CHAPTER - 7
SUMMARY AND CONCLUSION

In order to analyze the patterns of fund deployment by the Scheduled Commercial
Banks and their effect on the overall banking business in India, firstly, we have tried to
examine the changes in sources of banking funds such as, deposits, borrowings, other
liabilities and provisions along with the uses of these funds, namely advances,
investments, other liquid assets as well as cash in hand and balance with RBI, etc. during
the post-reforms period. Next the changes in different performance parameters like profit
and loss, provision and contingencies, interest earned component, interest expended
component, payment to employees and other operating expenses etc. during the study
period have been studied in details. An attempt has also been made to assess the effect of
fund deployment on the overall banking business through ratio analysis technique by
computing over time changes in selected liquidity, profitability and efficiency ratios of
the three categories of banks i.e., the Public Sector Banks divided into Nationalized
Banks and State Bank of India and its Associates, Private Banks, Foreign Banks and their
sample banks used in our study. We have also tried to measure efficiency of the banks in
our study through Data Envelopment Analysis which is a popular presently used non-
parametric approach to efficiency measurement. In the study, we have also tried to throw
some light on the non-performing assets and capital adequacy ratio of the banks
individually and group-wise. To facilitate the analysis the whole period under study
(from 1992 to 2007) has been divided into two sub-periods, viz. 1st sub-period (from 1992
to 1999) and 2nd sub-period (from 2000 to 2007). In this chapter the major findings of the
study have been summarized and conclusions have been drawn.

7.1 Summary of Major Findings

Growth Analysis

The deposits account for nearly 82.48 % of the total source of funds of the
banking sector in India. The borrowings are another important source of funds of the
banking sector while advances and investments are the important avenues for deployment
of funds by the Indian banking sector. The sample public sector banks, namely, Punjab National Bank, Allahabad Bank, United Commercial Bank as well as the Nationalized Banks as a whole have shown a high growth in deposits in the 2nd sub-period in comparison to the 1st sub-period. The results also show that for two sample banks namely Bank of Rajasthan and Standard Chartered Bank, the mobilization of deposits has increased significantly. But the growth rate in deposits has altogether decreased in the 2nd sub-period in comparison to the 1st sub-period group-wise for the Private Banks, Foreign Banks and Scheduled Commercial Banks as a whole in India. In regard to other sources of funds, (i.e. borrowings, other liabilities and provisions) the Private Banks as a whole have done relatively well. The individual sample banks such as SBI, UCO Bank, Punjab National Bank, Allahabad Bank, ICICI Bank and Standard Chartered Bank also have performed well.

The deployment of funds, on the other hand, is a very important area for the commercial banks. Among the avenues of funds deployment, loans and advances (which constitute 49.41% of the total deployable funds) as well as investments (which constitute 37.46% of the total deployable funds) constitute two important heads. The performance in loans and advances parameter by the Nationalized Banks and State Bank and its Associates cannot be undermined, especially in the 2nd sub-period. The sample PSBs too have performed well in the 2nd sub-period; even United Commercial Bank has revived from its previous dilapidated state of condition in the 2nd sub-period, which is a good sign of business indeed for the sample PSBs. The sample private and foreign banks such as Dhanalakshmi Bank, ICICI Bank and ABN Amro Bank have also performed well. On studying the pattern of deployment of funds under the head loans and advances, it is found that the advances have mainly been given as term loans and other loans. In term loans, the SBI and its Associates and Foreign Banks have done well. The sample PSBs too have done well in this parameter. But for the sample private and foreign banks the performance in relation to this parameter has turned out to be worse in the 2nd sub-period. In deployment of funds as other loans, too, the sample PSBs along with ABN Amro Bank and Standard Chartered Bank have done well.

In the investment component the deployment of fund has interestingly decreased in the 2nd sub-period in comparison to the 1st sub-period. However, the growth rate in this
component has been high in both the sub-periods for the Private Banks as a whole. ABN Amro Bank along with Hong Kong and Shanghai Bank has performed well in this component. Among the different types of investments, investment in government and approved securities has turned out to be the largest area of investment by the banking sector in India. This may be a step in order to reduce the size of non-performing assets by the banks. Investments outside India have been good for the Nationalized Banks and State Bank of India and its Associates. It is apt to say from the analysis on the investment component that the banks in general invest more in Government and approved securities. So they are conservative and make investment in those areas where risk is low and return is certain.

