

HOUSEHOLD DEPOSITS, THEIR SUBSTITUTES, INTEREST RATES, AND THE HOUSEHOLD SAVINGS RATE IN THE ECONOMY

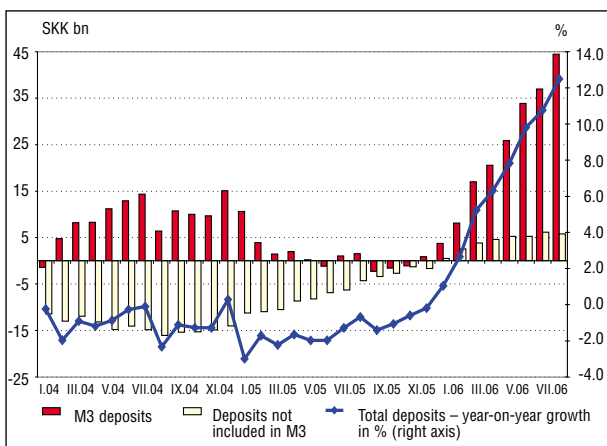
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This year has seen a renewal of interest in household deposits following a long period of decline in this form of saving. The cause of the steady growth in deposits can be viewed at two levels. Deposits are being used to send and receive non-cash payments, and also as a means of saving. In other words, the current increase in deposits is supported by strong economic activity accompanied by positive developments in the labour market and the raising of interest rates by the central bank. This article deals in more detail with these causes, the individual forms of deposits, their development trends, and their substitutes.

Development trends in household deposits

Household deposits were reporting long-term downward trend until 2005, which affected mainly the less liquid deposits not included in the M3 monetary aggregate. As regards the structure of M3 deposits, the only increase reported during this period was in deposits and received loans repayable on demand. The main determinant of this development in the preceding years were relatively low interest rates and the broadening appeal of money market fund shares/units (MMF shares/units) as an alternative form of saving.

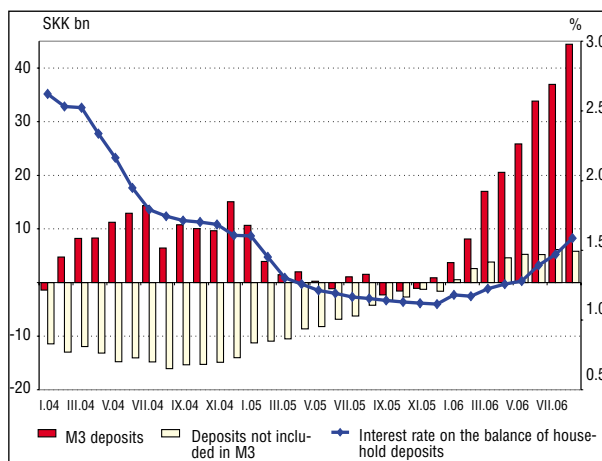
Chart 1 Year-on-year increase in household deposits



Source: NBS.

The development of household deposits turned around at the beginning of 2006. They were still falling in December 2005 (year-on-year decrease by 0.2%), but by August of this year their growth was already relatively sharp (year-on-year growth by 12.5%); the rising trend has affected not only depo-

Chart 2 Increase in deposits and their interest rate



Source: NBS.

