CHAPTER 3

RESEARCH METHODOLOGY

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3.1 INTRODUCTION

Banking sector reforms in India strive to increase efficiency and profitability of the banking institutions. the existing banking institutions has to face the global competition. As a consequence, there has not only been rapid expansion in the number of banking institutions in the country, but the banking horizon of the country has also changed significantly with the entry of new private sector and foreign banks. As of now the country has public sector, old private sector, new private sector and foreign banks operating side by side and giving cut-throat competition to each other. Apparently, these different types of banks differ significantly from each other in terms of financial performance including operational efficiency.

A well planned, organized, efficient and viable banking system is necessary commitment of social and economic infrastructure in an economy. Bank plays an important role in undertaking the development effort and works as a channel for social economic transformation as well as a catalyst to economic growth.

Banking sector of India has passed through different phases from privatization to socialization and then to nationalization and now again to privatization. Fourteen major banks were nationalized in 1969, with the primary objective of emphasizing their role as investment of social and economic transformation of country. It was followed by another six banks in 1980. After submission of Narshimhan committee recommendations, the whole banking scenario in India has set on the path of economic liberalization and globalization. Today, Indian bank management is facing two-faced challenges to improve their profitability on the one hand and to serve the social objective on the other. Hence, appraisal of financial performance of State Bank of India is needed for the development of the banking sector.

3.2 TITLE OF RESEARCH PROBLEM

The title of the research problem selected for this study is **"Evaluation of financial performance of State Bank of India (2005 to 2010)".** It consists of

1. Profit and Profitability of State Bank. Of India
2. Branch Productivity and Employee Productivity in State Bank. Of India
3. Deposits and Advances position in State Bank. Of India
4. Other social issue like priority sector lending by State Bank of India.

The financial performance cannot be evaluated only on the basis of traditional method of rate of return on funds employed, but more effective indicators like employee productivity, branch productivity, and priority sector lending performance are also required to be studied. It is also interesting to appraise the financial performance of State Bank of India in the rapidly changing banking environment in general and after banking sector reforms in particular.

3.3 LITERATURE REVIEWS

Some studies relating to financial performance of commercial banks in India conducted in the past are being reviewed below:

Maharashtra State government [1] made first attempt to publish literature on productivity in banking industries in 1966. A seminar on productivity in Indian banking industry was organized during the Indian productivity year 1966. As it was a first attempt, it cleared only conceptual aspect of productivity in banking industry.

Banking commission reviewed [2] Indian banks operating methods and procedures and made recommendations for improving and modernizing operating methods and procedures. It studied issues relating to customer service, credit procedures, internal control system, cost structure and profitability. It also examined other relevant aspects of banking like training and employee appraisal, information system and productivity and management development. It suggests measures to improve profitability. Banking commission recommended fixing of man-hours for different types of jobs for measuring productivity of employees. It suggested that branch profitability was not the appropriate method hence an integrated costing and financial reporting system is needed. It also suggested the use of various ratios for the measurement of the operational efficiency of branches.

O.B. Sayeed [3] in his Ph.D. research examined correlates of organizational health productivity and effectiveness in the SBI. The study is related to productivity and effectiveness. It is focus on the psychological aspect.

P. Singh [4] compared the 14 Indian nationalized banks in terms of changes in their profit and profitability, in the pre nationalization and post nationalization periods. He concluded that recruitment, promotion, branch expansion, deployment of personal and business growth had a very favorable impact of profitability of banks, if they are carried out in judicious manner. He suggested that key to profitability should lie essentially in higher volume of business per employee and higher volume of business per branch.

S. G. Shah [5] in his various studies discussed bank profitability and productivity. He expressed concurrence about slow growth in productivity and efficiency, wrong work practice, doubtful and overdue debts and increased expenses and overheads. He disapproved the attitude of Indian banks that higher profitability can result from increased spread and that innovations have a limited role. He emphasized on reduction of cost, creation of team spirit, improvement in the management for improving bank profitability and productivity.

