smh.com.au
The Sydney Morning Herald
Print this article | Close this window

Where are the great deals on term deposits?

John Kavanagh
February 24, 2010

There are great deals to be had in term deposits and online savings accounts as banks scramble for funds and investors seek safety, writes John Kavanagh.

Heard about the 8 per cent term deposit offer? Didn't get on to it? Too bad, it's gone. Westpac launched an offer of 8 per cent on a five-year term in the middle of December and replaced it with an offer of 7.25 per cent on February 5.

You had to be quick. The best rate in the market now is a Bank of Cyprus offer of 7.85 per cent for five years.

The Westpac offer illustrates two things about the current state of the deposit market: There are some great deals available and the market is very fluid, with lots of special offers.

The chief economist and head of investment strategy at AMP, Shane Oliver, says many private investors may not realise how good those rates are.

"Inflation should continue at a rate of 2.5 per cent to 3 per cent over the next few years," he says. "An 8 per cent term deposit would give you a real rate of return of 5 per cent or more with very low risk."

Fixed-interest broker Andrew Murray agrees that investors may not realise what a golden opportunity current term deposit rates are.

He says investors with cash to put on deposit should be thinking about how to make the best of the market conditions.

WIN FOR SAVERS

Murray, who is a director of Curve Securities, says: "In the normal course of events, term deposit rates are set at a discount to the wholesale cost of funds. So with the bank bill swap rate [the benchmark for the cost of money in the capital market] for 180 days at 4.3 per cent or 4.4 per cent, you might expect to be offered a six-month term deposit at around 4 per cent.

"But there are lots of offers for six-month terms at 6.1 per cent and 6.2 per cent. We are seeing a war for deposits and savers are getting the spoils."

In other words, investors are getting term deposit rates that are almost 2 per cent higher than they would be normally. The reason for all this generosity is that, since the onset of the global financial crisis, banks and other financial institutions have become more dependent on retail deposits to fund their lending activities.

The flow of wholesale funds through the global capital market, which funded growth in the banking sector for most of the past decade, has slowed.

Parts of the market, such as the securitisation of mortgages, are only now beginning to recover.

TREND TO CONTINUE

All financial institutions have been increasing the amount of funding that comes from retail deposits and they continue to do so.

Another factor is the recovery in the mortgage market. Home lending slowed in 2008 but picked up last year and grew about 8 per cent. As lenders do more lending, their need for funding increases.

This situation will continue for some time. Earlier this month, when the Commonwealth Bank reported its results for the six months to December, the bank's chief executive, Ralph Norris, said: "Funding pressure is not going to diminish any time soon."

KPMG's 2009 financial institutions performance summary says the funding priority that financial institutions established in 2009 - reducing wholesale debt and maintaining or growing share in retail deposits - will remain a high priority in 2010.

KILLING THE COMPETITION

Some commentators have suggested there is another factor at play - the big banks are offering high deposit rates as a way of squeezing their smaller competitors. Big banks can absorb the higher cost of deposits, without having to put up lending rates, more easily than small lenders. By offering high deposit rates, they are pricing their small rivals out of the market.

For investors, the question is how best to make the most of this situation. Murray believes the sweet spot for investors is near the 12-month term.

"We put a lot of clients into a one-year term at 7 per cent in recent weeks. There are still offers from 6.3 per cent up to 6.8 per cent for one-year terms and we think those are very good offers," he says. Most investors like to keep their term deposits turning over and tend to head for the three- and six-month terms. In a recent briefing the chief financial officer of Bendigo and Adelaide Bank, Richard Fennell, said the bank had $18 billion in term deposits and the average term was four months.

MORE RATE HIKES

Murray says investors should consider a longer term. "Our view is that the Reserve Bank will move the cash rate up to 4.5 per cent this year [currently 3.75 per cent]. That means we might see at-call and short rates move up another 75 basis points. A move of that magnitude in at-call rates will not match the long rates in the market now. Anything priced at 6 per cent or more is a better bet than staying in an at-call account or short term.

"There would have to be a big advantage to go longer than a year. There are lots of unknowns once you get out past 12 months. I might be comfortable out to three years if banks offered 8 per cent again."

AMP's Oliver says the investment decision has to factor in risk tolerance and the need for liquidity. "We would say that the sharemarket offers the prospect of the best returns for investors in the year ahead but some investors, especially older retirees, are uncomfortable with the market's volatility," he says. "If the security of your investment is a high priority a five-year term deposit paying 8 per cent is an attractive investment.

"You have to be sure that you are not going to want to invest in something else in the meantime because the term deposit will lock you in."

UNUSUAL TIMES

Oliver says that if investors are thinking of taking advantage of the unusually high term deposit rates they should not wait too long. "At some point the pressure for retail deposits will ease and then the rates will fall back to normal levels," he says. "Normally, with interest rates rising you would keep your money in short-term deposits or at-call and wait until rates reach their peak before locking in.

