Should you invest in bank FDs now?

An investor can earn better yields from shorter term debt funds, tax-free bonds, small savings schemes, floating rate instruments, and high quality corporate deposits compared to FDs.
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The rate hike cycle which started for India in May 2022 continued as the central bank raised rates by 0.5 percent in the last Monetary Policy Committee (MPC) meeting.
This has largely been driven by the fact that the inflation does not seem transitory, just like in the rest of the world. Thus, the RBI has raised interest rates by almost 1.9 percent in a short period, though only about 0.5-0.75 percent has been passed on by banks to fixed deposit (FD) investors thus far. As there was sufficient liquidity available in the system, bankers did not feel the need to lure investors by raising deposit rates much.
The recent drop in liquidity and increased credit demand could mean that more hikes in FD rates may bring some cheer to investors soon, though they may still need to view deposits through the lens of real returns, that is, returns post inflation.

The Reserve Bank of India's (RBI) inflation projections were around 6.7 percent for the year 22-23, while the rates for FDs of 3-5 year tenor are in range of 5.5-6.5 percent, indicating that the average FD investor continues to lose money, net of inflation. On top of that, FD interest income is taxable. Therefore, both inflation and taxation eat into the gross returns.

One should therefore reflect on whether there is merit in investing in bank FDs even as rates are going up, leaving aside some monies parked there for contingencies.

This brings us to the other question: what does an investor do to maintain returns which are ahead of the inflation, and also tax efficient.

Some ideas

Look for tax friendly incomes / products like debt mutual funds (MF) and tax-free bonds. Short term debt MFs like low duration funds and ultra-short term duration funds have started looking attractive as rate hikes have improved the yields of their portfolios.
They invest in bonds which mature in the shorter term. This helps them invest their proceeds at a higher investment rate on maturity. Thus, an investor can earn better yields from shorter term debt funds compared to FDs, when making short term investment decisions.

These funds also have an indexation benefit if held for more than three years, and therefore attract lesser tax as they are then taxed at long term capital gains (LTCG) rates, which can be lower than the tax slab for higher income investors. FD income has no such benefit.

Hold-to-maturity debt funds or target maturity debt funds can also be considered, which hold bonds that align to a target maturity date of the scheme. These are passive funds, which means they largely buy and hold bonds and do not have high portfolio turnovers. This helps reduce the cost of the portfolio.
Avail of the higher small savings rates still available: products like the Public Provident Fund (PPF), post office schemes, the National Savings Certificate (NSC), the Kisan Vikas Patra (KVP), etc., are available at

better rates than FDs. If you are comfortable with the lock-ins and possible issues with customer service on some of these products, then you can avail of these.
Consider floating rate instruments such as the government of India's taxable bonds issued in 2020 with a yield of 7.15 percent per annum over seven years. Since these are floating rate bonds, the rate — linked to prevailing NSC rates plus 0.35 percent — is expected to be reset every six months. In a rising rate scenario, this may be beneficial.

Senior citizens, of course, have other options as well, which can be explored. Other investors may consider high quality corporate deposits. All in all, higher interest rates have made multiple products more attractive than they were. How they fit into your portfolio to deliver the appropriate outcomes for you should be well thought through.

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