FINANCIAL EFFICACY OF PUBLIC SECTOR BANKS IN INDIA

DR. R.V.HEMA

ASSISTANT PROFESSOR

IDHAYA COLLEGE FOR WOMEN

KUMBAKONAM.

Abstract:

Banking system is the focal point in the financial set up of any developing country. Banks are regarded as special in view of their specialized functions in the financial intermediation and payment system. The banks undertake asset transformation whereby a depositor can place resources in a bank and the bank in turn can lead to the market. Banks also perform asset liability management focusing on the gap between amount of assets subject to interest rate risk and the quantity of liabilities subject to such risk. The banks have also to manage risk especially with new instruments like derivatives.. the growing international dimension of banking has also brought in a variety of risks like portfolio risk, credit risk, country risk, interest rate risk and foreign exchange risk. Management of risk has become an increasing challenge for commercial banks across the world and hence the need for uniform rules and regulations in the form of Basel norms. It is very essential to review the financial efficacy of banks to analyse its long term and short term solvency. This study aims to compare various aspects of select public sectors by using various parameters.

The financial system, especially banking, facilitates efficient allocation of resources from savers to investors and plays an important role in the economic growth. Banking system is the focal point in the financial set up of any developing country. The banks are conduits in channeling resources to borrowers with productive investment opportunity. The banking system provides financial intermediation and also creates money supply. The process of bank credit is an important channel of monetary policy transmission. Banks accept and deploy large amounts of public funds as well as leverage such funds through credit creation. The more developed the banking system is, better would be the financial intermediation. The Indian banking system has become a potent tool of socio-economic development of the economy and banking has assumed enormous importance as a subject of analysis and research.

Statement of the problem

An increasing rate of savings is essential for the increasing requirements of capital formation for a developing country. As the growth of the bank deposits is the key element in the progress of the banking business, bankers spend more time and man power to mobilize of deposits. The deposits along with other sources of funds, namely, capital, reserves and borrowings form the sources of funds for the banks. The lending and investment activities of the bank are based on the sources of funds. The main source of income is still the income on advances given by the bank and therefore, efficient credit management is very important to achieve the financial objectives of any bank.

The banks were exposed to greater risk of "Perform or Perish". The Reserve Bank of India and Ministry of Finance from time to time take a number of measures which aim to strengthen the banking system. The solvency and liquidity position of banks are important. To ensure the solvency, the RBI has insisted on the banks to follow the statutory requirements like Cash Reserve Ratio, Statutory Liquid Ratio and Capital Adequacy norms. Each bank has to ensure its solvency by monitoring and controlling various ratios for its survival.

The disadvantage of public sector banks with regard to wider branch network and greater mobilization of funds is that the most of their branches are located in remote areas and the cost of their maintenance is high, and their productivity is low. A lower productivity increases relative operational costs and hence lowers profitability. Thus, there exists a direct relationship between productivity and profitability of banks.

The level of NPAs of the banking system in India is still too high. It affects the financial standing of the banks which is a heavy burden to the banks.

The banks now face a number of challenges such as frequent changes in technology required for modern banking, stringent prudential norms, increasing competition, worrying level of non-performing assets, raising customer expectations, increasing pressure on profitability, asset-liability management, liquidity and credit risk management, raising operating expenditure, shrinking size of spread and so on. However, the public sector banks in India continue to be the major lenders in the economy due to their sheer size and penetrative networks which assure them high deposit mobilization and control of 80 per cent of banking business of India. Hence, it is essential to concentrate on public sector banks in India. Therefore, the present study attempts to analyze the overall financial efficacy of public sector banks in India.

Scope of the study

This study analyses the financial performance of public sector banks in India. The study has been made on three sample public sector banks excluding State Bank of India and its associates. The parameters used for the analysis of financial efficacy of public sector banks are solvency and liquidity, lending and non-performing assets, and productivity and profitability.

Objectives of the study

This study has been made with the following objectives.

1. To examine the solvency and liquidity position of select public sector banks.
2. To evaluate the lending activities and level of non-performing assets of select PSBs.
3. To measure the productivity and profitability of sample public sector banks.