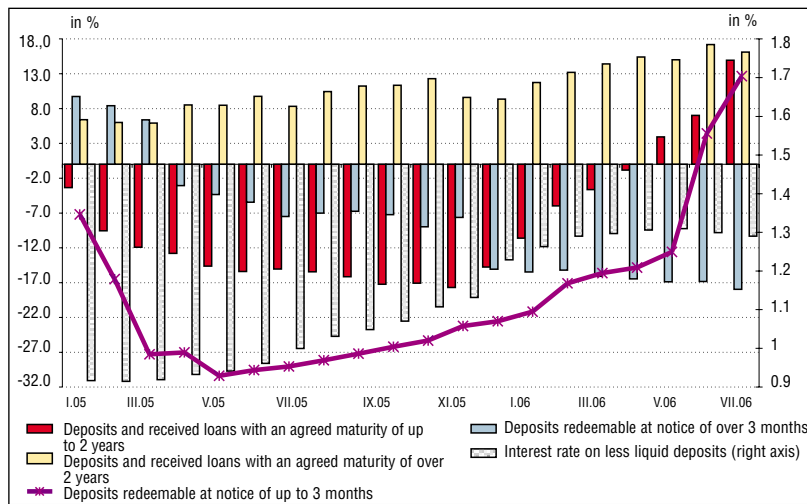
sits repayable on demand, but also less liquid deposits. That includes an increasing volume of household deposits with an agreed maturity of up to 2 years (year-on-year growth by 14.9%) and a steeper rise in deposits with a maturity of more than two years (their average year-on-year growth for the first eight months of 2006 was 14%, compared to 8% for the same period of the previous year).

From the view of time structure, the increase in the individual components of household deposits has reflected the development of clients interest rates¹ and their reaction to the steadily rising base rate of the NBS. The highest rise has been reported in interest rates on medium-term and long-term deposits. This has led to the growth in deposits with an agreed maturity of up to 2 years and more than 2 years, the

¹ Interest rates on new household deposits.

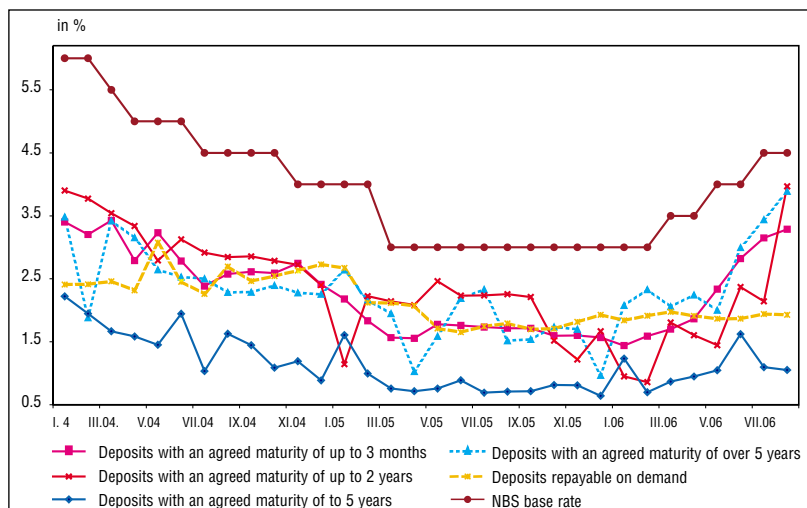


Chart 3 Year-on-year increase in household time deposits and savings deposits



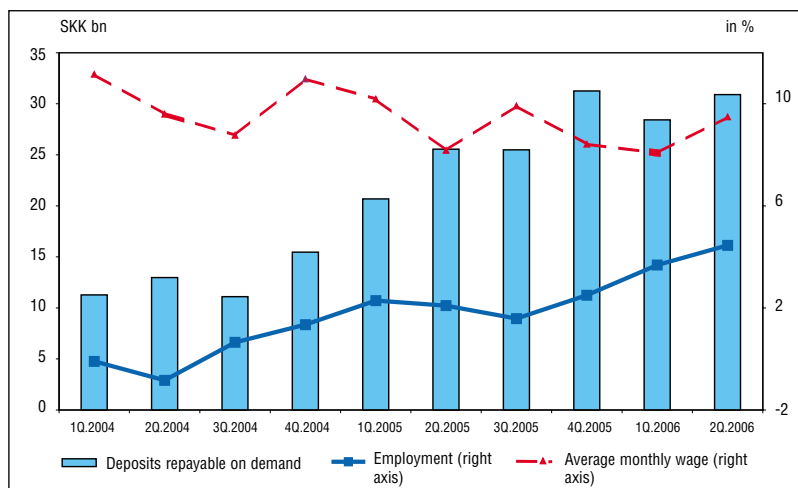
Source: NBS.

Chart 4 Development of interest rates on new household deposits



Source NBS.

