e-ISSN : 2347 - 9671 p- ISSN : 2349 - 0187

Impact Factor : 0.998

EPRA International Journal of Economic and Business Review

www . epratrust.com

November 2014 Vol - 2 Issue- 11

IMPACT OF BANKING SECTOR REFORMS ON THE PROFITABILITY OF PUBLIC SECTOR BANKS – A COMPARATIVE STUDY.

Dr. P.Mohan[1] & Gollapudi Sahadeva Rao[2]

[1]Principal, Manair College of Management, Khammam, Telangana, India

[2]Assistant Professor, Department of Bussiness Administration., Laqshya College of Management, Khammam, Telangana.

ABSTRACT

The Paper attempts to study the performance select Public Sector Banks in India in terms of profitability in the post reform era. The present study adopts Descriptive Research Design and the study is based on Secondary Data. Two Public Sector Banks were selected for the study. State Bank of Hyderabad from the SBI and its association's category and Andhra Bank from Nationalized category has been chosen for the present study. The study examines the operating and financial performance of the select banks during the period 2004-2013. A well developed Banking System is a necessary pre condition for economic development in a modern economy. Structural as well as functional reforms in the banking system are needed to enable the banks to perform developmental role in underdeveloped and developing economies.

KEY WORDS: *Commercial Banks, Profitability determinants, Capital Adequacy Ratio, Net Performing Assets, Return on Assets.*

1. INTRODUCTION

Commercial banks are an integral part of the financial system of any country. Banks play in important role in mobilizing savings of individuals into productive investments. In India, prior to nationalization, banking was restricted mainly to the urban areas. After nationalization, the Indian banking system registered tremendous growth in volume. Banks enjoyed little autonomy as both lending and deposit rates were controlled until the end of the 1980s. Although, nationalization of banks helped in spreading of banking to the rural and uncovered areas, the monopoly granted to the public sector and lack of competition led to overall inefficiency and low productivity on the other side. By 1991, the country's financial system had an inefficient and financially unsound banking sector. Based on recommendations of Narasimham Committee Report (1991), the RBI introduced several reforms that included reduction of reserve requirements, deregulation of interest rates, introduction of prudential norms, strengthening of banks supervision and improving the competitiveness of the system capital requirements for banks to address the issues relating to health. By mid-1997, the RBI reported that the reforms process had started showing result. It was found that the changes were only able to arrest the deterioration of the earlier system and there was still scope for considerable reforms. The period 1992-97 laid the foundation for reforms in the banking system (Rangarajan, 1998). The second Narasimham committee Report (1998) focused on issues like strengthening of the banking system, upgrading of technology and human resource development. The report laid emphasis on two aspects of banking regulation, viz., capital adequacy, asset classification and resolution of NPA – related problems. At present, banks in India are venturing into non-traditional areas and generating income through diversified activities other than the core banking activities. Strategic mergers and acquisitions are being explored and implemented. With this, the banking sector is currently on the threshold of an exciting phase. The banks are now facing a number of challenges such as frequent changes in technology, stringent prudential norms, increasing competition, worrying level of NPA's rising customer expectations, increasing pressure on profitability, asset-liability management, liquidity and credit risk management , rising operating expenditure and so on.

2. REVIEW OF LITERATURE

Varde (1973) in an empirical study on efficiency of rural branches, mentions that the success of a rural branch has to be judged in relation to the objective of rural banking, which is tow fold: to act as an active catalyst in the integrated socio-economic development of the area served by the branch, and to become a commercially profitable unit of banking.

O.P. Mathur (1978) studies the role of the public sector banks as an instrument for rapid growth of Indian economy in general and working of State Bank of India and its seven subsidiaries in particular.

Gosh D.N, Nanda karni, Dinesh. C, Bhat V.V, analyzed the importance of banking in Economic Development and the opportunities and challenges faced by commercial banks in India. They have mentioned that political, economic, social and technological changes have been largely influencing the role of these banks.

3. OBJECTIVES

The study aims at evaluating the performance of public sector banks in the post-reform period and to assess how far these banks have been successful in achieving the parameters set by the committee. The specific objectives of the study are as follows:

1. To examine the banking sector Reforms in India and performance of commercial Banks in the light of the reforms.
2. To examine the operational performance and Financial Performance of the Andhra Bank and State Bank of Hyderabad during the period 2004-2013.
3. To examine the impact of Reforms on profitability of State Bank of Hyderabad and Andhra Bank

4. To offer suggestions in the light of conclusions drawn out of the study for further improvement of select banks.

4. RESEARCH METHODOLOGY

4.1. Research Design:-

For the purpose of the present study, Descriptive Research design was adopted.