Methodology

The research design used to carry out this study is survey method. The present study is an analytical study. Primary data and secondary data have been collected for this study. The secondary data is the main source for this study and it has been collected from the annual reports published by the select public sector banks and the Reserve Bank of India and the house magazines of select banks. The use of various accounting and statistical techniques have been made in the course of the analysis of data. They are ratio analysis, trend percentage, common size percentage, average, co-efficient of variation, compound annual growth rate, multiple correlation, regression and ANOVA..

Sampling

In India, there are 21 public sector banks excluding SBI and its associates. The base year was fixed as 2013-14 for sampling, because the pilot study was carried out in the year. Out of the 21 public sector banks, three banks were selected for this study using stratified random sampling method. The stratification was made on the basis of net worth of public sector banks under three categories, namely, net worth of below Rs.10000 crores, Rs.10000-Rs.15000 crores, and above Rs.15000 crores. From each strata one bank was selected using random sampling method. The selected sample banks are Canara bank, Indian bank and Vijaya bank.

Chapterisation

The report of the research has been organized into seven chapters:

Chapter I - Introduction and Research design
Chapter II - Review of Literature
Chapter III - Profile of select public sector banks in India
Chapter IV - Solvency and Liquidity
Chapter V - Lending activities and NPA management
Chapter VI - Productivity and Profitability
Chapter VII - Findings, Suggestions and Conclusions

Findings:

Solvency

- From 2013-14, all the three select banks have followed Basel III norms. All the three banks have recorded fluctuated trend in CAR under Basel II and III norms, but has achieved the stipulated norm of RBI in all the ten years of the study period.
- The analysis of sources of funds of the three select banks has revealed that the share capital, and other liabilities and provisions of all select banks have fluctuation. The reserves of three select banks have increased except Canara bank in 2015-16. The deposits of all three banks have also increased which indicates the select banks perform efficiently. The borrowings of Canara bank have registered an increasing trend where as the borrowings of Indian bank and Vijaya bank have fluctuated. The amount of total funds and its trend percentage has increased which indicates the banks have focused on mobilizing the sources of funds to execute its various functions.
- The select banks have the financial ability to repay all the deposits and borrowings at the time of requirements of the customers.

- Regarding the ratio of advances to total funds, the Canara bank has not increased the advances to the increasing level of total funds for the last four years of study period. This may be due to the fear of NPA. The gradual increase in the ratio of Indian bank shows that the bank has been followed the conservative lending policy. The ratio of Vijaya bank has fluctuations.
- The debt equity ratio shows that the Vijaya bank has the highest average of Rs.1885.91 crores and co-efficient of variation of 10.95 per cent. The Canara bank has kept the ratio under control. There is also the fluctuation of the ratio of Indian bank.

Liquidity

- The current ratio of all three select banks had more or less the same trend i.e., fluctuating trend. Among the three select banks, the Indian bank has the highest ratio of 1.07 times in 2008-09.
- The liquid assets of three select banks have the fluctuations. Due to hike in CRR from 6.5 per cent to 7.5 per cent in two phases, the amounts of liquid assets of all three select banks have increased in 2007-08. The ratio of liquid assets to total assets and the ratio of liquid assets to total deposits have the fluctuations. The select banks have the highest ratio in 2007-08.
- The ratio of liquid assets to demand deposits has fluctuations due to the variations in the CRR and the amount of demand deposits.
- To fulfill the statutory requirements of RBI, the select banks have concentrated on government securities for the investment.

Lending

- Regarding the deployment of funds, the advances and investments have made in such a way to yield a fair return of interest and other income for its existence and for the execution of banking functions in a profitable way. The amount of cash and bank balance and investment in government securities have been maintained by the select banks as per the fluctuations of CRR and SLR.
- All the three select banks, have not fully utilized the loanable funds for their lending activities due to unwillingness to take risk in lending for the fear of occurrence of NPAs.
- The Canara bank and Indian bank have made the investment in India and outside India. But the Vijaya bank has not made any investment outside India. It has followed a uniform practice of investing in India throughout the study period.
- Except Indian bank in 2014-15, all other select banks have made investment more than 100 per cent of investible funds.
- The select banks have not maintained the stable and high ratio of advances to deposits due to changes in proportion of advances and deposits.