The performance of any bank depends on its pattern of deployment of funds and the ways in which these funds are collected. After analysing the sources and uses of funds in terms of over time growth rates, next the banking performance has been evaluated by using growth analysis of selected parameters (like profit and loss, provision and contingencies, interest earned and their components, interests expended and their components, operating expenses and their components) which are the outcomes of the former. It has been seen that the profitability picture in the Public Sector Banks is very gloomy; those banks have incurred losses in many years of the study period. But the profitability condition of Private Banks as a whole is good and particularly among the sample banks ICICI Bank, ABN Amro Bank and Standard Chartered Bank have done well. In terms of interest earned component the Private Banks as a whole have done well and ICICI Bank along with the sample foreign banks have shown a high growth in this parameter. But the share of PSBs in all components of income had been high, which establishes the fact that they are still dominating the Indian Banking Industry even in the matured state of the post-reforms era. In the interest earned on loans parameter the growth rate has been low for the Nationalized Banks but high for the Foreign Banks and Private Banks as a whole. The sample banks such as ICICI Bank, ABN Amro Bank and Standard Chartered Bank have performed well as their growth rates in interest earned on loans are found to be high. A sample PSB i.e., United Commercial Bank has, however, performed well in the 2nd sub-period in this parameter. The interest earned on investments, on the other hand, has shown a low growth rate in both the sub-periods for
the sample PSBs. On the whole, there has not been any remarkable growth in this parameter for the banking sector in general throughout the years of the study.

In the interest expended component it is found that there has been a low growth for the PSBs in both the sub-periods but its mean level is quite high, which indicates that the level of their business activity is quite high. But the expenditure on interest has been too high for the Private Banks as a whole, whereas it is found to be low for the Foreign Banks. Interest spent on deposits as a whole by the Banks has decreased in the 2nd sub-period in comparison to the 1st sub-period. But for United Commercial Bank, the interest spent on deposits has increased in the 2nd sub-period in comparison to the 1st sub-period which may be due to the fact that it has revived in the matured state of the post-liberalization era and thus has gathered more deposits in the 2nd sub-period. The interest spent on borrowings by the banks on the whole has increased in the 2nd sub-period in comparison to the 1st sub-period. It is so because the growth rate in borrowings as a whole has increased in the Indian banking sector in the 2nd sub-period.

In consideration to the operating expenses parameters, our study has concentrated on the payments to and provision for employees and other operating expenses. It has been seen that PSBs account for nearly 87% of the staff expenses of the banking sector as a whole which may be due to the massive network of branches of the Public Sector Banks in general. But the growth rate in this parameter has been low for the sample PSBs, whereas the growth rate in this parameter has been high in both the sub-periods for ICICI Bank, ABN Amro Bank along with Hong Kong and Shanghai Bank. The reason for this may be due to the fact that there are more officers in the Private and Foreign Banks but more clerks in the PSBs. In terms of other operating expenses, the Public Sector Banks as a whole have done well. All the sample foreign banks along with ICICI Bank (a sample private sector bank) and Private Banks as a whole have shown a high growth rate in this component in both the sub-periods.

Ratio analysis

For analyzing the effect of fund deployment on the overall banking business through ratio analysis technique, different ratios under three broad groups, namely, liquidity, profitability and efficiency are computed and presented bank-wise using two measures, viz GM (i.e., geometric mean that represents average value of ratios over the
years in a particular period) and CV (i.e., coefficient of variation which reflects the stability/instability in values over the years in any period). The liquidity ratios that are used in the study are current ratio, liquid ratio and absolute liquid ratio. These ratios are computed for the whole period and for both of the sub-periods. It is observed that the liquidity ratios of the banks, in general, have decreased in the 2nd sub-period in comparison to the first sub-period. The reason of such findings may be due to the fact that the banking sector as a whole has tried to achieve the stringent prudential regulations in the latter stage of the post-reforms era which has been reflected through their lower values of liquidity ratios in the second sub-period. However, the Foreign Banks and Private Banks are maintaining better liquidity than the PSBs. The liquidity ratios of the sample PSBs were lower than the industry average; on the other hand, the liquidity ratios of the sample private and foreign banks were better than the sample PSBs.