Chart 5 Year-on-year increase in household deposits (in SKK billion) and growth in employment (according to a sample survey of the workforce) and in nominal wages (in %)



Source: NBS, Statistical Office of the SR.

rates for which have risen by 2.3 percentage points year-on-year. As rates have climbed since the beginning of the year, so the gap between them and the NBS base rate has narrowed. In 2005, in respect of less liquid deposits, the gap averaged around 1.5 percentage points, and by August 2006 it had decreased to 0.5 of a percentage point.

Household transaction deposits

The substantial increase in household deposits is largely accounted for by overnight deposits, which since 2005 have been recording relatively high year-on-year growth. The initial impulse for the accelerated growth in the most liquid household assets was the small difference in interest on deposits repayable on demand and time deposits. Households therefore sought a higher-earning alternative for their savings or simply left them in current accounts. The increase in household demand deposits has been supported in recent years also by high economic activity, including positive developments in the labour market (growth in both wages and employment).

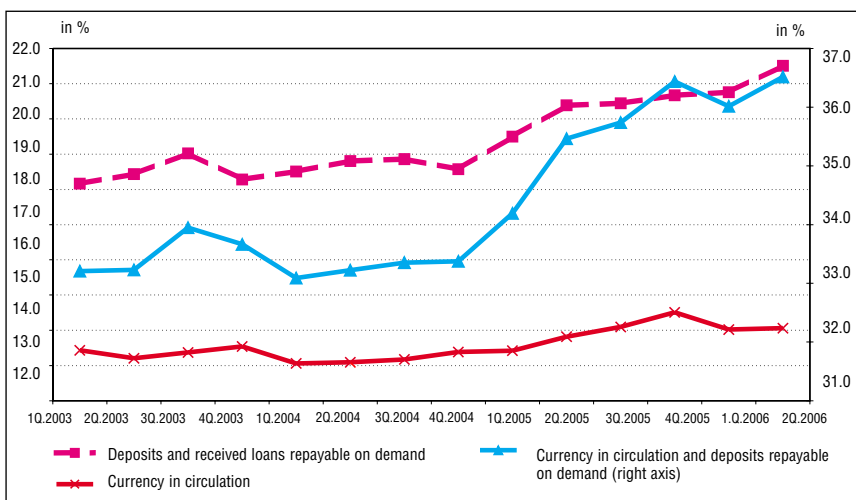
As regards the structure of household deposits, overnight deposits have increased their share while the total volume of deposits has declined. In an environment of relatively low interest rates, the share of currency in circulation and current account deposits in household final consumption have also risen (36.5% in August 2006). The share of deposits repayable on demand has increased more quickly than the share of currency in circulation.

Less liquid household deposits (time and savings deposits)

The low interest rate on time deposits and savings deposits of households resulted in a substantial

