BANK LIQUIDITY MANAGEMENT AND ITS IMPECT ON PROFITABILITY

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As banks have become one of the most vital components of any financial system, ensuring stability of the banking sector has gained significant importance as a policy initiative worldwide. Banking stability as an economic indicator can be used to determine whether an economy is robust enough to withstand both internal and external shocks. Banking stability in itself is a function of several health parameters of individual banks. For example, asset quality, LQD risk, capital adequacy, performance, etc. (Reserve Bank of India, 2013).The core purpose of the said study is to know the effect of liquidity position on the performance of Indian Banking Sector. Whatever be the size of a business, liquidity may be considered as one of its controlling nerve centre. Thus, liquidity management is a very important facet of financial management. Both excessive liquidity as well as inadequate liquidity hurt the normal activity of the business firm. Excessive liquidity implies idle funds which fail to earn any profit for the firm. Paucity of liquidity not only impairs the firm's profitability but also results in business operation interruptions and inefficiencies. An overall control over liquidity of the firm can ensure a smooth running of its business wheel.

Key Words: liquidity, profitability, ratio, analysis etc.

Introduction: In today's developing and competitive world, the banking sector has emerged as a key player that contributes to the growth of economy, development of financial sector and more importantly, creation of employment in the country. Banks are the fulcrum of financial system of any economy and they play an important role in contributing to a country's economic development. The major role of banks is to collect money from the public in the form of deposits and then along with its own funds to serve the demands of the customers quickly, paying interest for the deposits and to meet out the expenses to carry out its activities. For this purpose, banks maintain adequate liquidity and earn profits from their activities. Profit is the main reason for the continued existence of every commercial organization and profitability depicts the relationship of the absolute amount of profit with various other factors. In any case, compared to other business concerns, banks in general have to pay much more attention for balancing profitability and liquidity. Liquidity is required to meet the prompt demands of customers and profitability is required to meet the expenses of banks. But both the terms are contradictory in nature. If banks maintain more liquidity, their profitability decreases, and if they increase their profitability, they will have to reduce their liquidity.

Liquidity of bank refers to reserves of cash, securities, bank's ability to convert an asset into cash, and unused bank lines of credit. Liquidity must be adequate to meet all maturing unsecured debt obligations due within a one-year time horizon. Despite different approaches that can be used to analyze bank's liquidity, the following are the key ratios that can be used to examine bank's liquidity: Cash-Deposit Ratio (CDR), Credit-Deposit

Ratio (CRDR) and Investment-Deposit Ratio (IDR) and whether they could be converted quickly to cover redemptions. On the other hand, profitability of the bank determines its ability to increase capital (through retained earnings), support the future growth of assets, absorb loan losses and provide return to investors. The key financial ratios that are used in assessing the profitability of a bank include: Return on Assets (ROA), Return on Equity (ROE), Net Interest Margin to Total Assets, and Operating Profit to Total Assets. Keeping this in mind, banks have to do a balancing act between liquidity and profitability.

Objectives of the study:

- To know the relationship between management of liquidity and profitability of the banks]
- To be aware about the effect of liquidity management on profitability

Research Questions:

- Is there any impact of liquidity management on profitability of banks?
- Whether the impact is positive or negative

Significance of the Study:

The said study will be helpful to the new burning researcher of finance in the field of impact of liquidity management on profitability by providing relevant literature in order to build the better insight of that area.

Review of Literature:

Spacious studies in different countries of the world have been conducted to investigate the factors that impact a bank's LQD Previous studies play a significant role in conducting any type of research. Thus, the researchers by taking guidelines form such studies can make their research more valuable. The few studies that are related to our research are given below:

Sopan and Dutta (2018) investigated the bank-specific factors and macroeconomic factors that influence the banks' LQD in India. Bank-specific determinants contain bank-size, deposit rate, profitability, asset quality, funding cost and the rate of capitalization in a bank. While the macroeconomics factors include GDP and inflation rate. The results indicated that among internal (bank-specific) determinants, the size, profitability level, funding cost, and the quality of assets negatively impact the LQD risk of Indian commercial banks. Whereas, the rate of deposits and the capitalization rate have a positive influence. Amongst the macroeconomic determinants, inflation rate and GDP growth rate have a positive and negative association with bank LQD respectively.

Almaqtari et al. (2018) studied internal and external factors that influence of commercial banks' profitability in India.

Singh and Sharma (2016) investigated internal and external determinants that determined the Indian commercial banks' LQD. They revealed that bank ownership impacts LQD of commercial banks. They suggested that all bank-specific factors except (cost of funding) and macroeconomic determinants except (unemployment) have a significant impact on commercial banks' LQD.

Sheikhdon and kavale (2016) concluded that significant linear relationship between Account receivable management, Account payable and cash management on commercial banks performance in Mogadishu. Questionnaire was used as a method of data collection. The target population was 112 employees of commercial banks in Mogadishu. The sample size of 87 respondents was selected using slog van's formula. By using SPSS version the data was analyzed.

Ibe (2013) discussed that liquidity management was an important problem in the Nigeria. There was need for banks to examine the optimal liquidity position to resolve such problem. The data was collected from three banks which was selected randomly represent the whole banking sector of Nigeria. Profitability represents the after tax profit dependent variable and the liquidity management is independent variable which include the Bank cash assets (CA), Bank Balance, Treasury Bills and certificate. Regression was used to analysis the data.

The variables:

variables are used to examine liquidity management effect on banks profitability. Banks profitability is measure using return on assets (ROA), return on equity (ROE) and earning per share (EPS) respectively. A number of variables are used as a proxy of liquidity management.

Dependent Variable:

Banks profitability is taken as a dependent variable of the study and to measures Banks profitability two proxies i.e. Return on Assets (ROA) and return on equity have been used.

Independent Variable: Liquidity Management Practices is used as an independent variables and to measures Liquidity Management Practices four ratios i.e. Current Ratio, Advances to deposit ratio ,Cash deposit ratio and Deposit Assets Ratio to be used.

Econometric model specification

To be aware about the impact of liquidity management system on banks performance in India following two regression equations are implemented.

ROA=B0+B1CR+B2ADR+ B3CDR+ B4DAS+Ui

ROE=B0+B1CR+B2ADR+ B3CDR+ B4DAS+Ui

Data Analysis and Interpretation:

The descriptive statistical analysis resulted that the data used for profitability measurement of banks in India like ROA and ROE produced the averaged of 1.893 and 1. 935, respectively. The mean values is found to be 5.735, 83.049 and

41.640, respectively. here the profitability performance of public sector banks have are found very low compare to private sector banks.

Conclusion:

Interest coverage ratio has positive and significant relationship with banks profitability when it analyzed by banks profitability determinants return on assets and return on equity as quick ratio has positive and significant relationship when evaluate using return on equity .

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