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EDITORIAL ANALYSIS

India's Financial System Imbalance — Credit Growth Constrained Despite Ample Liquidity

 **BUSINESS STANDARD**

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SUBJECTS COVERED**ECONOMY****GS PAPERS****GS3****CURATED & WRITTEN BY****Bharat Choudhary**

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Business Standard

24 March 2026

GS3

BS

Business Standard

MAINS RELEVANCE:

GS Paper 3



INTERVIEW ANGLE

"If Indians are increasingly investing in equities rather than bank deposits, what are the systemic risks for credit availability and financial stability?"

India's Financial System Imbalance — Credit Growth Constrained Despite Ample Liquidity

Business Standard's opinion piece highlights a structural imbalance in India's financial system: credit growth is constrained despite ample systemic liquidity, as household savings increasingly move from bank deposits to equity markets, leaving banks struggling to mobilise the deposits needed to fund loan growth.

THE CORE PROBLEM

India's banking system faces a paradox:

- **RBI has injected liquidity** through OMOs, VRR auctions, and CRR cuts
- **Credit demand is robust** — corporates and retail borrowers want loans
- **But deposit growth is lagging** — households are redirecting savings to equity markets, mutual funds, and alternative investments

The Numbers

INDICATOR	VALUE (2025-26)
Bank credit growth	~12-14%
Deposit growth	~8-10%
Credit-Deposit ratio	~80%+ (historically ~72-75%)
Household financial savings rate	Declining (from 11.5% to ~5.1% of GDP)
Mutual fund AUM	Rs 72+ lakh crore
Demat accounts	18+ crore

The **credit-deposit gap** — where credit grows faster than deposits — creates a structural funding problem for banks.

WHY DEPOSITS ARE SLOWING

The Equity Shift

- **Mutual fund SIPs:** Rs 25,000+ crore/month flowing into equity mutual funds
- **Direct equity:** Over 18 crore demat accounts (up from 4 crore in 2020)
- **Insurance-linked investments:** ULIPs and endowment policies
- **Gold and real estate:** Traditional alternatives to bank deposits

Low Real Returns on Deposits

- Bank FD rates: 6.5-7.5%
- Post-tax returns (30% bracket): ~4.5-5.25%
- CPI inflation: ~5%
- **Real return on FDs: Near zero or negative**
- Equity returns (Nifty 50, 3-year CAGR): ~12-15%

Rational investors are moving to higher-return instruments.

Demographic Shift

- Younger investors (under 35) prefer **SIPs and stocks** over FDs
- Digital platforms (Zerodha, Groww, Upstox) have democratised equity investing
- Financial literacy campaigns have promoted equity as a long-term wealth builder

THE SYSTEMIC RISK

For Banks

- **Higher cost of funds:** Banks must offer higher FD rates to attract deposits, squeezing margins
- **Dependence on wholesale funding:** Banks turn to Certificate of Deposits (CDs) and inter-bank borrowing — costlier and more volatile
- **Credit rationing:** Banks may slow lending if deposits do not catch up

For the Economy

- **MSME credit crunch:** Small businesses depend on bank loans (not bond markets)
- **Infrastructure financing gap:** Long-term projects need stable deposit base
- **Transmission breakdown:** RBI rate cuts may not translate to lower lending rates if banks face deposit scarcity

For Financial Stability

- **Asset-Liability Mismatch (ALM):** Long-term loans funded by short-term wholesale borrowing
- **Concentration risk:** If equity markets correct sharply, household wealth erodes and consumption crashes
- **Moral hazard:** Banks chase risky borrowers to maintain margins

WHAT THE RBI CAN DO

MEASURE	STATUS
CRR cut	Already reduced from 4.5% to 4% (released ~Rs 1.16 lakh crore)
OMO purchases	Ongoing — buying government securities to inject liquidity
Repo rate cut	February 2026: Cut 25 bps to 6.25%
ICRR	Infrastructure Credit Regulatory Relaxation — under discussion
Long-term refinance	TLTRO-like operations possible if needed

However, the editorial notes that **monetary tools cannot solve a structural savings behaviour shift**. The problem is not liquidity scarcity — it is deposit scarcity.

INTERNATIONAL COMPARISON

COUNTRY	HOUSEHOLD SAVINGS IN BANK DEPOSITS
Japan	~52% of financial assets
Germany	~40%
India (2020)	~35%
India (2025)	~25% (declining rapidly)
USA	~13% (but deep bond/equity markets compensate)

The editorial cautions that India does not yet have the deep corporate bond market that allows the US to bypass bank intermediation.

THE WAY FORWARD

- ① **Develop the corporate bond market** — reduce dependence on bank credit for large corporates
- ② **Tax parity** — make long-term FD returns competitive with equity LTCG treatment
- ③ **Inflation-indexed deposits** — protect savers from real value erosion
- ④ **Regulatory framework for deposit insurance** — DICGC limit raised from Rs 1 lakh to Rs 5 lakh (2020), but awareness remains low
- ⑤ **MSME credit guarantee expansion** — CGTMSE and ECLGS-type programmes

UPSC RELEVANCE

Credit-Deposit ratio, CRR, OMO, DICGC, repo rate, TLTRO

MAINS GS-III:

Banking sector reforms, monetary policy transmission, household savings patterns, financial inclusion

INTERVIEW:

Is India's equity market boom a sign of financial maturity or a systemic risk?

★ FACTS CORNER — KNOWLEDGEPEDIA

BANKING SYSTEM DATA:

Credit-Deposit ratio: ~80%+ (historically 72-75%)

Bank credit growth: ~12-14% (2025-26)

Deposit growth: ~8-10% (2025-26)

CRR: 4% (cut from 4.5%)

Repo rate: 6.25% (cut 25 bps in Feb 2026)

HOUSEHOLD SAVINGS:

Financial savings: Declining from 11.5% to ~5.1% of GDP

Mutual fund AUM: Rs 72+ lakh crore

Monthly SIP inflows: Rs 25,000+ crore

Demat accounts: 18+ crore (up from 4 crore in 2020)

RBI TOOLS:

CRR: Cash Reserve Ratio (funds locked with RBI, no interest)

SLR: Statutory Liquidity Ratio (government securities)

OMO: Open Market Operations (buy/sell govt securities)

Repo rate: Rate at which RBI lends to banks

TLTRO: Targeted Long-Term Repo Operations

OTHER RELEVANT FACTS:

DICGC: Deposit Insurance and Credit Guarantee Corporation

Deposit insurance limit: Rs 5 lakh per depositor per bank (since 2020)

CGTMSE: Credit Guarantee Fund Trust for Micro and Small Enterprises

India's corporate bond market: ~18% of GDP (vs 80%+ in US)

NPA ratio (gross): ~3% (lowest in a decade)

Sources: [Business Standard](#), [RBI](#)

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