Indian Economy · GS - III

Examine the major factors influencing credit growth in India. How can a moderation in bank and NBFC lending affect economic activity and financial stability?

EXAM YEAR	PAPER	SUBJECT
DAILY PRACTICE 28/10/2026	GS - III	Indian Economy

MARKS	WORD LIMIT
10	~150 words

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Answer Hint

Interest rates; crude oil prices; monsoon performance; retail credit demand; corporate leverage; deposit mobilisation; liquidity conditions; financial stability

Model Answer

Introduction

Credit growth reflects the availability and demand for loans across households, businesses and other economic sectors. Its trajectory influences consumption, investment and overall economic activity.

Factors influencing credit growth

1. Macroeconomic conditions: Elevated crude oil prices can increase inflation and production costs. An inadequate monsoon may weaken rural incomes and agricultural demand, affecting borrowing patterns.

2. Borrowing costs: Higher interest rates increase the cost of loans and may discourage household consumption and business investment.

3. Sectoral demand: Retail borrowing can support consumption, while low corporate leverage may provide businesses with capacity to borrow for expansion.

4. Deposit mobilisation and liquidity: Banks require stable deposits to sustain lending. When system liquidity tightens or credit demand grows faster than deposits, funding costs may rise.

Economic and financial implications

Moderating credit growth may restrain investment and consumption, particularly in credit-dependent sectors. However, excessively rapid lending can increase indebtedness, asset-price risks and non-performing assets.

Way Forward

Banks and NBFCs should maintain prudent underwriting, diversify funding sources and monitor vulnerable borrowers. The Reserve Bank of India should continue effective liquidity management and financial supervision, while lenders balance credit expansion with asset quality.

Conclusion

Healthy credit growth requires a balance between adequate financing for productive activity and safeguards against excessive leverage and financial instability.

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