

## Impact of RBI's Liquidity Policies on the Profitability of Commercial Banks

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### Abstract

RBI, the Central bank of India, plays a critical role in managing liquidity in the economy. CRR helps RBI to control the flow of money in the market whereas SLR helps the banks to handle a sudden increase in demand for deposits. CRR, SLR has a critical impact on the liquidity as well as the lending ability of the banks. The control on liquidity results in the availability of quantum of money for lending, which in turn affects the earnings of the banks. This paper examines the relationship between SLR and CRR and their impact on the profitability of Scheduled Commercial Banks. The paper analyses the conformity to the central bank's liquidity policy along with the impact on their profitability. The study highlighted the distinction between Public Sector Banks and Private Sector Banks with reference to research parameters.

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**Keywords :** RBI, CRR, SLR, NDTL, ROA, ROI, Banking, SCB; PSBs, Liquidity, Profitability, Central Banking, India

### I. Introduction

THE RBI CONTROLS the short-term volatility in the interest rates by adjusting the amount of liquidity available in the system through CRR and SLR. They are the important components of the RBI's monetary policy intended to control and manage liquidity in Commercial banks in India. RBI mandates every bank should have specific liquidity reserves to control the interest rates of lending and borrowing in the loan and deposit market.

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**Table VI**  
**Correlation of SLR & ROI**

Banks	r	r square	SE	Strength	Significance	Hypothesis
<b>PSBs</b>						
AB	-0.68	0.47	0.17	Good	Significant	HF1
BOI	0.17	0.03	0.31	Weak	Insignificant	HF0
CB	0.06	0.00	0.32	Weak	Insignificant	HF0
<b>PrSBs</b>						
HDFC	-0.33	0.11	0.28	Weak	Insignificant	HF0
ICICI	0.05	0.00	0.32	Weak	Insignificant	HF0
KMB	-0.66	0.44	0.18	Good	Significant	HF1

**Note :** \* Pearson Product – Movement Correlation Coefficient Critical Value (CV) at 0.05 level of is 0.444.

Source : Self Computed

For AB, KMB banks r is greater than the critical value, H<sub>0</sub> is rejected and for all the remaining banks r is less than the critical value, H<sub>0</sub> is accepted.

#### 6.7.2. Analysis of Strength of Correlation

AB, KMB banks showed Good Correlation, and remaining all the banks showed Weak Correlation. The banks which showed Good Correlation also showed Significant Correlation and the remaining banks showed Insignificant Correlation.

### VII. Conclusion

The study proves that all the banks have been adhering to the liquidity policies of RBI, irrespective of the sector they belong to. However, mixed results were obtained relating to the correlation between Central Bank's liquidity policies and commercial bank's profitability. While PSBs' showed a positive impact with reference to liquidity policies on ROA, PrSBs showed a divergent trend. The PrSBs' were relatively less affected by RBI's liquidity policies. All the banks under study showed a negative correlation with ROI. The positive correlation for ROA is because of the direct impact of liquidity on assets. A negative correlation for ROI is due to other factors affecting the investments of select banks. PrSBs' seem to be higher freedom in managing their liquidity and profitability as compared PSBs'.

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#### Appendix Strength of Correlation

Exactly -1	Perfect downhill linear correlation.
1 to -0.70	Strong downhill linear correlation.
-0.50 to - 0.70	Good downhill linear correlation.
-0.30 to -0.50	Moderate downhill linear correlation.
< -0.30	weak downhill linear correlation.
0	No correlation
1 to 0.70	Strong uphill linear correlation.
0.50 to 0.70	Good uphill linear correlation.
0.30 to 0.50	Moderate uphill linear correlation.
< 0.30	weak uphill linear correlation.