Bankers Opinions Regarding Factors Responsible for Financial Performance of Indian Banking Sector

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Abstract

Banks are trying to manage costs better, deepen relationships with customers and enhance product mix and pricing decisions. These and other factors are causing banks to re-examine and improve the ways in which they measure and report business performance. The present study analyze the bankers opinions regarding factors responsible for the financial performance of Indian banking sector and based on the primary data which is collected through the survey of the 352 bankers in Haryana with the help of well structured questionnaire. Analysis of the data through various statistical techniques such as mean, percentage and frequency and for testing the hypothesis, ANOVA has been applied. It was found that market related factors were affecting the performance of the banks in India.

Key Words: - ANOVA, Banks, Financial, Market, Performance, Survey.

Introduction

After the financial crisis that began in 2008, banks are taking steps to improve their performance measurement capabilities in light of changed economic and market conditions and new management needs. For example, new regulatory strictures are affecting the underlying economics of such businesses as payment-card issuing and processing. Capital requirements are increasing for most banking businesses. New channels like mobile phones are becoming more important. Revenue growth continues to be difficult to achieve due to weak economic conditions, low interest rates and regulatory restrictions. Banks are trying to manage costs better, deepen relationships with customers and enhance product mix and pricing decisions. These and other

factors are causing banks to re-examine and improve the ways in which they measure and report business performance.

Some major areas of emphasis and trends are emerging across the industry:

- Reviewing and enhancing organizational management profitability-reporting methodologies;
- Emphasizing the use of business-unit key performance indicators (KPIs);
- Refining customer- and channel-profitability measurement and analytics;
- Improving alignment of the components of the performance management process;
- Improving systems support and automation of the performance management process;
- Improving data quality and consistency.

Performance Measurement Methodologies

Banks have their own performance measurement improvement agendas tied to their unique needs and strategies. For some banks, these are continuations of prior efforts, while for others they are new initiatives. Banks are reviewing and enhancing key organizational management profitability-reporting methodologies to reflect changes in business models and their underlying economics. One focus is harmonization with risk management methods and definitions:

- **Cost allocation.** Allocation methodologies are being changed to provide more transparency to recipients and to support better decisions about the use of resources. More attention is being paid to understanding fixed and variable cost structures and cost and volume variances. Deeper analyses of channel costs are being developed. For certain categories of costs, such as overhead or administrative functions, allocations are being simplified to streamline budgeting and profitability-reporting processes.

- **Funds transfer pricing.** FTP curves are being changed. The use of the swaps curve as opposed to LIBOR for maturities between three months and one year is becoming more common. Liquidity premiums are being added to reflect the banks' specific funding costs at each point in the curve. More analysis is being performed on the core deposit book to determine its "stickiness."

- **Credit charges.** Approaches to assigning provision for credit losses are being modified. The use of Basel-driven expected losses versus GAAP provision is being considered. Further, the implications of "mark-to-market" loan valuation under accounting

pronouncements such as SOP 03-3 and FAS 141-R on monthly line-of-business results are being analyzed.

- **Capital allocation.** Banks that attribute equity to lines of business for organizational-profitability reporting are revising their methodologies for doing so. Because regulatory capital requirements are being raised, banks are not using economic capital calculations as the sole bases for line-of-business (LOB) capital attribution. Instead, combinations of economic capital, regulatory capital and goodwill attributions are being used. Despite the new capital attribution methodologies, considerable shareholder equity continues to be held at the "top of the house."

- **Inter-LOB revenue and expense-sharing arrangements.** Banks are reviewing the methods by which revenues and expenses are shared among LOBs. They want to promote cross-selling, as well as to understand the true stand-alone economic value of each business line. In some cases, flat amounts or percentages of revenue are being put in place for cross-sales or referrals between LOBs.

Review of Literature

Omotola and Roya (2011) found that recent global economic meltdown triggered by the subprime mortgage crisis of United States in 2007 and its adverse effect on financial markets and participants in the financial industry worldwide have resulted in a capital management crisis in most financial institutions especially banks. This study was a case for the Nigerian banking industry, focusing on factors affecting risk management efficiency in banks. For empirical investigation, it employed Panel regression analysis taking a stratum of time series data and cross-sectional variants of macro and bank-specific factors for period covering 2003 to 2009. Result for panel regression indicated that risk management efficiency in Nigerian banks was not just affected by bank-specific factors but also by macroeconomic variables.

