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ANALYZING THE IMPACT OF LIBERALIZATION ON BANKING STRUCTURE

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ABSTRACT

Banks play very crucial role in the development and growth of an economy. Banks helps to accumulate the saving of public and invest their saving to create new demand deposits, loans and in purchasing investment securities. Banks plays role to provide mobility of capital. Now a day's banking sector is one of the biggest service sectors in India. The five most important banking services are related with checking and saving accounts, loans, and mortgage services, wealth management, providing credit and Debit cards, overdraft services. The banking system is assumed to be most important due to the intense competition. The present paper aims to analyze the impact of liberalization on banking structure. As it is known very well that the growth and profitability are interrelated. The productivity affects in positive way to the growth. The trends equations have been estimated for the liberalization period of twenty five years. The methodology is framed with the Chow test to know the structural changes in the banking sector.

***KEYWORDS**: Commercial Banks, Growth, Productivity, Liberalization.*

Introduction

The development of a nation depends on the efficient performance of commercial banks. The performance of an economy is very much connected with the performance of the financial sector of that economy. Financial sector comprises a very important ingredient in any economy. The financial sector of India is gaining strength over the years and its contribution to growth is overwhelming. Banks are considered the main component of the Indian Financial Sector. A good performance of the banking sector itself indicates the overall good performance of the sector, which ultimately leads to improved performance of the economy. In India the banking sector was totally traditional before 1991. India has witnessed an exceptional revolution in the banking sector in the last two decades. Banking today has been redefined and re-engineered with liberalization of interest rates and credit allocation policy. Traditionally, banks were involved in accepting deposits from the public at a lower rate and issuing loans at a higher rate and thereby making profit on interest margin. Banking sector reforms aimed at, introduction of new indirect monetary policy, strengthening prudential regulation, opening the financial sector to foreign financial institutions and promotion of the capital market. Many studies have been conducted on factors influencing performance of banks. Researchers have tried to analyze bank performance based on external and internal variables in various country contexts (Gizyeki, 2001). External variables include rate of economic growth, industry-wide developments, inflation, money supply, economies of scale and scope, dynamics of bank competition, global presence of financial conglomerates, disintermediation in banking activities and other macroeconomic factors; while bank specific internal variables mean an increase in the business over a period of time in the areas of Reserve and Surplus growth, Advance growth, Investment growth, Interest Earned growth, Operating Expenses growth, Equity Dividend growth, Net profit growth and EPS growth of the current year in comparison to previous year (Pathak, 2011). The performance of the Indian economy is one of the strongest drivers for the banking industry's growth. Panda and Lall (1991) had found certain factors which influence the profitability improvement of banks to the great extent. They argued that branch expansion is one of those factors which can impact on profitability. Rammohan and Ray (2004) revealed that with regard to the revenue maximizing efficiency, public sector banks are significantly better than private banks but they found no significant difference between public and foreign banks on this parameter. The study by Kumar (2006) depicts that the bank nationalization in India marked a paradigm shift in the focus of banking as it was intended to shift the focus from class banking to