"But these are unusual circumstances because term deposit rates are being driven by factors other than the interest-rate cycle. Cash rates will go up this year but they might not reach the levels that the long-term deposits are at now."

In contrast to their high term deposit rates, banks and other deposit-taking institutions have tended to hold back on passing some of the recent interest rate rises through to customers with at-call high-interest online accounts.

All financial institutions want to increase their level of funding from retail deposits but they are also keen to make sure they hold on to those deposits for as long as possible.

TERM DEPOSITS WIN

A significant number of institutions did not move their online savings account rates by the full 0.75 of a percentage point to match the change in the official cash rate between October and December. Of the 53 banks, credit unions and building societies in the Infochoice database offering high-yield online savings accounts, only 36 passed on all three of the 25-basis-point increases in the official cash rate and only 13 exceeded the level of the official cash rate increases.

The managing director of fixed-interest broker FIIG Securities, Jim Stening, says the long-term rates are a standout but suggests that if investors are wary of putting too much money into deposits for 12 months or more, they should split it up among several different maturities.

Stening says he would usually talk to clients about higher yields available from corporate debt securities, hybrids and other high-yield instruments but now his attention is on term deposits.

"We have not seen such intense competition for the humble term deposit ever before. There are great returns with very little risk," he says.

See the top rates for term deposits and online accounts, Page 6

Negotiate on large amounts

Fixed-interest broker Andrew Murray says he took a call last week from a credit union manager who needed money fast. Murray, a director of Curve Securities, says the credit union had made some big loans and needed funding.

"The credit union was prepared to offer a better rate than its advertised term deposit rate," Murray says. "We sent an email out to our clients and raised the money."

All financial institutions offer special rates on deposits when the need arises or when the right customer is involved, although the conditions vary and it is hard to pin an institution down on how they actually do it.

Commonwealth Bank says it may negotiate with customers who have $500,000 or more to put on deposit, depending on the timing and the term the customer is looking for.

ANZ says that customers with balances of more than $100,000 have access to a dedicated phone pricing team that can "develop a tailored offer".

People with that sort of money might also consider dealing with a broker.

Murray says Curve Securities deals with small institutional investors and trustees of self-managed superannuation funds. The average balance it handles is $1 million. It will work with private investors who have $100,000 or more but prefers to work with investors who can place $500,000 or more.

The value of brokers is that they are always sniffing out a deal and financial institutions know they can use brokers to raise funds quickly. Last week, when Bank of Cyprus was advertising a five-year term deposit for 7.85 per cent, broker FIIG Securities was advertising the same deal at 7.95 per cent for its clients.

A director of FIIG Securities, Jim Stening, says part of his job is to be in contact with financial institutions hunting for deals.

FIIG takes clients with a minimum of $50,000. Neither broker charges clients commissions.

They are paid commissions by the deposit-taking institutions. These commissions do not change the rate being paid on the term deposits and other investments

Government guarantee on retail deposits

A couple of weeks ago the Treasurer, Wayne Swan, announced the government would withdraw its deposit guarantee scheme. The announcement caused some confusion because the government introduced two guarantee schemes in October 2008 — one for large deposits and wholesale funding and the other for retail deposits.

From March 31 there will no longer be a government guarantee on deposits of more than $1 million in banks, credit unions and building societies. The guarantee on wholesale debt securities issued by these institutions will also be removed.

The announcement does not affect the government's guarantee of retail deposits. The guarantee covers deposits of up to $1 million for each depositor in any one approved deposit-taking institution. For example, if a depositor has three accounts with an institution, each with a balance of $400,000, these are added together and protection is provided for $1 million of the $1.2 million.

The retail deposit guarantee is administered by the Financial Claims Scheme, which was also established in October 2008 and is run by the banking regulator, the Australian Prudential Regulation Authority.

The $1 million retail deposit guarantee runs until October 12 next year. The Financial Claims Scheme will continue to operate past that date and the government has said it will review the retail guarantee and will apply a new guarantee limit.

TOP RATES WHAT YOU GET

ONLINE SAVINGS ACCOUNTS

MINIMUM BALANCE $10,000

		RATE 1/10/09	CURRENT RATE
AMP	eASYSaver Account	2.80	3.55
CBA	NetBank Saver	2.75	3.75
Nab	Nab iSaver	2.75	3.50
St George	Direct Saver	3.20	3.95
Westpac	eSaver	2.75	3.50

ONLINE SAVINGS ACCOUNTS

SMALLER BANKS

		RATE 1/10/09	CURRENT RATE
UBank	USaver	5.11	5.51
Arab Bank	Online Savings Acc.	4.55	5.30
Railways CU	Express Saver (S50)	3.90	5.10
Rural Bank	RBonline Savings	3.75	5.10
Bank of Cyprus	Midas Account	3.75	5.00

PLEASE REFER TO PDF MONEY SMH 24-2-2010 PAGE 6 FOR MORE TABLE INFORMATION