Thiagarajan, Ayyappan and Ramachandran (2011) analyzed the role of market discipline on the behaviour of commercial banks with respect to their capital adequacy and concluded that the commercial banks are well capitalized and the ratio is well over the regulatory minimum requirement. The private sector banks show a higher percentage of Tier-I capital over the public sector banks. However the public sector banks show a higher level of Tier-II capital. The study

also indicated that the Non-Performing Assets influenced the cost of deposits for both public and private sector banks in a significant manner. The return on equity had a significant positive influence on the cost of deposits for private sector banks. The public sector banks can reduce the cost of deposits by increasing their Tier-I capital.

Prasad, Ravinder and Reddy (2011) evaluated the performance of banking sector with the help of CAMEL model which measures the performance of banks on the parameters like Capital Adequacy, Assets Quality, Management Efficiency, Earning Quality and Liquidity. All public sector banks and thirteen private sector banks were analyzed in the study. According to the importance of study, each parameter is given equal weights. Results depict that on average KarurVysya Bank was at the top most position followed by Andhra bank. It is also observed that Central Bank of India was at the bottom most position.

Aregbeyen(2011) studied the determinants of banks selection criteria by banking and business customers in Nigeria. A total of 1750 respondents from six most metropolitan cities across the six geo-political zones were sampled and data was analyzed by percentage and ranking method. The findings of the study reveal that the safety of funds and the availability of technology based service(s) are the major reasons for customers' choice of banks.

Patnaik, Satpathy and Pradhan (2011) studied the customer satisfaction in banks under study in Orissa. A total of 350 questionnaires were served and 284 customers responded. This includes 103 respondents are of AXIS bank customers, 94 are PNB bank customers and rest are of UCO bank of various branches in Orissa. Creditability, customization, consistency in service components, innovation, employee behavior, record maintenance, responsiveness and reliability are identified as key factors influencing customer' service quality.

Sharma and Kumar (2013) analyzed the impact of banking sector reforms on the performance of 15 foreign banks in India in the pre-reform (1987- 1995), post- reform period (1996-2010) and whole study period (1987-2010). The information has been collected from various relevant publications of Reserve Bank of India (RBI) and Indian Banks Association (IBA).In addition to it information has also been collected from various journals, newspapers, magazines and websites etc. The study has included all the twenty-six public sector banks working in India. The

study has undertaken the following variables; Total Assets (X1), Net Interest Margin (X2), Total Expenditure (X3), Total Business (X4), Non-Interest Income (X5), Establishment Expenses (X6), Number of Employees (X7), Number of Branches (X8) and Net Worth (X9). To sum up, under growth and efficiency criteria, all explanatory variables had shown significant impact on the performance of foreign banks. More than 90 percent of variation in total income was on account of undertaken explanatory variables and a very little proportion of variation could be attributed to disturbance variable.

Murerwa (2015) evaluated the determinants of banks financial performance in developing economies with a focus on Kenyan commercial banks. The population of study was all the 44 commercial bank licensed to operate in Kenya as at 31st December 2013. A census study was carried out where primary data from the banks and secondary data from relevant central bank data was used. The study found out that industry factors relating to competition, product innovation and the development of mobile banking mostly affected the profitability of the banks.

Research Objective

The present study analyzes the bankers' opinions regarding factors responsible for the financial performance of Indian banking sector.

Research Hypothesis

To achieve the objectives the following hypothesis are formulated and tested:

H_{01} = There is no significant difference between profile of the bankers with regard to factors responsible for the financial performance of the banks.

Research Methodology

The present study is both exploratory as well as descriptive in nature and based on primary and secondary data. The primary data was collected to achieve the remaining objectives of the study.. For this purpose, a well-structured questionnaire devoted to factors responsible for the financial performance of the banks and response was obtained on five-point scale ranging from 5 to 1. Here 5 means to strongly agreed, 4 means to agree, 3 means to indifferent, 2 means to disagree and 1 means to strongly disagree. The analysis is, thus, based upon the feedback received from the 352 bankers' from public, private and foreign banks carried out in Haryana.The analysis of

data has been made by using various descriptive and inferential statistical tools like Frequency distribution, Percentage, Arithmetic Mean, and ANOVA (one way).

Data Analysis

Table 1a shows that gender profile of the bankers (Respondents). Majority of the respondents i.e. 68.7 percent is male and 31.3 percent respondents are female in the study.