4.2. Sources of Data:-

The proposed Research study is based upon the secondary data. The data has been collected from the Annual Reports of State Bank of Hyderabad and Andhra Bank, Reports on Trends and Progress of Banking in India, basic statistical returns of scheduled Commercial Banks published by Reserve Bank of India and IBA Bulletins etc.

4.3. Sampling:-

For the purpose of the present study public sector banks were selected. Since nationalized Banks and State Bank of India and its Associate Banks are two categories of public sector Banks; one from each section have been selected for the study. State Bank of Hyderabad from SBI and its Associates category and Andhra Bank from Nationalized Banks category have been chosen for the present study.

4.4. Tools and Techniques Used In Data Analysis:-

The various statistical tools viz., Growth rate, growth index and percentage etc., are used for analysis of study.

Growth Rate = (((b-c) / b) x 100)

Where b= Figure of immediate previous year

c= Figure of current year

in some cases growth index is calculated using the following formula

Growth Index = (((b-c) /b) x 100)

Where b= Base year data

c- Current year data

4.5. Period of Study:-

For the purpose of analyzing the performance as well as the profitability position of the select banks, a period of 10 years from 2003-04 to 2012-13 has been selected.

5. BANKING SECTOR REFORMS

From the 1991 India economic crisis to its status of third largest economy in the world by 2011, India has grown significantly in terms of economic development. So has its banking sector. During this period, recognizing the evolving needs of the sector, the Finance Ministry of Government of India (GOI) set up various committees with the task of analyzing India's banking sector and recommending legislation and regulation to make it more effective, competitive and efficient. Two such expert Committees were set up under the chairmanship of M.Narasimham. They submitted their recommendations in the 1990s in reports widely known as the Narasimham Committee-I (1991) report and the Narasimham Committee-II (1998) Report. These recommendations not only helped unleash the potential of banking in India, they are also recognized as a factor towards minimizing the impact of global financial crisis starting in 2007. Unlike the socialist –democratic era of the 1960s to 1980s, India is no longer insulated from the global economy and yet its banks survived the 2008 financial crisis relatively unscathed, a feat due in part to these Narasimham Committees.

The Narsimham Committee -II was tasked with the progress review of the implementation of the banking reforms since 1992 with the aim of further strengthening the financial institutions of India. It focused on issues like size of banks and capital adequacy ratio among other things. M.Narasimham, Chairman, submitted the report of the Committee on Banking Sector Reforms (Committee-II) to the Finance Minister Yashwant Sinha in April 1998.

Table No.1: Capital Adequacy Ratio-Bank Group-wise

(Percent)

Bank Group	1998	1999	2000	2001	2002	2003	2004	2005	2010	2012	2013
Nationalised Banks	10.3	10.6	10.1	10.2	10.9	12.2	13.1	13.2	12.3	12.4	12.1
State Bank of India Group	14.0	12.3	11.6	12.7	13.3	13.4	13.4	12.4	11.9	12.3	13.2
Old Private Sector Banks	12.9	12.1	12.4	11.9	12.5	12.8	13.7	12.5	11.7	12.1	14.1
New Private Sector banks	13.2	11.8	13.4	11.5	12.3	11.3	10.2	12.1	12.6	12.0	14.4
Foreign Banks	10.3	10.8	11.9	12.6	12.9	15.2	15.0	14.0	13.0	12.4	13.1

Source: Report on Trend and Progress of Banking in India.

6. MAJOR ISSUES OF BANKING

The Committee recommended the following major issues of banking sector like Autonomy in Banking, Reforms in the role of RBI, Stronger Banking System, Non-Performing Assets, Capital Adequacy and tightening of provisioning norms and Entry of Foreign Banks.

7. OPERATIONAL PERFORMANCE AND FINANCIAL PERFORMANCE OF SELECT BANKS

The growth rate of fixed deposits of State Bank of Hyderabad is higher than the other components of total deposits (i.e. demand deposits and savings deposits) through out the study period. The Amount of fixed deposits of Andhra Bank was Rs.7262 crores in 2004 have been increased to Rs.32832 crores but the share of fixed deposits in total deposits decreased in 66.43 in 2013 from 69.57 in 2004.