J. C. Luther [6] chaired the committee appointed by RBI to study the productivity efficiency and profitability of Indian commercial banks. The committee studied the various issues related to planning, budgeting, marketing information system, performance evaluation system and other relevant issue like annual accounts, trends in earnings expenses and profitability. The major recommendations where (I) Bank should transfer at least 40per cent of the disclosed profit to reserve, free of taxation. (ii) The interest on additional cash reserves in excess of the minimum 3per cent should be related to cost of funds for banks. (iii) To improve productivity, efficiency and profitability of banks, a well planned, prompt and regular flow of information and its analysis is essential for banks to contemplate timely corrective actions. (iv) To estimate the cost of various services and profitability of various activities, the RBI in collaboration with commercial banks should organize regular and systematic surveys. (v) There should be uniform system of audit for all types of bank. Simplification of system and procedure in banks is essential to bring economy in expenses and provide better customer service.

R. C. Bhatia [7] studied the economic performance of the Indian banking system. In his study profitability of banking system measured the ratio of profit as a percentage of capital and profit as a percentage of assets. The major findings of the study were: (I) the profit performance of the Indian banks during the period 1950 to 1960 showed an upward trend. (ii) Number of bank offices and the deposit concentration ratio showed an insignificant effect on its performance during 1950 to 1968. (iii) There was significant difference in the levels of intermediation of different banking sectors in India during the period under review. (iv) None of the sectors showed any significant profitability differences (v) Output performance of the Indian banking system can be improved by the suggestion, that the banking rules in India should not emphasize on direct regulation of the rate of return as much as the regulation of the asset portfolio of banks.

O. P. Mathur [8] attempted to describe and analyze the public sector banks in Indian economy by selecting a case study of the State Bank of India. The main findings of the study was that the State Bank of India has accelerated the growth of Indian economy in two different ways (I) By rural branch expansion (ii) By playing a leading role in the priority sector lending and development of backward regions.

H. C. Sarkar [9] in his research paper studied the profits of Indian public sector banks over a time frame and suggested that banks need greater maneuverability in their routine operations so as to achieve the dual objective of profit with growth.

V. V. Divetia and T. R. Venkatchalam [10] studied operational efficiency and profitability of banks and proposed to create a composite index. They used the size of bank as represented by its total deposit as a rough yardstick of its performance. A set of 8 indicators is chosen which is further classified into indicators of (a) Operational efficiency in terms of productivity (b) Operational efficiency in social objectives(c) Profitability.

L. G. Kurkarni [11] in his paper compared developmental responsibility and profitability of banks. He reviewed that one of the important reasons for the decline in profitability of banks is the developmental responsibility undertaken by them. He suggested that carrying of developmental business could be possible as well as profitable only by reducing costs, improving systems and improving productivity.

S. G. Shah [12] in his paper analyzed weaknesses of the banks and pointed out the specific areas where action could be taken to improve profitability. He revealed that rising expense and overheads increase in wasteful work practices, declines in productivity were major weaknesses. He suggested these following areas for improving profitability of banks. (I) to evolve measures that could widen the spread between the cost of funds, services and administration and the return on them. (ii) To developed supplementary sources of income. (iii) To find profit centers and cost centers in the bank. (iv) To assess the extent to which these elements of the structure could be influenced by policy and planning or by changing the nature of operations. (v) To recognize the elements that controls or settles the income and cost structure at each such center and for the bank as a whole.

K. Ganesh [13] in his paper studied the effectiveness of monitoring system profit centers, standards for comparison and management information system. The study suggested that the working fund as the base for the purpose of comparing profitability at the branch level is inadequate and he related it to the total business.

Makrand [14] studied the performance of public sector banks. He selected six quantitative indictors for performance index. Which were, branch expansion, priority sector lending, deposit mobilization, export credit, net profit to working funds and wages-cost of business development. The main recommendations of his study were (I) counseling and expert opinion to the priority sector lending on diversified activities is needed. (ii) The lower level staff should also actively be involved in priority sector lending activities. (iii) Necessary lending power should be vested with the branch managers.

H. N. Aggarwal [15] studied the concept of social obligations of banks. The study recommended that, providing more branch offices to the public, particularly in semi-urban and rural areas, providing greater credit facilities to the public as well as to the priority sector. Helping, (1) Generation and maintenance of employment opportunities in the country (2) Financing the government securities and popularizing the bill form of credit.

Nayan Kamal [16] recommended a model for evaluation of performance of commercial banks. He suggested that the basis of all the important and quantifiable parameters of performance, an integrated performance index needs to be developed, which will act as a model for evaluating the performance of commercial banks.

V. B. Angadi and V. J. Devaraj [17] in their paper studied that difference in cost of working fund, interest earning, social banking, funds management, other than income, expansion of banking business, banking services are the main factors contributing to difference in productivity and profitability ratios of the banks.