Table 1a: Gender Group of Respondents

S.No.	Gender	Frequency	Percent
1	Male	242	68.7
2	Female	110	31.3
	Total	352	100.0
Table 1b: Age groups of Respondents (in years)			
1	Up to 30	174	49.4
2	30-40	114	32.4
3	Above 41	64	18.2
	Total	352	100.0
Table 1c: Education Qualification of Respondents			
1	Graduate	103	29.3
2	Post graduate	93	26.4
3	Professionals	156	44.3
	Total	352	100.0
Table 1d: Experience of Respondents (in years)			
1	0-5	226	64.3
2	6-10	87	24.7
3	11-15	29	8.2
4	above15	10	2.8
	Total	352	100.0
Table 1e: Location of the Bank			
1	Urban	250	71.0
2	Rural	102	29.0
	Total	352	100.0

Source: Survey

Table 1b shows the age groups of the respondents in years and found that most of the respondents (49.9 percent) are belongs to age group of up to 30 years followed by 32.4 percent belongs to 30-40 years age group and rest 18.2 percent are belongs to age group of above 41years.

As for as the educational-wise of the respondents concern, from **Table 1c** noticed that most of the respondents (44.3 percent) are professional such as MBA, B.Tech, MCA etc. followed by 29.3 percent are graduate and rest of i.e. 26.4 percent are post graduate in the study.

Regarding the experience of the respondents, from **Table 1d** found that majority of the respondentsi.e.64.3 percent having experience in between or equal to 5 years, 24.7 percent respondents are having experience of 6-10 years, 8.2 percent respondents having experience of 11-15 years and few respondents i.e. 2.8 percent are having total experience of above 15 years.

Further as concern for the location of bank branches in which respondents are working **Table 1e** depicts that majority of the branches are established in urban area i.e. 71 percent and only 29 percent of the bank branches are established in rural area.

Table 2:Age-wise response on Market related Factors

S. No.	Market related Factors	F	Sig.
1	Liquidity	0.959	0.032*
2	Interest rate changes	0.099	0.021*
3	Foreign exchange rate changes	3.844	0.001*
4	Selling of assets before maturity	0.440	0.041*
5	Fluctuation in the price of instruments used in capital and money market	1.363	0.020*

Source: Survey   **df**= 2   *Significant at 5 percent level**

Table 2 presents the age-wise response of bankers with regard to market related factors. The ANOVA results at 5 percent level of significance and 2 degree of freedom shows that there is significant association between in liquidity (F=0.959, p= 0.032), interest rate changes (F=0.099, p= 0.021), foreign exchange rate changes (F=3.844, p= 0.001), selling of assets before maturity (F=0.440, p= 0.041), fluctuation in the price of instruments used in capital and money market (F=1.363, p= 0.020) as p- value is less than 0.05,therefore the null hypothesis (H_{01}) rejected and alternative hypothesis is accepted.

Table 3:Age-wise response on Liquidity Factors

S. No.	Liquidity Factors	F	Sig.
1	Structure of the source and use of funds	0.337	0.001*
2	Competition among commercial banks	0.322	0.050*
3	Political situation	0.134	0.002*
4	Government policy	0.229	0.000*
5	Overseas money market conditions	3.011	0.005*
6	Financial crises	1.072	0.044*

Source: Survey   **df**= 2   *****Significant at 5 percent level**

Table 3 depicts the age-wise response of the bankers towards the liquidity factors affecting the performance of the banks in India. It is noticed that there is significant association in structure of the source and use of funds (F=0.337, p=0.001), competition among commercial banks (F=0.322, p=0.050), political situation (F=0.134, p=0.002), government policy (F=0.229, p=0.000), overseas money market conditions (F=3.011, p=0.005), and financial crises (F=1.072, p=0.044) on that are significant at 5 percent level of significance. As p-value is less than 0.05, therefore the null hypothesis (H_{01}) rejected and alternative hypothesis is accepted.

Table 4:Age-wise response on Interest rate Factors

S. No.	Interest rate Factors	F	Sig.
1	Monetary policy adopted by banks	0.340	0.001*
2	Competition among banks on market share	0.859	0.021*
3	Narrow spread between deposit and lending interest rates	3.448	0.033*
4	Structured product crises	0.374	0.688

Source: Survey   **df**= 2   *****Significant at 5 percent level**

Analytically, the result of ANOVA is given in **Table 4**, presents age-wise response of interest rate factors affect the financial performance of the banks. It is found that there is no significant association at 5 percent level of significance in structured product crises (F=0.374, p=0.688) as p-value is greater than 0.05, therefore null hypothesis H_{06} is partially accepted where as there is significant association in Monetary policy adopted by banks (F=0.340, p= 0.001), Competition among banks on market share (F=0.859, p=0.021) and Narrow spread between deposit and lending interest rates (F=3.448, p=0.033) as p-value is less than 0.05, therefore null hypothesis is rejected and alternative hypothesis accepted.