The savings deposits of Andhra Bank were Rs.2259 crores with a percentage of 21.64 to total deposits in 2004 have increased to Rs.12184 crores with a percentage of 24.65 in 2013. The current deposits were increased to Rs.4409 crore sin 2013 from Rs.917 corres in 2004. The share of current deposits in total deposits 8.79 percent in 2004 has become 8.92 percent in 2013.

Total advances sanctioned by Andhra Bank are continuously increasing throughout the study period. And the advances to priority sector of the bank are also increased to Rs.12660 crores in the year 2013 from Rs.1874 crores in the year 2004. But the share of priority sector advances in total advances decreased to 36.97 percent in the year 2013 from 40.97 percent in the year 2004.

The credit per branch office of the State Bank of Hyderabad has been increased by six times during 2004-2013. i.e., from Rs.0.54 in 2004 crores to Rs.3.27 crores in 2013, whereas the same of Andhra Bank during the same period increased by four and half times i.e, Rs.0.46 crores in 2004 to Rs.2.51 crores in 2013.

Table No. 2: Return on Assets of State Bank of Hyderabad and Andhra Bank

Year	State Bank of Hyderabad	Andhra Bank
2004	0.85	0.78
2005	0.82	1.76
2006	0.82	0.59
2007	1.02	0.97
2008	1.15	1.63
2009	1.25	1.72
2010	0.72	1.59
2011	1.13	1.38
2012	1.14	1.31
2013	1.00	1.16

Source:Annual Reports of State Bank of Hyderabad and Andhra Bank and RBI Report on Trend and Progress of Banking in India from 2003– 04 to 2012 – 13.

The total Income of the State Bank of Hyderabad during the study (2004-2013) has been increased three and half times i.e. from Rs.1416 crores in 2004 to Rs.5080 crores in 2013. During the same period the Andhra Bank has been increased it's Total income by four times a little bid higher than the State Bank of Hyderabad i.e. from Rs.1200 crores in 2004 to Rs.4871 crores in 2013.

At the beginning of the study period in 2004 interest income as percentage of total assets was 9.3 and 9.11 of State Bank of Hyderabad and Andhra Bank respectively both are higher than the average of the public sector banks. And at the end of the study period in 2013 the same marked as 7.14 and 7.58 of the bans respectively again these are higher than the average of public sector banks 7.08.

Table No. 3 Capital Adequacy Ratio – A Comparative Study of State Bank of Hyderabad and Andhra Bank with Public Sector Banks

Year	State Bank of Hyderabad	Andhra Bank	Public Sector Banks
2004	10.65	11.02	NA
2005	10.86	13.36	NA
2006	12.28	13.4	11.2
2007	14.03	12.59	11.8
2008	14.91	13.62	12.6
2009	14.29	13.71	13.2
2010	11.74	12.11	12.9
2011	12.08	14	12.17
2012	12.51	11.33	12.36
2013	12.35	11.61	12.51

Source: Annual Reports of State Bank of Hyderabad and Andhra Bank and RBI Report on Trend and Progress of Banking in India from 2003 –04 to 2012– 13.

At the beginning of the study period in 2004 the interest expenditure constitutes 58.33 per cent in total expenditure of State Bank of Hyderabad and 64.62 per cent of Andhra Bank. The same has been increased to 72.74 per cent and 66.82 per cent respectively.

The operating expenditure of the State Bank of Hyderabad in 2004 was 29.32 per cent in total expenditure and of Andhra Bank was 29.42 per cent, which has decresed to 17.67 per cent and 21.98 per cent respectively.

Table No. 4 Gross Non – Performing Assets as percentage of Total Assets – A Comparative study of State Bank of Hyderabad and Andhra Bank with Public Sector Banks

Year	State Bank of Hyderabad	Andhra Bank	Public Sector Banks
2004	7.00	3.90	6.71
2005	6.03	2.89	5.95
2006	5.84	2.31	5.31
2007	4.06	2.5	4.89
2008	2.83	2.35	4.21
2009	2.26	2.28	3.5
2010	1.58	1.35	2.73
2011	1.12	1.07	2.05
2012	0.72	0.84	1.6
2013	0.51	0.66	1.34

Source : Annual Reports of State Bank of Hyderabad and Andhra Bank and RBI Report on Trend and Progress of Banking in India from 2003-04 to 2012 –13.

