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Short-Term Instruments: Lock your funds now

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In a move that will bring down interest earning for investors of small saving instruments, the government, on Tuesday, announced to reduce interest rates on some small savings schemes by 25 basis points. It also decided to align interest rates on several small saving schemes with government securities to be recalibrated on a quarterly basis.

Experts say that a decision to cut interest earning on popular small saving schemes will not only reduce the interest earning on such schemes but will also result into a reduction in interest offering by the banks.

“Since the cut in interest rates is mostly in shorter-term deposits ranging up to 3 years, it will lead to a reduction in deposit rates by banks and so bring down the interest income for investors,” said Vishal Dhawan, founder, Plan Ahead Wealth Advisors. He thus suggested that investors looking to deposit their money in shorter term debt instruments should lock their funds now into those products as a cut in rates from banks may come anytime.

The investors will also see a shift in their interest earning on a quarterly basis as the govt has also decided to align the interest rate for several small saving schemes with G-Sec that will be adjusted every three months. As a result of this, if the interest income for investors of those schemes will go up in a rising interest rate scenario, they will see a fall in their interest income during the year if rates fall.

“While in a rising interest rate environment it is good for investors, it will be negative in a falling rate environment. However, in the longer term it should be neutral,” said Dhawan.

On Tuesday, the government said that only for instruments such as, term-deposits of 1, 2 and 3 year, KVPs and 5-year recurring deposits, the rates will get aligned with G-Secs.