Table 5:Age-wise response on Foreign exchange rate changes

S. No.	Foreign exchange rate changes	F	Sig.
1	Increasing volatility	0.014	0.028*
2	Sub-prime mortgage	0.251	0.047*
3	Depreciation of the US Dollar against Asian currencies	0.127	0.034*

Source: Survey   **df**= 2   *****Significant at 5 percent level**

The analysis of bankers' viewpoints with regard to foreign exchange rate changes factors is given in **Table 5**, in which age-wise ANOVA result shows there is significant association (at 5 percent level of significance, degree of freedom is 2) in increasing volatility (F=0.014, p=0.028),

sub-prime mortgage (F=0.251, p=0.047) and depreciation of the US Dollar against Asian currencies (F=0.127, p= 0.034) as p-value is less than 0.05, therefore null hypothesis is rejected and alternative hypothesis accepted.

Table 6:Age-wise response on Credit Factors

S. No.	Credit Factors	F	Sig.
1	Problem in verifying Customer's identity Online	1.816	0.016*
2	Monitoring Problem due to Increased Volume	0.199	0.020*
3	Problem in valuing collateral due to Geographic area	1.011	0.036*
4	Problem in collecting loans due to wider geographic Area	1.539	0.048*

Source: Survey   **df**= 2   *Significant at 5 percent level

Analytically, the result of ANOVA at 5 percent level of significant and degree of freedom is 2 is given in **Table 6**, shows the bankers age-wise response of Credit factors which affect the financial performance of banking sector in India. So, there is significant association in problem in verifying customer's identity online (F=1.816, p=0.016), monitoring problem due to increased volume (F=0.199, p=0.020), problem in valuing collateral due to geographic area (F=1.011, p=0.036) and problem in collecting loans due to wider geographic area (F=1.539, p=0.048). As the p-value is less than 0.05, therefore the null hypothesis (H_{01}) is rejected and alternative hypothesis is accepted.

Table 7:Age-wise response on Others related Factors

S. No.	Others related Factors	F	Sig.
1	Difficult macroeconomic environment	8.834	0.000*
2	Inadequate risk management systems	5.966	0.003*
3	Poor corporate governance	1.507	0.023*
4	Nonperforming assets	3.074	0.048*
5	Chronic liquidity challenges	2.967	0.050*
6	Diversion from core banking to speculative activities	0.396	0.673
7	Foreign exchange shortages	0.282	0.755
8	Rapid expansion drives	1.977	0.140
9	Unsustainable earnings	2.012	0.135
10	Creative accounting	0.796	0.994
11	Insufficient regulatory framework	1.173	0.011*
12	Ineffective credit risk system	0.266	0.049*

Source: Survey   **df**= 2   *Significant at 5 percent level

The analysis of bankers' viewpoints with regard to others related factorsis given in **Table 7**, in which age-wise ANOVA result shows there is significant association (at 5 percent level of significance, degree of freedom is 2) in difficult macroeconomic environment, inadequate risk management systems, poor corporate governance, nonperforming assets, chronic liquidity challenges, insufficient regulatory framework and ineffective credit risk system whereas no significant association in diversion from core banking to speculative activities (F=0.396, p=0.673), foreign exchange shortages (F=0.282, p=0.755), rapid expansion drives (F=1.977, p=0.140), unsustainable earnings (F=2.012, p=0.135)and creative accounting (F=0.796, p=0.994). On the basis of above, the null hypothesis (H_{01}) is partially rejected as p-value is less than 0.05 in case of difficult macroeconomic environment, inadequate risk management systems, poor corporate governance, nonperforming assets, chronic liquidity challenges, insufficient regulatory framework and ineffective credit risk system. Therefore, alternative hypothesis is accepted.

Findings

It may be concluded from above study that there is number of the factors which are responsible for the financial performance of Indian banking sector. In study, age-wise response of bankers with regard to market related factors; it is found that there is significant association between in liquidity, interest rate changes, foreign exchange rate changes, selling of assets before maturity, fluctuation in the price of instruments used in capital and money market. Further in liquidity factors, noticed that there is significant association in structure of the source and use of funds, competition among commercial banks, political situation, government policy, overseas money market conditions, and financial crises. With regard to interest rate factors, found that there is significant association in monetary policy adopted by banks, competition among banks on market share and narrow spread between deposit and lending interest rates. And there is significant association in problem in verifying customer's identity online, monitoring problem due to increased volume, problem in valuing collateral due to geographic area and problem in collecting loans due to wider geographic area with regard to age-wise response on credit factors. As far as other factors, there is significant association in difficult macroeconomic environment, inadequate risk management systems, poor corporate governance, nonperforming assets, chronic liquidity challenges, insufficient regulatory framework and ineffective credit risk system.

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