The provisions & Contingencies of the State Bank of Hyderabad during 2004-2013 has been increased by 269.57 per cent but the percentage of the same to total expenditure has been decreased to 9.60 per cent in 2013 from 12.36 per cent in 2004. Regarding to Andhra Bank the provisions and contingencies has been increased by 728.79 per cent during 2004-2013 and the percentage of the same to total expenditure has also increased to 11.20 per cent in 2013 from 5.96 per cent in 2004.

The State Bank of Hyderabad interest expenditure as percentage of total assets was lower as compared to average of Public Sector Banks during the period 2004-2008 later the same of the banks has been higher than the public sector banks average. And the same of the Andhra Bank in the year 2004 was 6.2, which is almost equal to public sector banks 6.21 decreased to 5.07 of Andhra Bank and 4.93 of Public Sector Banks in 2013.

8. IMPACT OF BANKING SECTOR REFORMS ON THE PROFITABLITY OF SELECT BANKS

With the implementation of Reforms over a period of one and half decade the Quality of Assets of the Indian Commercial Banks has improved. The Gross Non – Performing Assets as percentage of Total Assets of both the banks have been decreased from 7.00 percent and 3.90 percent in 2004 to 0.51 percent and 0.66 percent in 2013 of State Bank of Hyderabad and Andhra Bank respectively, and the same also much lower than the average of Public – Sector Banks 1.38 percent in 2013.

The Gross Non – Performing Assets as percentage of Total Advances of State Bank of Hyderabad and Andhra Bank have been decreased to 0.87 percent and 1.08 percent in 2013 from 15.84 percent and 9.72 percent in 2004 respectively. And it also be noted that now and then the percentage is lower than the average of the public sector banks.

The Net Non – Performing Assets as percentage of Total Assets of the State Bank of Hyderabad and Andhra Bank have become almost near to zero i.e.0.09 percent in 2013 from 3.55 percent and 1.67 percent respectively in 2004. The Net Non – Performing Assets as percentage of Total Advances of the State Bank of Hyderabad in 2013 is 0.16 percent and 0.15 percent of Andhra Bank, which is very much lower than public sector banks average of 0.99.

By this it can be concluded that the Quality of assets owned by the select banks is much better as compared with the average of all public sector banks.

9. CONCLUSION

A well developed banking system is a necessary pre-condition for economic development in a modern economy. Besides providing financial resources for the growth of industrialization, banks can also influence the direction in which these resources are to be utilized. The Changes affecting the banking sector in the wake of globalization and opening up of the economy in the early nineties has provoked much reflection on the ways and means to strengthen the banking system. In the underdeveloped and developing countries, not only the banking facilities are limited to a few developed urban areas, but also the banking activities are limited mostly to trade and commerce, paying little attention to industry and agriculture. Structural as well as functional reforms in the banking system are needed to enable the banks to perform developmental role in underdeveloped and developing economies.

10. SUGGESTIONS

1. The State Bank of Hyderabad and Andhra Bank should take necessary precautionary measures to curtail NPAs while extending loans to Real Estate.
2. The Public Sector Banks have a unique advantage over their competitors in terms of their branch network and the large customer base. But it is not sufficient to increase their profitability. Hence the banks are advised to properly utilize the technology to improve the profitability.
3. Profitability of Indian banks is still low as compared to the banks of several developing countries. The banks need to improve their profitability by diversifying their business especially in the non – funds based activities.

REFERENCES

1. *Varde(1973)-"Efficiency of Rural Branches-An Empirical Pilot study Prajnan, II (April-June) PP 187-203*
2. *Mathur.O.P. –"Public Sector Banks in India's Economy, a case study of the State Bank" Sterling Publisher Pvt.Ltd. New Delhi, 1978.*
3. *Gosh D.N.-"Commercial Banking, lessons from Indian Experience". State Bank of India, Monthly Review, Mumbai, November 1988.*
4. *Joshi-Committee on Productivity, Efficiency and Profitability",. Government of India 1997.*
5. *Amalesh Benerjee and Singh S.K. – "Banking and Financial Reforms in India 2001", Deep & Deep Publications, New Delhi.*
6. *Annual Reports of Reserve Bank of India*
7. *Annual Reports of State Bank of India and State Bank of Hyderabad*
8. *Annual Reports of Andhra Bank*
9. *Report of the Committee on Banking Sector Reforms (Narasimham Committee-I), RBI, 1991*
10. *Report of the Committee on Banking Sector Reforms (Narasimham Committee-II), RBI, 1997*
11. *Reports on Trend &Progress of Banking in India, RBI*
12. *Statistical Tables relating to Banks in India, RBI.*