ABSTRACT

The Banking System forms the core of the Financial Sector of any economy. The role of Commercial Banks is more relevant in developing economies. The nationalization of 14 major Banks in 1969 and another 6 Banks in 1980 and implementation of reforms, resulted in a shift from Class Banking to Mass Banking, traditional banking to e-banking to more profitable, efficient and sound Banking System. The recent global financial crisis has led to a realization of the inadequacies in the Global Banking Sector, which in turn, has manifested in the declining public confidence in the Banking Industry. The ROA showed a divergent trend across various economies and in general, witnessed a declining trend. The analysis of top 100 Global Banks shows the trends of moderate shift in the Global Banking business from advance economy to emerging market economies continue. Since the slippage ratio of the Banking System, which showed a declining trend during 2005 – 08, increased during subsequent period, the Banks need to refine their risk management skills, strengthen their due diligence, credit appraisal and post sanction loan monitoring systems. Banks need to innovate and use appropriate technology to bring down their intermediation costs while protecting their bottom lines. Assessment of previous literature shows the lack of consistency in approach for performance analysis of Banks. Therefore, more sophisticated performance evaluation measures are needed in order to better understand the functioning of Banks and their performance in the whole system.

An effort has been made in this Study for exploring the two major research questions: Why was the reforms needed for Indian Banking System? and Did the implementation of the reforms measures contributed towards improvement in financial performance of Indian Commercial Banks? The overall objective of this study is to assess the impact of Banking Sector Reforms on the financial performance of Public and Private Sector Banks, which is measured through Profitability (ROA) of the Banks (Dependent Variable). Profitability of the Banks depends and relies upon few performance indices (Volume and Size, Efficiency and Asset Quality), which are Independent Variables. Several literature have been reviewed for this study to highlight the research work already done on the subject in India and abroad which proved beneficial to delineate the various issues and methodologies adopted. Due to
changes in Banking policies and practices during the last 20 years of reforms period, it was appropriate to evaluate the impact of reforms measures on the overall performance of Commercial Banks for the said period 1991-92 to 2011-12. The study has been conducted by using specific financial ratios. These ratios have been classified into five Performance indicators viz. Volume and Size, Efficiency, Profitability, Asset Quality and Soundness. Statistical tools viz Mann-Whitney U test and Karl Pearson Correlation Coefficient, have been used to analyze the relevant data, in SPSS 16.0, for testing the Hypothesis framed for the study. The study has been conducted Group-wise on PSBs and PBs Groups, containing all the 26 Public and 20 Private Sector Banks, operating in our Country. The period of study is in two phases: One for the period 1991-92 to 1997–98 (Narasimham Committee–I) and second for the period 1998-1999 onwards (Narasimham Committee–II) till 2011–12. The study relied on the secondary data such as Annual Reports of the Commercial Banks, Publications of Reserve Bank of India, Indian Bankers Association (IBA), Indian Institute of Banking and Finance, National Institute of Bank Management. The Research Methodology for the purpose of current study has been so adopted that it reflected the realities and had helped in reaching the logical conclusion in an objective and scientific manner.

Indian Commercial Banks have made good progress in all performance parameters including annual deposits and credit growth, profitability and trend in NPAs, with overall Capital Adequacy touching 14 percent as on 31st March 2012. However, some adverses have also been faced by the Banking System. While the reforms process has thrown open galore of opportunities for Indian Banks, there are host of challenges also emanating from the same. Business per branch of PSBs was higher than PBs during 1991-92 to 1994-95, and there after PBs were ahead. PBs performed better in terms of Profit per branch, except from 2007-08 onwards, when PSBs have overtaken. The performance of PBs was much better than PSBs when viewed from the Business per Employee from 1993-94 till 2008-09 and from 2009-10 onwards PSBs are performing better. Performance of PBs with regard to Profit per Employee has been consistently good during the entire period of the study as employee cost of PSBs were more due to the changing composition of the staff and increased provisioning requirements towards superannuation liabilities in 2004-05. The study brought to light that PSBs have not been technology responsive as much as their
counterparts in Private Sector. PSBs also lack appropriate strategic planning resulting in lower operational efficiency. **Return on Asset (ROA)** of PSBs during phase I was negative due to marked decline in net profits on account of higher provisions made towards implementation of prudential norms. PSBs started earning positive returns from 1996-97 onwards and had maintained edge over PBs till 2004-05. Higher ROA was achieved by certain PSBs whose Interest Income had improved as the Reserve Bank has allowed Banks to recognize income on an accrual basis in respect of some categories of projects under implementation with time-overruns. **Return on Equity (ROE)** in case of PSBs, have seen a negative variation during 1995-96, 1998-99, 2000-01, 2004-05, 2005-06, 2009-10 and 2010-11 due to impact of raising fresh capital and ploughing back of profits. The decline reflected lower Profitability during 2004-05 for SCBs and higher provisioning requirements in 2010-11, for housing loans extended by SBI and Associates at teaser interest rates. ROA and ROE declined marginally during 2011-12, reflecting deceleration in the Net Profit of Banks caused by increased interest expenditure. Significant variations are observed in **Net Interest Margin (NIM) (Spread)** across the Bank Groups, due to the varying quantum of fee-based income earned. PSBs had much better spread than the Private Sector Banks from 1991-92 till 2006-07. A subdued interest rate environment coupled with a low credit off-take partly explains the decline in the NIM. The increase in NIM could be due to variations in interest rates prevalent at different points of time during the year while it may remain unchanged if the overall return on funds and overall cost of funds during the year increases more or less by the same margin. There is a need to bring down NIM to improve efficiency of Financial Intermediation. The analysis of profitability indicators undertaken in the study reveals that PSBs have shown the downbeat tendency during 1992 - 97, shown the positive trend thereafter in the performance of all the profitability ratios.

On the basis of the current study and findings thereof, it has been suggested that Mobile Banking should be accorded a thrust area, as it has got potential scope for Profitable Business, due to its penetration and reach. Banks may take advantage of deregulation of Savings interest and mobilize higher CASA Balances, from select customer segment, to reduce the average cost of funds and thus improving the operating margins. The Banks may scout for increasing share in Wealth Management products/facilities as the same is likely to have rapid accumulations in the years to
come, due to the economic prosperity of a section of the society. The Banks to adopt low cost Branch network model with smaller size Branches. Further, in order to minimize operational costs, Banks to encourage -Use of Electronic Payment System and minimize use of cheques, Processing charges to be levied on every Dividend/Interest warrant deposited in the account to encourage opting for electronic payment (direct credit to the account) by the Investors, Suitable charges may also be levied for high (both in amount and frequency) cash withdrawals and deposits to avoid increased dependence or slippage to cash-based transactions, In case of loans, the practice of obtaining Post-dated Cheques should be completely stopped and loan repayments should be through electronic payments only. The Indian Banking System is moving towards a more cohesive and strong system, capable and responding to the dynamic economy.

The future reforms process need to be so designed that it should focus on ensuring sustained viability and efficiency of the Banking System. The future reforms should contain, among others, the following like - Policy Framework for NPAs, Legal Reforms for faster recovery, Improvement of operational efficiency, Reducing the entry Barriers of new Private Sector Banks, Consolidation of Indian Banking System to create Global Bank, Withdrawal of directed lending, Compensation Policy.

**Keywords:** Mass Banking, Credit Appraisal, Reforms process, Net Interest Margin, Electronic Payment System, Non-Performing Asset