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mass banking and efforts are also being made internationally to study causes of financial inclusion and designing strategies to ensure financial inclusion of the poor and disadvantaged. He discussed that the banks should redesign their business strategies to incorporate specific plans to promote financial inclusion of low income groups, treating it as both a business opportunity as well as a corporate social responsibility and financial inclusion can emerge as a commercially profitable business. Venkatesan (2007) viewed in his study that the net interest margin has come down over the last one decade with increased competition in the banking industry. He viewed that banks will look for fee based income to fill the gap in interest income. Bennaceur and Goaied (2008) observed in the study those factors affecting profitability for the period 1980-2000 and also suggested that capital and overhead expenses are positively related to profitability level. Kosmidou (2008) suggests in his findings that the more profitable banks have higher levels of capital and lower cost to income ratio. Manoj (2010) discussed that enhanced profitability and efficiency has become vital for survival and growth of the banks in the era of globalization and significantly affected by asset quality, capital adequacy and liquidity of the banks. Ghosh (2010) finds the interplay between credit growth bank soundness and financial fragility in Indian banks. The soundness of banks is measured by their distance to default. Loan growth is often directly associated with soundness but an extension could weaken bank soundness. Anjum and Deepika (2012) made a comparative study of the profitability of the Indian Banking Sector and the impact of technological investment on the profitability of the Public and Private Sector Banks. They discussed that the Indian Banking Industry in technological advancement is still in gestation phase and RBI has to take various steps so that the Public Sector Banks (Nationalized and SBI & its Associates) become able to manage their profitability by striking the balance between technological Investments (Expenditures) and Incomes. Ayyappan and Sakthivadivel (2012) revealed that the compound growth rate of the private sector banks is comparatively higher than that of the public sector banks. The banks were grouped into two categories: i.e., Public Sector Banks Group (22 banks) and Private Banks Group (15 banks). Their study predicted that at the current rate of growth the private sector banks can pose a challenge in the market place and may even overtake the public sector banks in the longer period of time. The study does not provide any idea regarding the growth of any individual or frontline public and private sector commercial banks but the growth picture at macro level. The present study attempts to measure the growth of the banking sector. Thus, the objectives of the study are;

- To know the structural changes between the rural and urban sector banks.
- To analyze the performance of rural, semi urban, urban and metropolitan commercial banks.

Data and Methodology

The present paper is concerned with the Indian banking system. For this study all the commercial banks have been selected. The study is based on time-series secondary data from the time period 1990-91 to 2015-16. The ordinary least squares method has been used to analyse the trend equations. To compare the performance of rural, semi urban, urban and metropolitan banks Compound Growth Rate has been computed. To measure Branch Productivity and Labour Productivity ratio analysis has been used. The Chow test is framed to know the structural changes between rural and urban sector banks. For all purposes the parameters such as number of branches, number of accounts, number of employees, Deposits, Branch productivity and labour productivity are considered. The data have been collected from the Handbook of Statistics, Reserve Bank of India.

Estimates of Trends

The linear trend equations have been estimated for the variables total number of branches, total numbers of accounts and total deposits. The following linear model is used.

$Y= a+ bt$

Where, Y is dependent variable, a is the autonomous quality, b is slope of variable and it measures the change in Y as the result of one unit change in time. i.e. $dy/dt=b$. The t is considered time in the study.

Results and Discussion

The trend equations have been estimated for the variable number of branches, number of accounts and deposits in Table-1. In metropolitan areas performance of banks is better than the rural, urban and semi-urban area banks. The coefficient of variation is 90% in the number of banks in metropolitan area banks, while it is very less in rural area banks. The increasing trend can be seen in all the banks. The calculated value of F is 20.675in chow test is more than the tabulated value in case of the number of branches of scheduled commercial banks. Similarly, the calculated value of F in case of number of account and deposit is 10.617 and 19.176 respectively that is more than tabulated value. Thus, the null hypothesis is rejected and the structural difference in rural and urban area banks exists.

- **Commercial Bank Branch Expansion:** The total number of branches of scheduled commercial banks went up from 60220 in 1991 to 126299 in 2015. Table -2 shows that in metropolitan areas the growth rate of branches is 5.6% which is highest among the other area branches. The less growth rate of branches is noticed in rural area banks by 1.3%. The total growth rate of all scheduled commercial banks is 3.1%.
- **Accounts Position:** The accounts position of all scheduled commercial banks is shown in Table-3. In the rural sector the highest compound growth rate of the number of accounts was 6.49%. In the urban sector the compound growth rate was 5.08% which was the least among the four sectors. The total increase in growth rate of accounts in all scheduled commercial banks is 5.99%. The number of accounts increased in rural areas due to Jan Dan Yojana started by Prime Minister Narender Modi.
- **Deposits:** The important parameter of performance in commercial banks is deposits. The public deposits money in banks and after deposition the banks lend it to the public. There are two types of deposits in banks: time deposit and demand deposit. We know that deposit indicates the growth and development of a bank. It is clear from Table-4 that the deposit increased less in rural sector banks while the number of accounts increased more in metropolitan sector.
- **Branch Productivity:** It depicts the capacity of a branch to produce. The ratio has been computed by dividing total deposits by the number of branches of the commercial bank. The total branch productivity was 0.032 in 1991 and increased to 0.706 in 2015.
- **Labour Productivity:** The labour productivity brings in light employee’s capacity to produce. The total deposit is divided by the number of bank employees’ measures of the labour productivity of bank employees. It increased with the time from 1.02% in 2001 to 6.9% in 2015.

