higher outflows.
  - Businesses may face liquidity challenges due to **limited access** to credit.
  - Workers' salaries could be delayed, affecting their livelihoods.
  - The overall economic impact may be significant, **necessitating urgent measures** to stabilise the banking sector.
- **Solutions:**
  - The worst deposit crunch in nearly 20 years demands immediate attention and strategic interventions.
  - As India navigates this challenging phase, safeguarding our banks and ensuring financial

stability remains paramount.
- The **RBI** and banks must collaborate to find solutions.
- Encouraging higher deposits and **managing loan disbursements** effectively are crucial steps.
- **Public awareness** about the severity of the crisis can drive collective efforts to safeguard our banking system.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims:

Q. Consider the following statements: (2018)

1. The Reserve Bank of India manages and services Government of India Securities but not any State Government Securities.
2. Treasury bills are issued by the Government of India and there are no treasury bills issued by the State Governments
3. Treasury bills offer are issued at a discount from the par value.

Which of the statements given above is/are correct?

(a) 1 and 2 only
(b) 3 only
(c) 2 and 3 only
(d) 1, 2 and 3

Ans: (c)