

GOVERNMENT OF INDIA  
MINISTRY OF FINANCE  
DEPARTMENT OF FINANCIAL SERVICES  
LOK SABHA

UNSTARRED QUESTION NO. 528

TO BE ANSWERED ON THE 20<sup>TH</sup> JULY 2018/ ASHADHA 29, 1940 (SAKA)

**Increase in Net Interest Margin**

**528. SHRIMATI VASANTH M.:**

Will the Minister of FINANCE be pleased to state:

- (a) whether the Reserve Bank of India study has stated that deterioration in the health of the banking sector at the initial stages impairs monetary transmission through interest rate channel as banks are able to charge extra credit risk premium for possible loan losses, if so, the details thereof;
- (b) whether at a low level of gross Non-Performing Assets ratio, banks were able to pass on the burden of deterioration in asset quality to tier borrowers in the form of higher lending rates, which reflected in increase in Net Interest Margin; and
- (c) if so, the details thereof?

**ANSWER**

**Minister of State in the Ministry of Finance  
(SHRI SHIV PRATAP SHUKLA)**

(a) to (c): With regard to the question, the Reserve Bank of India (RBI) has informed that a paper titled 'Asset Quality and Monetary Transmission in India', authored by M/s Joice John and three others (all officers in RBI's Monetary Policy Department), has been published in RBI's *Occasional Papers* volume 37 No. 1&2, 2016. According to the paper: "A bank faced with a high level of non-performing assets (NPA) – prospective or realised – will seek to build up provisions by loading credit risk premia on its performing loans, thereby pushing up the lending rates and hence its net interest margin (NIM). In the process, notwithstanding lower funding costs in response to the policy rate cut by the central bank and comfortable liquidity conditions, banks may not reduce their lending rates or may reduce them only partly, thereby impeding monetary transmission. Thus, movements in NIM of banks, among others, could provide an important indication of the effectiveness of monetary transmission."

RBI has further clarified that the views expressed in the said paper are those of the author and not necessarily those that of RBI.

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