J.C Desai [18] studied staff productivity in banks. Basic objective of the study was to detect and correct staffing imbalances. He felt that in service industries like banking with wide variations in work mix, a universally applicable and fully scientific formula is difficult to evolve in any area of management.

A. K. Kanthale [19] observed in his paper that credit policy of the government has a great impact on the profitability of banks and there remains hardly a factor or determinant of working result, which is independent of credit and monetary policies.

P. N. Joshi [20] studied the trend of gross and net profits of Scheduled Commercial Banks. His conclusion is as follows: (I) Lower capacity for fund management of the banks was due to statutory liquidity ratio, cash reserve ratio, and priority sector lending. (ii) Lowering yield and rising cost rate year by year. (iii) Declining demand from the corporate sector for bank funds had seriously contributed a lot to the decline trend in profitability.

Kiran Chopra [21] studied the emerging trends in the profitability of selected public sector banks at micro level. She recommended the need for the introduction of management essentials for efficient management of profit and profitability of public sector banks and suggested proper management of both costs and earnings.

Vipin Shah [22] in his imperical work cost and efficiency in banking studied the factors affecting costs, earnings and efficiency of banking services at branch level. He evaluated the relationship between size and costs at bank branch level. He suggested that activity wise cost and efficiency studies at branch level would be helpful for improving operational efficiency of rural and urban branches. He was of the opinion that the size of the bank was an important variable affecting costs, earnings and efficiency of banking services.

A. K. Vashist [23] in his study titled "Performance appraisal of commercial banks in India", evaluated the performance of public sector commercial banks with regard to six key indicators i.e. branch expansion, deposits, credit, priority sector advances, DRI advances and net profit. He developed the composite weighted growth index, which is used for ranking the banks. For improving the performance of commercial banks, he suggested (I) the developing of marketing strategy for deposit mobilization (ii) profit planning and strength, weaknesses, opportunities and threat analysis in commercial banks.

S. Singh [24] in his paper noted that profitability of the banking system has been subject to several stresses and strains due to many factors. Those being continuous increase in SLR, CRR, persistent emphasis on social goals, growing incidence of industrial sickness, rapid branch expansion in rural areas, unfavorable changes in the deposit mix and growing incidence of financial disintermediation.

H. P. Rao [25] in his study made a comparison of business ratios of profit making and loss making rural branches of nationalized banks. He pointed out that the main reason for less profit is the low volume of business. He recommended monitoring the break even business level for the banking sector to be of great importance for improving profitability.

J. Oza [26] in his paper made an international comparison of productivity and profitability of public sector banks in India. Analyzing the productivity of public sector banks, he observed that there has been substantial growth in productivity per employee.

K. Srinivas Rao [27] attempted to study the productivity in banking. The study covered productivity of the banking industry as a whole in the country. This work heavily stresses on profitability. He concluded that social banking has become an essential ingredient of productivity alongside conventional banking.

S. Garg [28] attempted to study the main determinants of cost, profits and profitability of banking sector and also studied the intergroup differentials of SBI and its subsidiaries, nationalized banks, private sector banks and foreign banks. He observed that the operating income of all bank groups increased as lower rate as compared to operating expenses, which resulted in a decline in profitability.

B. Murugesan and K. Chandrashekhar Rao [29] in their paper studied profit, productivity, profitability and social objectives in public sector commercial banks in India. They suggested 21 indicators for evaluation of the performance of commercial banks.

B. Satyamurty [30] identified 26 ratios categorized into 6 different groups of performance. Their interrelationship he observed can be interpreted for a systematic & needful evaluation of productivity and profitability performance of banks.

M. R. Vyas [31] studied financial performance of regional rural banks in Rajasthan. He analyzed the financial performance with the help of quick ratio, credit deposit ratio, and profit to proprietor's capital ratio and working capital analysis. He concluded that regional rural banks had a bright future as an effective instrument in the economic growth and up-liftment of downtrodden sections of Indian society particularly in rural area.

N. A. Shan hag [32] in his paper evaluated various target based social obligations assigned to banks from time to time after their nationalization. He suggested re-grouping of the priority sectors with the contemporary relevance.

J. Panda and G. S. Lall [33] in their paper attempted to develop internal management techniques for improving the profitability of the Indian banks. They identified most important factors influencing the profitability i.e. productivity development of funds, quality of advances, information system organizational setup and branch expansion policy.