NPA Management

- The ratio of gross NPAs to total assets of three banks has increased abnormally which shows the intensive risk of banks to control NPA to avoid losses in future. In analyzing CAGR, growth rate of

Canara bank was high and Indian bank ranked second and Vijaya bank ranked as third and recorded 22.82 per cent, 18.06 per cent and 12.75 per cent respectively.

- The ratio of gross NPA to gross advances has fluctuated for all the three select banks. In the last four years of study period, the ratio has increased and especially in 2015-16, it reached to its abnormal level 9.74%, 6.84% and 6.77% respectively.
- In all the three select banks, the amount of net NPA and ratio of net NPA to net advances has recorded abnormal trend, due to the stipulated norms of RBI to reveal right amount of NPA. The co-efficient variation of Indian bank 96.07% denotes the high variability in the ratio, when compared to other banks.
- As the NPA has abnormally increased in 2015-16, the proprietor's risk ratio of 2015-16 has abnormal record of highest percentage of 65.92% for Canara bank, 33.33% for Indian bank and 56.09% for Vijaya bank.

Productivity

- The number of employees of select banks had not registered any changes drastically. The banks have maintained the constant staffing level. The analysis of BPE reveals that the total businessand business per employee increased during the decade irrespective of the number of employees. The Indian bank has highest CAGR of 17.25 % and Canara bank and Vijaya bank has CAGR of 12.41% and 11.68% respectively.
- The net profits of the select banks have recorded fluctuating trend because of fluctuations in income and expenses and provisions. Due to high amount of provisions for NPA, the Canara bank has reported a net loss in 2015-16. Even though it has operating profit, the highest provisions made to face the loss. The profit per employee has the fluctuations for the three select banks during the decade.
- The ratio of spread per employee of all three select banks has variation. It has been observed that the average spread per employee of Canara bank, Indian bank and Vijaya bank recorded as 4.68%, 6.37% and 3.59% respectively has achieved in the last six years of study period. It shows that the employees have taken steps to increase the spread.
- While studying the variability in the ratio of interest on deposits per employee, Indian bank stood first, Canara bank stood second and Vijaya bank can be ranked as third which has low variability when compared to other two banks.
- The ratio of interest on borrowings per employee has recorded fluctuations due to variations in interest on borrowings and number of employees. It reveals that the bank has taken steps to decrease the borrowings and increase the deposits.
  - The operating expenses per employee has increased for three select banks, except 2013-14 and 2014-15 in Indian bank and 2011-12 in Vijaya bank.
  - The employee expenses per employee has increased for three select banks except in one or two years of study period.

Profitability

- The ratio of interest earned to working funds of all three select banks has registered a fluctuationary trend which ensured that the banks have taken steps to augment its interest income and risk taking attitude. The interest income and working funds has increased but their proportion out of working funds made the ratio to differ. The Vijaya bank has good CAGR of 2.48% when compared to other banks.
- The interest paid and working funds of the select banks have increased except the interest paid of Vijaya bank in 2009-10 and 2015-16.
- The ratio of spread to total assets has fluctuated for the select banks. The maximum of spread 2.43% for Canara Bank (CB), 3.33% for Indian Bank (IB), and 2.53% for Vijaya Bank (VB) was recorded only in the first year of study period. The fluctuation in the subsequent years indicates that the bank has been striving to increase its income.
- The ratio of net profit to interest earned of the three select banks has fluctuations which indicates the fact that the income generation capacity of the banks have fluctuated due to competition, increasing expenditure, provisions and contingencies. The ANOVA shows that the dependent variable i.e., net profit to interest earned is significantly predicted by independent variables namely CAR, Current ratio, Loanable ratio, Net NPA to Net advances and Business Per Employee (BPE). Multiple regression analysis was revealed that all the independent variables of Canara bank have a positive effect on the net profit to interest earned except the variable net NPA to net advances. All the independent variables of Indian bank have a positive effect on the net profit to interest earned except the variables loanable ratio and net NPA to net advances. All the independent variables of Vijaya bank have a positive effect on the net profit to interest earned except the variables CAR, loanable ratio and BPE.
- The ratio of net profit to working funds has fluctuated due to difference in proportion of net profit to working funds. The working funds of select banks have increased which indicates the efficiency of banks in promoting the business. The ANOVA shows that the dependent variable i.e., net profit to working funds is significantly predicted by independent variables namely CAR, Current ratio, Loanable ratio, Net NPA to Net advances and BPE. The multiple regression analysis shows that all the independent variables of Canara bank have a positive effect on the net profit to working funds except the variable net NPA to net advances. In the case of Indian bank, all the independent variables have a positive effect on the net profit to working funds except the variables loanable ratio, net NPA to net advances and BPE. All the independent variables of Vijayabank have a positive effect on the net profit to working funds except the variables loanable ratio and BPE.
- The EPS of three select banks have recorded a fluctuated trend during the study period. Especially, in 2015-16, the banks have to provide huge amount for NPA, the profitability has decreased. It was reflected in the ratio.

