

9.5% interest on FDs in small finance banks: How to invest in fixed deposits 'safely' to get best return

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Synopsis

Small finance banks are offering as high as 9.5 per cent interest rate on fixed deposits. Should you go book an FD in a small finance bank to get sky-high return? Here are the key things you need to check while booking a fixed deposit in small finance banks



Rising interest rates have once again made fixed deposits (FD) attractive in the last one year. The Reserve Bank of India (RBI) has increased the repo rate by 250 basis points (bps) since May 2022. In a bid to lure investors, banks have also hiked the interest rates of fixed deposits. Small finance banks are one step ahead. Senior citizens can earn an interest rate of up to 9.5 per cent on fixed deposits maturing in 1001 days in Unity Small Finance Bank. Suryodyay Small Finance Bank offers an interest rate of 8.76 per cent on FDs maturing in 999 days. In short, FD interest rates of small finance banks such as Unity Small Finance Bank, Equitas Small Finance

Bank, Suryodyay Small Finance Bank, Utkarsh Small Finance Bank, and Jana Small Finance Banks are higher than those offered by the public sector and private banks. Should you go book an FD in a small finance bank to get sky-high return?

Here are the key things you need to check while booking a fixed deposit in small finance banks.

Safety matters You might be wary about the safety of your fixed deposit when you opt for a relatively unknown small finance bank such as Unity Small Finance Bank instead of a large commercial bank like SBI, HDFC Bank or ICICI Bank. Small finance banks have limited lending scope and are considered riskier than traditional scheduled commercial banks. Hence, depositors prefer to invest in FDs of the latter. To reward depositors for the extra risk and make their FDs attractive to investors, small finance banks offer higher interest rates than private or public sector banks.

Small finance banks are regulated by RBI just like other banks Do keep in mind that small finance banks are also regulated by the Reserve Bank of India (RBI). "Small finance banks are directly regulated by the RBI since they have been categorised as scheduled banks just like PSUs and other private sector banks by the central bank," said Adhil Shetty, CEO, BankBazaar.com.

Check the track record and financial strength To get some extra return, you should not compromise the safety of your money. Do remember that it is your hard-earned money at the end of the day. "One should also assess the financial health and stability of the bank itself and not just go after the highest or increasing rates," said Dev Ashish, a SEBI Registered Investment Advisor and founder of StableInvestor.com.

"Do research the bank's credibility and reputation in the market to ensure that your investment is safe," said CA Manish P. Hingar, founder of Fintoo, a financial consulting firm. You can also check the bank's credit rating to gauge the level of risk associated with investing in its fixed deposit, he added.

When booking large FDs, you need to be very cautious. When you are planning to book a big FD, you need to be extra careful. "While depositors might be tempted by high-interest rates offered by many banks, especially smaller ones, one should never choose a bank based on the interest rate alone when planning to park large amounts," said Dev Ashish.

How much should you invest in small finance bank FDs? Deposits opened with small finance banks are protected by the deposit insurance program to the tune of Rs 5 lakh. However, it includes both the principal and interest amounts. So, if you want to book a cumulative fixed deposit in a small finance bank, you should invest in a way that the total amount remains within the threshold of Rs 5 lakh at the time of maturity of your deposit. "Having cumulative deposits (including fixed deposits) of up to Rs 5 lakh with each of these small finance banks is as safe as depositing money with PSU and large private sector banks," said Shetty.

How to allocate your FD in small finance banks? Diversify your investment, including your FD exposure, said experts. "Do not overexpose yourself to small finance bank deposits," said Vishal Dhawan, a CFP and founder of Plan Ahead Wealth Advisors.

Ensure that you keep the overall allocation to fixed income in mind while allocating to small finance deposits as well, he added. If you have earmarked a total fund for FDs, do not invest more than 30 to 40 per cent in FDs of small finance banks, said experts.

To make sure you enjoy the Rs 5 lakh insurance cover you can go for multiple smaller FDs in different SFBs. With the same SFB you can go for multiple smaller FDs in different right and capacity such as joint account with spouse and children, as guardian of minor, as a director of a company and so on.

"Spread your fixed deposits across a few banks. Put at least 60 to 80 per cent in RBI-identified systematically important banks (State Bank of India, ICICI Bank, and HDFC Bank). Rest you can park in other smaller banks, which may seem attractive to you as they may be offering higher rates," said Dev Ashish.

FD investment should match your overall investment horizon. While investing in FD, you should take note of your overall investment horizon. Don't book an FD just because it is offering 9.5 per cent interest. The FD tenure that you will select must match your investment goal, said experts.

Do remember to check whether your fixed deposit is callable or non-callable. If you park your money in a non-callable fixed deposit, you will not have an option to prematurely withdraw your deposit. "Understand the penalty charges that may apply if you withdraw your investment before the maturity date, and make sure you are comfortable with it," said Hinger.

"Overall, investing in fixed deposits in small finance banks can be a viable investment option, provided you do your due diligence and make an informed decision," he added.