

PROCYCLICALITY OF BANKS - THE INDIAN EXPERIENCE

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ABSTRACT

Supervisors and policy makers pay increasing attention to the possible procyclical nature of banks' behaviour. To ensure macroeconomic and financial stability, it is important that regulators understand whether, and to what extent, banks are affected by the macroeconomic and lending cycles. This paper attempts to provide a comprehensive investigation of these issues using a dataset of Indian commercial banking sector over the period 1996-2007. By estimating static panel data model, it tries to investigate whether loan loss provisions and non-performing assets show a cyclical pattern. The estimated relations are studied to analyse the sector wise (public sector banks, foreign banks and private sector banks) behaviour of Indian banks to assess the effects of macroeconomic shocks on banks' balance sheets.

Keywords: procyclicality, loan loss provisions, non-performing assets, lending cycle.