Suggestions

Following measures are suggested to improve the operations of the select banks:

- The select banks should focus on saving deposits and current deposits with planned strategy to reduce the cost of funds.
- The select banks should maintain a balance between liquidity and profitability. Idle or low income yielding assets must be deployed in loans or investment category to mount the interest revenue.
- The select banks must take all efforts to maintain their CAR at optimum level. The excess capital and reserve funds may be deployed in long term lending to earn interest income.
- The Indian bank and Vijaya bank have to maintain more equity to ensure strong solvency.
- The select banks have to give more importance on the upkeepment of current assets to maintain an adequate liquidity.
- The select banks can maintain a good amount of government securities to fulfill the norms of SLR and to earn a safe and reasonable return. But at the same time, equal importance should be given to maintain the investments of other modes to increase their interest income.
- Bankers spend more time and man power in the mobilization of deposits. The same level of effort or more should be taken by the bankers to deploy the funds so collected. The banks shall not be able to sanction loan as per their discretion. The banks should sanction the right amount of loan. The purpose of loan can be met out only when it is provided to the customer at the right time and right amount.
- High percentage of funds deployed in investments beyond the required level denotes that the banks take low risk and derive low income. The select banks must review their investments and other assets periodically to avoid accumulation of idle assets.
- It is the primary responsibility of banks to ensure proper end use of funds/monitor the funds flow to minimize NPA. Effective and regular follow-up of the end use of the funds sanctioned is required to ascertain any embezzlement or diversion of funds.
- A healthy banker - borrower relationship should be developed to recover debt in a congenial environment.
- The bank can train its officials to handle the credit portfolio efficiently in order to increase the interest income of the bank.
- The employees are to be motivated through monetary and non-monetary ways to improve their productivity and thereby the profitably can be enhanced.
- The select banks should take efforts to reduce the operating expenses by means of improving the efficiency of the non viable branches by utilizing some expert services like professional management.
- The select banks should try to upgrade technology and should formulate customer friendly policies to face competition at the national and international level.

Conclusion:

On the whole the total business of select banks has increased. The number of employees has not increased to the level of total business due to the implementation of core banking solutions. The select banks have to employ more workers to recover NPA so that net profit will be increased in the forthcoming years. the bank has to formulate a fair strategy in the recruitment and maintenance of optimum number of the employees and also provision of monetary and non monetary requirements of employees. The some parameters only differs among the select banks. The banks have to concentrate to rectify the factors which will affect the productivity and profitability.

References:

1. Saira S (2013) http://www.hamariweb.com/articles/article.aspx
2. Sumra MS (2011) The Impact of e-Banking on the Profitability of Banks: A study of Pakistani Banks. Journal of Public Administration and Governance1: 31-38.
3. Rust RT, Kannan PK (2003) e-Service: a new paradigm for business in the electronic environment. Communications of the ACM 46: 37-42.
4. Ashiqullah S (2006) A relational study on automated service quality, customer satisfaction and financial performance in the context of Bank Asia Ltd. IUB University, Bashundhara.
5. De Ruyter K, Wetzels M, Kleijnen M (2001) Customer adoption of e-service: an experimental study. International Journal of Service Industry Management 12: 184-207.
6. Hall G (1995) Surviving and prospering in the small firm sector. Routledge, London.
7. Saha S, Nesa Z (2011) Measuring service quality: a comparative assessment based on customer service of HSBC and DBBL. Journal of Banking & Financial Services 5: 111-127.
8. Shreyas, a house magazine of Canara Bank, March 2015.
9. Hema. R.V.(2018), " Financial Efficacy of Public Sector Banks in India", Thesis, Bharathidasan University, Trichy.