# POLICY CHANGES AND ITS IMPACT ON DEMAND AND SUPPLY OF BANK CREDIT

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# DECLARATION

I, Mini Joseph, hereby declare that this thesis entitled **Policy Changes and Its Impact on Demand and Supply of Bank Credit**, is a bonafide record of research work done by me during the course of my research and that the thesis has not previously formed the basis for the award to me of any degree, diploma, associateship, fellowship or other similar title or recognition.

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## CERTIFICATE

Certified that this thesis entitled **Policy Changes and Its Impact on Demand and Supply of Bank Credit** is a record of bonafide research work done independently by Smt. Mini Joseph under my guidance and supervision and that it has not previously formed the basis for the award of any degree, diploma, associateship or fellowship to her.

She is permitted to submit the thesis to the University.

Dr. Gabriel Simon Thattil
(Supervising Teacher)

# ABSTRACT

Changes in monetary policy instruments like repo and reverse repo rates are made by the RBI to influence the demand for and supply of bank credit to achieve the goals of price level control and economic development. Indian banks are responding positively to the changes initiated by the RBI and hence policy instruments are effective in influencing the supply of credit. But direct as well as indirect policy instruments do not have any significant impact on the credit supplied by the foreign banks operating in India. Liquidity Adjustment Facility and Market Stabilization Scheme are highly effective in controlling the day-to-day money supply in the economy. Reduction in the weighted average lending rate to agriculture and industries positively influenced the demand for credit and in turn the contribution by these sectors to the GDP of India improved considerably. Household customers who have no access to formal credit are not bothered about the changes in interest rates. But those who have access to different sources of credit are cautious about the interest rate changes and hence the demand for retail credit may be influenced by policy changes.

**Keywords:**- Monetary Policy, Bank Credit, Cash Reserve Ratio, Repo rate, Reverse repo rate, Demand for Credit, Supply of Credit.

# PREFACE

Monetary Policy acts through influencing the cost and availability of bank credit directly. To ensure the objectives of monetary management, the RBI has introduced indirect policy instruments like repo and reverse repo and also came up with Liquidity Adjustment Facility and Market Stabilisation Scheme to ensure short term money management. Recognising the importance of low cost funds in the economic development, the Government of India, made drastic reduction in the bench mark interest rates and gave freedom to the banks in India to fix interest on deposits and loans on the basis of market forces.

In this context, the response of the commercial banks to the monetary policy actions deserves special research attention. The present study made an attempt to see whether the responses of the bank groups in India differ on the basis of the nature of ownership of these banks.

It seems that while monetary policy actions do influence commercial bank behavior, not all bank groups respond uniformly. Attributes like ownership and liquidity play important roles in shaping the nature of response. The reduction in the lending rate to achieve enhanced flow of credit to agriculture and industries definitely made positive contribution towards the economic growth of the nation during the post liberalized era.

The commercial banks in India are now concentrating on retail banking. Hence the demand for credit depends, to a certain extent, on the perceptions of household customers regarding the interest rate changes. In this context the perceptions of households regarding the importance of interest on loans, in deciding the amount of loans demanded and the choice of lender were studied. It is found that people who do not have access to credit (economically marginalized) are not much bothered about changes in interest rates but those who have access to credit are very cautious about the changes.

# CONTENTS

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