The ratios related to profitability, which are used in the study are financial return, financial cost, operating expenses, miscellaneous income and risk cost. In case of profitability ratios, it has been observed that these ratios were better for the Foreign Banks as a whole. Foreign Banks as a whole have performed better than others as they have earned a high financial return coupled with low financial cost. The Private Banks have earned a high miscellaneous income but their financial return is low. The Nationalized Banks have earned high financial return and miscellaneous income but their coefficient of variation are also high too, which is undesirable; their financial costs have also been high. For SBI and its Associates financial return has been low and financial costs as well as operating expenses have been high, which is unfavourable.

The efficiency ratios that are used in our study are interest cost of deposits, interest cost of borrowings, interest yield on loans, interest yield on investment and bank balances and credit-deposit ratio. In regard to the efficiency ratios the group of Foreign Banks has performed well, as interest yield on loans and credit to deposit ratio of this group have been higher and interest cost on deposits has been lower than the related industry ratios. The efficiency ratios are mostly unfavourable for the Private Banks. For the Nationalized Banks as a whole, the interest yield on investment has been high but the CD (Credit-Deposit) ratio and interest yield on loans are found to be low. Low CD ratio gives a sign of shift of fund utilization from credit to other avenues and that might lead to
loss of interest earnings. For the SBI and its Associates as a group, the interest costs of deposits and borrowings are high and CD ratio is unfavourably low. Therefore, the effect of fund deployment on the efficiency ratios has been favourable only for the Foreign Banks as compared to other groups of banks.

In order to get an overview of the effect of fund deployment on the banking business, it is also required to assess the overall position of Non-performing Assets (NPAs) of the banks as well as to examine whether the stipulations with respect to the Capital Adequacy Ratio of the banks have been met or not. This is essential as per the prudential regulations mentioned by the Narashimham Committee II in its recommendations for the banking industry. In terms of Non-performing Assets (NPAs) it has been observed that those have decreased consistently throughout the years of the study in the banking sector. The decline in the NPAs has been sharp for the PSBs as a whole, that results also in a steep decline in the NPAs of the Scheduled Commercial Banks in India as a whole. On examining the Capital Adequacy Ratio of the banks which was strictly prescribed for the banks by the Narasimham Committee II while making its recommendations, it was found that nearly all the sample banks have achieved the required Capital Adequacy Ratio and the Tier I Capital Adequacy Ratio as recommended by the Narasimham Committee II. This represents a good scenario of banking business in India.

Data Envelopment Analysis

For measuring efficiency of the banks group-wise and individually for the sample banks for each of the years of the study and also in aggregative way for the two sub-periods separately, Data Envelopment Analysis (DEA) is used. DEA results have been studied year-wise as well as sub-period wise. From the summary results on year-wise efficiency measures of the banks it is observed that the Foreign Banks as a group is the most efficient one. Again ABN Amro Bank has performed the best among the sample banks. It is further noticed that Private Banks are the most inefficient ones followed by the Nationalized Banks. Having a glance at the summary results on the sub-period wise efficiency scores it is observed that the efficiency scores of most of the banks have improved in the second sub-period in comparison to the first sub-period. Scheduled Commercial Banks as a whole, Nationalized Banks along with State Bank of India and its
Associates have shown moderate efficiency results in the 1st as well as 2nd sub-period of the study. The efficiency of the Foreign Banks has further improved from moderate efficiency (during 1st sub-period) to hundred percent efficiency in the 2nd sub-period of the study. It must be mentioned here that United Commercial Bank has also shown improved efficiency results in the 2nd sub-period of the study (as its inefficiency in the 1st sub-period has turned into moderate efficiency in the 2nd sub-period of the study). The results support the fact that the Verma Committee recommendations had worked for the revival of this bank. Quite contrary to the earlier findings, it is observed that the efficiency scores of the Private Banks as a whole along with ICICI Bank are unimpressive. The performances of the State Bank of India along with ABN Amro Bank among the sample banks are found to be remarkably good.

