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CREDIT RATING AGENCY

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IMPROVING LIQUIDITY, FALLING CDs - APRIL 2024

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Introduction

CDs issued by various banks are a function of multiple factors. Such factors include the liquidity position of banks; the asset-liability mismatches, particularly in some buckets; competitively priced funds in other liability instruments; credit demand; the cash availability in the system; and the pressure on profits and profitability. Hence this aspect needs to be looked at holistically for a comprehensive assessment and perspective. This is why Treasury officials of most banks meet the top management at the start of the day and decide the quantum and pricing of the CDs to be taken depending on the position of the individual bank and the larger banking system. This system has generally been working well.

System liquidity deficit — as measured by net injections under the liquidity adjustment facility (LAF) — declined to ₹1 trillion during February-March 2024 compared with ₹1.61 trillion in December 2023- January 2024.

During March 2024, CDs of the value of ₹1.2 lakh crore were issued by banks as against only ₹19,850 crore in April (till April 2021). There is pressure on banks to bolster their balance sheets and reach the targeted business levels in March. Hence a correction from the high base of March is not all that surprising.

There was pressure on liquidity in March 2024 but this pressure eased in April 2024 for various reasons explained above with the result that liquidity surplus in the second week of April reached ₹ 80,000 crore. There were also liquidity infusing factors, such as, government spending, maturity of forex swap and buoyant foreign portfolio flows.

Liquidity in the banking system has eased considerably after March 2024 after staying in deficit mostly since November 2023. Apart from cyclical factors, government spending, maturity of forex swap and buoyant foreign portfolio flows contributed to swelling liquidity conditions.

During FY 24, the RBI took a slew of stern regulatory action against JM Financial, Paytm, Bajaj Finance, Mahindra & Mahindra and HDFC Bank. Hence, because of these and other factors, credit growth could dip from 16 per cent in FY 24 to 13.5 per cent in FY 25.

This is an evolving situation and needs to be monitored carefully for prudent and effective financial management.