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AUTHOR OR EDITOR

Martha López, Fernando Tenjo, Héctor Zárate

Publication Date:
Friday, 01 July 2011

Abstract

The recent financial crisis has brought to the forefront the need for a better understanding of the transmission mechanisms of monetary policy. The main step forward on this issue has drawn on work aimed at stressing the role of the financial sector in this transmission. Particular emphasis has been placed on how policy actions impact risk perceptions and attitudes of banks and other financial institutions, leading to shifts in the supply of credit. Along these lines, and based on evidence from Colombia, this paper finds a significant link between low interest rates and banks' risk-taking based on evidence from Colombia. Lower interest rates raise the probability of default on new loans, but reduce that on outstanding loans. Furthermore, this channel of policy transmission depends on some bank, loan and borrower characteristics, as well as on macroeconomic conditions, such as the growth rate of the economy.