M. N. Mishra [34] in his paper evaluated the profitability of Scheduled Commercial Banks taking into account the interest and non-interest income and interest expenditure, manpower expenses and other expenses. The author has identified that the growing pre-emption of funds in the form of statutory liquidity ratio, cash reserve ratio, faster increase of expenses as compared to the income, advances and total investment than interest income and few more factors have contributed to the declining profitability of Indian commercial banks.

A. M. Sadare [35] analyzed public sector banks, private sector and foreign banks for a period of six years from 1985 to 1990. He concluded that policy supports as well as effectiveness is important factors for improving the profitability of banks.

M. Chandra [36] in his article studied the aspects of Public Sector Banks profitability. He concluded that despite huge working funds, public sector banks were not able to show better results due to high cost operation on account of priority sector advances and more than 56 percent branches being rural.

A. V. Rajagopalan [37] in his paper has given an overall view on productivity in banks. He concluded that profitability and productivity depends on various factors like reduction of costs, recovery, work reorganization, computerization etc. He opined that establishment expenses play a key role in determining the level of profit. He suggested that attention should be given on staffing pattern.

Jagwant Singh [38] has analyzed productivity of Indian banks. He has used 17 indicators that can be categorized into three main indicators i.e. per employee indicators, per branch indicators and financial indicators. He observed that United Commercial Bank was the one bank that from all angles was giving poor performance after nationalization. SBI was able to make considerable improvement in its productivity. He recommended that all the banks should set up productivity cells.

Amandeep [39] in her work on profitability of commercial banks has made an attempt to examine the trends in profits and profitability of twenty nationalized banks. She used trend analysis, ratio analysis and concentration indices of the selected parameters. She also used multi variant analysis. She concluded that to have excellent profitability performance, banks need to have excellent performance in managing burden.

H. L. Verma and A. K. Malhotra [40] in their study on fund management in commercial banks have attempted to examine the fund management in selected five nationalized banks. They concluded that the selected nationalized bank has experienced a very low profitability. They observed inadequacy of capital fund, phenomenal growth in deposits, less borrowing from Reserve Bank of India, improvement in liquidity position and remarkable performance in priority sector lending.

3.4 OBJECTIVEW OF THE RESEARCH STUDY

1. To analyze the financial performance of State Bank of India.
2. To measure branch productivity and employee productivity of State Bank of India.
3. To analyze the trends of deposits and advances of State Bank of India
4. To study the priority sector lending by State Bank of India
5. To search out the major problems and prospects of the banking sector.
6. To suggest an appropriate strategy for improvement of financial performance of sample banks.

3.5 HYPOTHESIS

In order to carry out this study scientifically, the following hypotheses have been formulated.

Hypothesis No. 1

Null Hypothesis: Financial performance of State Bank of India is independent of banking sector reforms.

Hypothesis No. 2

Null Hypothesis: Productivity performance of State Bank of India is independent of banking sector reforms.

Hypothesis No. 3

Null Hypothesis: Priority sector lending by State Bank of India is independent of banking sector reforms.

3.6 SOURCES OF DATA

The study is mainly based on secondary data obtained from the annual published reports of SBI. Financial Annexure published. Data necessary for testing the validity of hypotheses are obtained from published annual reports of the State Bank of India for different years. Other publications of State Bank of India, Reserve Bank of India and Indian Bank Association bulletin and reports of different task forces, study groups and committees provide other necessary data required for the study, besides information has also been taken from different publications, various books, periodicals, journals etc.

3.7 PERIOD OF RESEARCH STUDY

Present study has been made covering the period of 5 years from April 2005 to March 2010. The period of time before the year 2005 and even after 2010 has also been considered wherever necessary.

As the process of nationalization of commercial banks was completed, reformation and globalization of the banking sector, period of latest 5 years from 2005 to 2010 has been selected for study. The period of 5 years i.e. from 2005 to 2010 highlights the financial performance of banks in the globalised economy. During this phase, the economy of the India has been grown globally and the role of the banking became prominent for the development of liberalized.

Thus, the selected period provides latest picture of Indian banking for study. The evaluation of changes due to changes in economic policy and the study of financial performance of State Bank of India, which happens to be the market leader in banking industries in India, shall be useful to serve as a model for banking industries in India.