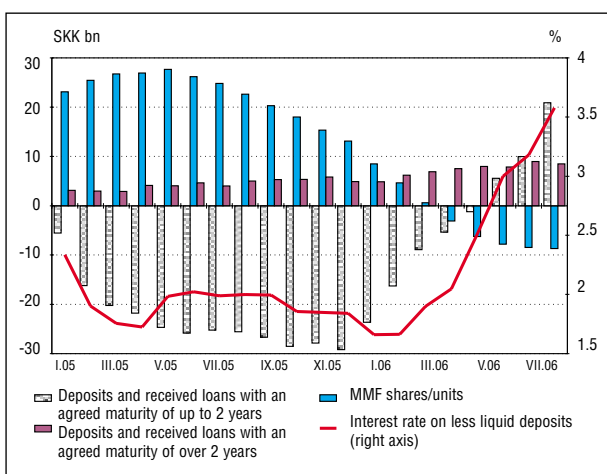


Chart 6 Deposits as a share of household final consumption



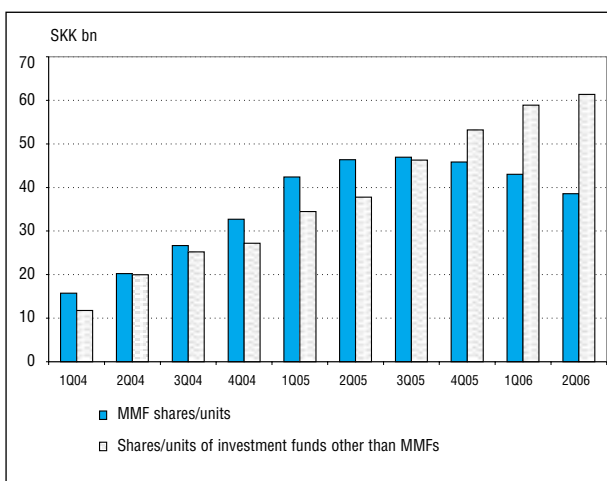
Source: NBS, Statistical Office of the SR.

Chart 7 Year-on-year increases in household deposits



Source: NBS.

Chart 8 Shares/units of investment funds – balances



Source: NBS.

decline in these deposits, especially in 2005. The main substitute for them in this period was investment in investment fund shares/units. As deposit interest rates have increased in 2006, so household deposits and loans with agreed maturities have declined more slowly year-on-year and recently began to increase. When the returns on MMF shares/units became less attractive, there was a partial shifting of household funds back to higher-yielding time deposits. Some of the funds from MMF shares/units have been reinvested in the shares/units of investment

funds other than money market funds (share funds and mixed funds).

As for the structure of less liquid household deposits, the only increase has been in deposits with agreed maturities (time deposits). This applied not only to M3 deposits (with an agreed maturity of up to 2 years), but also to longer-term deposit products. Their growth may to some extent be accounted for by the intensive way in which these products were advertised.

Savings deposits have long been holding back the overall growth in household deposits. These deposits consist largely of household funds deposited in pass-books. Their trend decline is related to the low uptake of this less attractive form of saving (with outdated products).

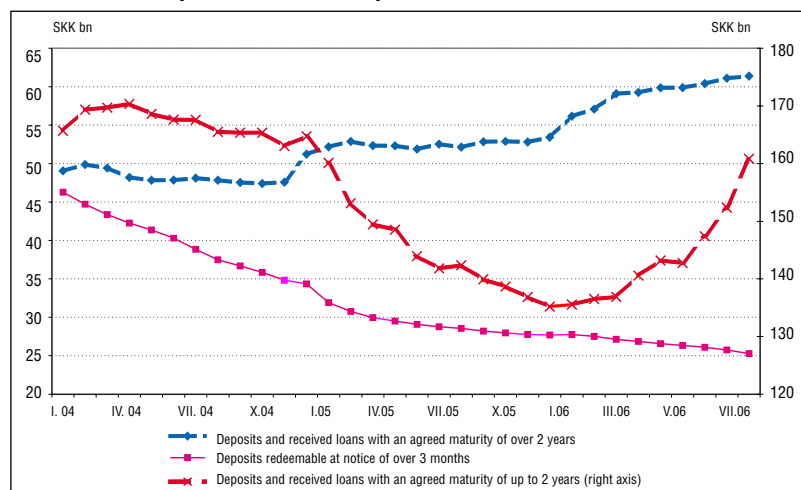
Household savings rate in the economy (deposits and fund shares/units)

The development of household deposits has also affected the ratio of deposits to gross domestic product; this fell by around 10 percentage points from 2003 until the beginning of 2006, since when it has recorded upward trend. The decline in deposits was substituted by higher investment in investment funds (money market and others). But whereas deposits have declined as a share of GDP, the ratio of fund shares/units to GDP has increased. The development of the aggregate ratio (household deposits and fund shares/units) to GDP, in other words the household savings rate in the economy, has been constant with a recent slight increase, reflecting the renewed pace of growth in deposits.