In order to find out the causes of relative inefficiencies of the Banks our study concentrated on the following points: Firstly, from an in-depth study of the causes of inefficiencies it is observed that on the whole, 53% of the priority sector advances are met by the Nationalized Banks and around 25% of the same are met by the State Bank of India and its Associates (thus 78% by the PSBs), whereas only 17% of the priority sector lending has been catered to by the Private Banks and nearly 5% of the same are met by the Foreign Banks. On comparing the percentage of total advances with the percentage figures of priority sector lending, it is observed that while making advances, the PSBs (Nationalized Banks and State Bank of India and its Associates) give more thrust to fulfill their social objectives in comparison to the Foreign Banks. This dominance of priority sector lending by PSBs may be a reason of inefficiency of the banks (other than Foreign Banks) operating in India in the post-liberalization era.

Secondly, on comparing the percentage of unsecured loans to total loans over the years by the various categories of Scheduled Commercial Banks (SCBs) in India, it has been observed that the Private Banks are taking more risk, than others as the average percentage of their disbursed unsecured loans is the highest among different categories of banks. Therefore, in search of earning higher returns the Private Banks is undertaking higher risks, as a result of which they are probably loosing their efficiency in the post-reforms era.
Thirdly, the number of branches of the Public Sector Banks are the highest followed by the Private Banks. Among the branches, the rural branches are maximum for the Nationalized Banks followed by the SBI and its Associates and Private Banks. The Nationalized Banks, State Bank of India and its Associates as well as Private Banks have rural, semi-urban, urban as well as metropolitan offices, whereas, the Foreign Banks concentrate only in the metropolis. This is probably another cause of inefficiency of the Public Sector Banks and the Private Banks compared to Foreign Banks as the rural branches are mostly loss making units (as established by different committees set up from time to time on the Indian banking).

Fourthly, the existence of high operating expenses incurred by the PSBs and Private Banks is another cause of their inefficiency.

Fifthly, on analysing the employees cost to total banking business, it is seen that this ratio is high for the PSBs due to their large number of branches having adequate employees. It is adding to the cause of inefficiency of the PSBs.

7.2 Conclusions

From the major findings of the study it can be summarized that the Foreign Banks in general have performed better than the Private and Public Sector Banks as a whole. Among the sample banks, the foreign banks like ABN Amro as well as Hong Kong and Shanghai Bank have performed well. The Private Banks though have shown good results in the growth rates of sources and uses of funds, yet they have failed to show any relatively good performance in the efficiency scores, which means that their low levels of sources of funds and also their pattern of funds deployment have not been able to fetch them good efficiency scores over the years. The performance of the Public Sector Banks, on the other hand, have been good specially in respect of size of sources and uses of funds, as indicated by the averages as well as growth rates of deposits, loans and advances over the years of the study. The interest yield on investment and bank balances of the sample Public Sector Banks have been good but their interest cost of deposits is also high since they mobilize huge deposits. The PSBs are still dominating the banking industry; this is felt from the huge share of the PSBs in the deposits of the banking sector at large and also their shares in the income and expenditure components. But their overall
efficiency scores are not found to be good. On analyzing the causes of inefficiencies and low profitability of the Public Sector Banks, it is felt that their performance with the Foreign Banks is in no way comparable. This is so because over the years, the PSBs have fulfilled the social objectives of banking and have reached out to the Indian masses. Their presence in the rural areas has been highly appreciable. It is clear that both social objective and the profit motive can not go hand in hand. The only need is to make a balance between these two with the help of time to time checking of performance and making recommendations, if required, as happens in the case of United Commercial Bank, a sample PSB, which has been revived over the years, after the implementation of Verma Committee recommendations.

In fine, it may be concluded that in India though the performance of the Foreign Banks has been good, the performance of the Public Sector Banks in no way can be undermined and the performance of the latter can further be improved through deploying funds judiciously.