3.8 SCOPE OF THE RESEARCH STUDY

This study covers the financial performance of State Bank of India only. It excludes other members of State Bank of India group. The study also does not make separate analysis of domestic and foreign operations of State Bank of India. The operations at branch level or micro level have not been touched in this study. This aspect is left for further specific research. The data used for this study is based on annual reports and other reports published from time to time. Therefore, the quality of this research depends on quality and reliability of data published in annual reports. Financial performance has been analyzed in aggregate and segmental analysis is left for future research efforts. Since this study is in the nature of a positive empirical research, it is not proposed to enter in the normative aspect and offer suggestion for improvement in the working. The researcher does not have firsthand experience of working in banking industry and, therefore, it is not felt proper to offer suggestions for improvement in financial performance. Since this study is related to State Bank of India only, it is not proposed to make any generalization for universal application.

3.9 TOOLS OF THE FINANCIAL ANALYSIS

The financial health of banks can be diagnosed by analyzing profitability, productivity and trends of deposits and advances. For making such analysis more meaningful various tools or techniques for analyzing the financial data are used. These tools can be classified into two:

I. Accounting Tools
II. Statistical Tools

I. Accounting Tools

For analyzing financial performance and measuring financial efficiency to banks, accounting tools like:

Trend Analysis

2. Ratio Analysis
3. Comparative Statement Analysis, have been used.

II. Statistical Tools

For making the study more scientific and accurate Statistical tools

Like:

1. Arithmetic Mean
2. Index Numbers
3. Diagrammatic and Graphic presentation of data
4. "T"-Test technique, have been used

The performance of banks can be measured by analyzing profitability, productivity and priority sector advances. Profitability is one of the most important and reliable indicators for analysis of financial performance of banks.

3.10 SCHEME OF PRESENTATION

The result of this study would be presented as per the following chapter plan:

Chapter-1 deals with history and development of the banking sector in India, Overview of the State Bank of India, It covers history, organization, structure, corporate philosophy, strength and weaknesses, growth and overall business of State Bank of India.

Chapter- 2 : Conceptual Frame Work and Measurement for "Performance Appraisal" This chapter covers: Concept: Performance, Measurement of Performance ,Concept: Appraisal, Performance Appraisal – Financial Appraisal– Significance of Performance Appraisal – Areas of Performance – Performance Appraisal: Effectiveness in planning, control and in decision making – Performance and Efficiency – Techniques for Performance Appraisal – Objectives of Performance Appraisal – Process of Performance Appraisal – Conclusion.

Chapter-3 covers introduction, the title of the problem, objective of the study, review of earlier literature, period of study, sources of data, framework of analysis, significance of the study, hypothesis, limitation of study and organization of study.

Chapter-4 analyses spread, burden and profitability. It covers the analysis of the trends of income, expenditure, spread, burden, net profit and profitability. It also covers ratio analysis of spread ratios, burden ratios and profitability ratios deals with an empirical analysis of profitability. It covers analytical framework of empirical analysis, empirical analysis of profitability and result of empirical analysis.

Chapter-5 analyses the employee productivity and branch productivity of State Bank of India in terms of deposit, advance, business, total expenditure, total earning, establishment expenses and spread.

Chapter-6 deals with the credit efficiency and productivity with the aspect of State Bank of India. It analyses the trend and ratios of priority sector lending, agriculture lending, small- scale industries lending, small business finance and other priority sector lending, etc.

Chapter-7 presents a summary of the research study and conclusions. It also examines the findings of the study.

3.11 LIMITATIONS OF THE RESEARCH STUDY:

1. The study is restricted to only one public sector bank i.e. State Bank of India. It's quite a small sample. which may not be representing all the common characteristics of the universe.
2. This study is based on secondary data taken from published annual reports and accounts of the bank under study. The reliability of such data is sometimes doubtful as the figures may be polished or grouping and regrouping of figures is also possible. Besides, unit insiders' view can't be revealed in the study.
3. There are different sophisticated methods and techniques for analyzing the profitability and productivity of the sample bank. Application of all the methods and techniques is not possible for the researcher because of time and economic limitations.
4. This research is empirical type of research so it doesn't offer or develop any new concept or reinterpret any existing concept.
5. This research study is restricted to five consecutive years only because of non-availability of data. The trend and conclusion drawn with the help of this five years data only. so. it may not support the past and future performance of the sample bank.

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