In comparison with the other V4 countries, Slovakia

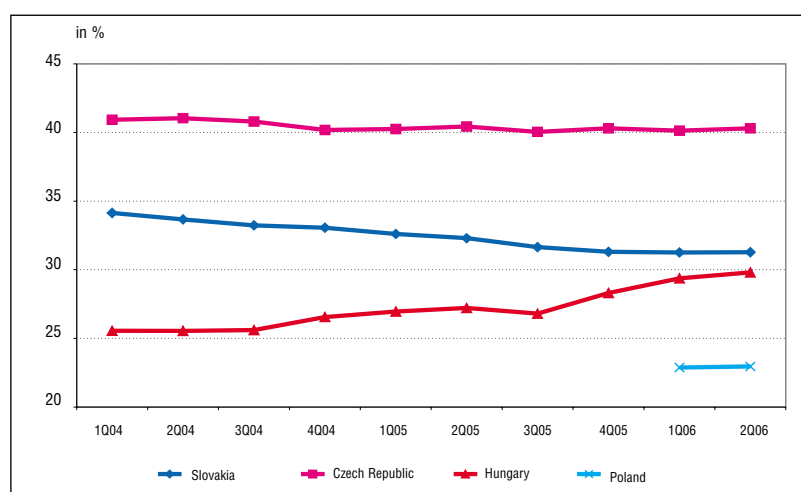


Chart 9 Less liquid household deposits



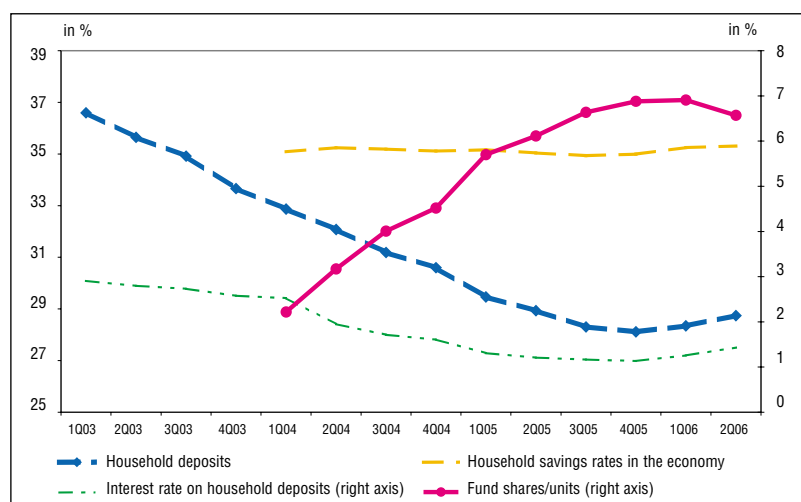
Source: NBS.

Chart 10 Share of household deposits and MMF shares/units in GDP



Source: NBS, Eurostat, websites of national banks.

Chart 11 Share of deposits and fund shares/units in GDP



Note: Fund shares/units represents the sum of MMF shares/units and shares/units in investment funds other than MMFs, reported since 2004.

Source: NBS.

has one of the highest ratios of household deposits (including money market fund shares/units) to GDP. After declining slightly up to and including 2005, this ratio in Slovakia remained stable this year, reflecting the renewal of growth in deposits. The Czech Republic has long had the highest ratio of deposits and MMF shares/units to GDP (approximately 40%), notwithstanding long-time low deposit interest rates.

Conclusion

The development trend of household deposits is undergoing a change. After recording a year-on-year decline in 2005, it began to increase relatively quickly in 2006.

In connection with the continually high economic activity and favourable developments in the labour market, the growth in deposits repayable on demand has increased. Less liquid deposits have reacted to interest rate changes, with clients already seeing rises in the NBS base rate passed on to these deposits. This has also stimulated a renewal of growth in their volume and a shifting of funds back out of MMF shares/units, which were in previous years their most important substitute.

Deposits had not only been moved into MMF shares/units, but also into other investment funds, and so when the ratio of household deposits to GDP was steadily declining (up to 2006), the household savings rate in the economy remained more or less stable.

The ratio of deposits and MMF shares/units to GDP in Slovakia is the second highest among the V4 countries, after the Czech Republic. Its long-term decline came to an end in 2006 with the upsurge of growth in deposits.