Conclusion

The paper concludes that although various reforms after 1991 have been made in commercial banks. In the globalization world, banks are facing many internal and external competition and challenges. The banks are mainly concentrating on providing customer service more effectively and efficiently so that their bank may gain the trust of customers. The success of any financial institution depends upon the service providing and satisfaction of the customer. The global financial crisis of 2007-08 has not influenced the Indian banking sector. But, the growth of banks during the period 2009-2012 is under challenges due to stressed financial conditions. Greater customer oriented is the only way to gain loyalty and stay ahead. So the banks need to bring about customer oriented and the policy should be customer focused. Technology plays a crucial role in the banks. The rural sector banks should provide the internet banking facilities and mobile banking to the customers. The use of technology should be motivated by the banks to the customers. The public perception about the rural banks is very poor. The rural sector banks should improve their perception by all means to remain competitive in the market. Political interference is the most serious damage to the banking system. It should be checked.

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Table 1: Estimates of Linear Trend: Y=a+bt

Sector / Parameters	Rural			Semi-Urban			Urban			Metropolitan		
	NOB	A/c	Deposit	NOB	A/c	Deposit	NOB	A/c	Deposit	NOB	A/c	Deposit
a	31612.7	37368.7	-1367.5***	7549.23*	43225**	-21007***	5308.7*	46521.5***	-3624***	2961.8*	27837.7*	-10261.9***
b	197.98**	10982.2*	306.5*	770.12*	8729.7*	4480.1*	568.6*	5820.2*	692.2*	611.5*	7299.9*	1821.9*
R^2	0.114	0.642*	0.818*	0.777*	0.636*	0.814*	0.863*	0.714*	0.807*	.906*	0.803*	0.821*

Note:*-Significance at 1% level
**-Significance at 5% level
***-Significance at 10% level

Table 2: Number of Branches of Scheduled Commercial Bank

Year / Sector	1991	2001	2011	2015	Compound Growth Rate
Rural	35206	32562	33460	48247	1.31
Semi-Urban	11344	14597	23318	35959	4.91
Urban	8046	10293	17681	23115	4.48
Metropolitan	5624	8467	16447	20824	5.59
Total	60220	65919	90906	126299	3.12

Table 3: Number of Accounts of Scheduled Commercial Banks (Number of Accounts in Thousands)

Year / Sector	1991	2001	2011	2015	Compound Growth Rate
Rural	108876	131723	250254	493970	6.49
Semi-Urban	98084	116400	212043	404661	6.07
Urban	80889	92769	168037	266228	5.08
Metropolitan	67342	87137	179796	275033	6.02
Total	355191	428029	810130	1439892	5.99

Table 4: Deposits of Scheduled Commercial Banks (Amount in Rs. Billion)

Year / Sector	1991	2001	2011	2015
Rural	310.10	1394.31	4932.66	9156.76
Semi-Urban	414.39	1861.88	7168.31	13172.51
Urban	419.40	2178.33	11105.13	19649.01
Metropolitan	789.79	4059.81	30689.14	47242.83
Total	1933.68	9494.33	53895.24	89221.11

Table 5: Number of Employees of Scheduled Commercial Banks

Year / All Sector	2001	2011	2015
Total	926518	1050885	1291542

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