# IMPACT OF OWNERSHIP PATTERN ON THE PROFITABILITY OF THE NATIONALIZED PUBLIC SECTOR BANKS IN INDIA

**Dr. P. Hanumantha Rao**

## Abstract

If an attempt is made to study the economic scenario of last 8 years or so, one can see that it has been very volatile for not only the Indian economy but also for the entire world economy. Most of the economies are in the process of recovery. Many investors have lost their money as the stock prices reached minimal levels in most of financial markets over the world during this period. The performance of banking sector always had a very significant impact on the performance of the national economies. In India, public sector bank dominates the entire banking sector as they account for over 80% of banking business in India. The performance of banks depends on so many factors. One of the important factors can be pattern of ownerships. If we look at the pattern of ownerships of public sector banks, we can find they are owned by entities like Government, Financial institutions, corporate entities and individual shareholders. The present article attempts to study how the pattern of ownerships has an impact on the performance of the banks in terms of two key variable, namely, RoA and net profit for the last two financial years, 2013-14 and 2014-15.

**Keywords :** *Ownership and Control, Nationalized Bank, Financial Institute*

## Introduction

One of the significant features of Indian economy in the recent past has been the emergence of India among the few large economies with brighter growth perspectives. This is despite the fact the many big and emerging economies of the world are facing the problem of instability and uncertainty. All major service-sector activities including financing, insurance, real estate etc have contributed to the process of growth in the financial year 2014-15.India is expected to grow by a robust 7.8 per cent in 2016 and 7.9 per cent in the next two years as per the estimates of World Bank. India is predicted to be the fastest growing economy in the world in the next three years and would outpace China. With the recent fall in oil prices, India emerges as the bright spot of the global economy as Chinese growth is expected to slow further. Growth in India remained robust, led by strong investor sentiment and the positive effect on real incomes of the recent fall in oil prices. As per the estimates of IMF also, India will be the world's fastest growing economy, for the second consecutive year in 2016 at 7.5 per cent, In its World Economic Outlook Update released, IMF has retained India's growth projection for current year at 7.5 per cent, which is higher than China's 6.8 per cent. As per IMF data. China was the fastest growing economy in 2014, at 7.4 per cent as against India's 7.3 per cent. However, IMF's growth projection for India is lower than the estimates of the Indian Finance Ministry and the Reserve Bank of India. The Finance Ministry forecasts GDP growth to be 8-8.5 per cent in 2015-16, while the Reserve Bank of India expects it at 7.6 per cent.

One of the strongest pillars of Indian economy is robust banking system we have. The Indian banking system consists of 27 public sector banks, 20 private sector banks, 43 foreign banks, 56 regional rural banks, 1,589 urban cooperative banks and 93,550 rural cooperative banks, in addition to cooperative credit institutions. The Indian banking sector's assets are estimated to have reached US$ 1.8 trillion in the financial year 2013-14 from US$ 1.3 trillion in financial year 2009-10, of which almost 70% account for public sector banks. Total lending and deposits increased at a compound annual growth rate (CAGR) of 20.7 per cent and 19.7 per cent, respectively, during 2007-14 and are expected to faster, backed by demand for housing and personal finance. Total asset size of banking sector assets is projected to increase to US$ 28.5 trillion by the year 2025. Deposits have grown at a CAGR of 13.6 per cent during 2005-15 to an estimated US$ 1.48 trillion in 2014-15The growth in deposits is mainly driven by strong growth in savings amid rising disposable income levels of the people. However, for the financial 2014-15, the performance of the Indian banking sector has not been up the expectations as it experienced a slowdown in balance sheet growth in 2014-15. While the public sector banks had registered a decline in credit growth, the private sector banks and foreign banks have recorded a higher credit growth. Retail loan portfolio of the banks registered a growth at around 20 per cent during 2014-15. Credit growth to priority sector also reduced during 2014-15. Despite the increase in profit growth in the previous year, the return on assets (RoA), which is a common indicator of financial viability, has not shown any significant improvement in 2014-15.In India, the PSBs accounts for 72 per cent of total banking sector assets, but they accounted for only 42 per cent in total profits during 2014-15, whereas private sector banks have surpassed the PSBs in the share of total banking sector profits. The decline in the asset quality of banks in general, and public sector banks in particular, continued during the year.

## Literature Review

A study of literatures on the subject throws ample light on the factors impacting the performance of public sector banks in India. There are number of studies which concluded that privately-owned enterprises usually perform better than state-owned enterprises; however, there are many critics who oppose those views. Many studies which examined the performance effects of bank ownership type—whether an institution is state-owned, private domestic or foreign—found very significant differences among these types. A study by Vining and Boardman (1992) who reviewed 54 studies that compared the performance of firms' between private and state ownership and found that 36 studies observed that private firms perform better; six studies revealed that state-owned banks perform better; and 16 studies did not support either form of ownership. On the contrary, several studies, such as Caves and Christensen (1980), Borcherding et al. (1982), Millward (1988), and Ramaswamy (2001), concluded that ownership does not matter much in the presence of sufficient competition between state and private enterprises. Further, a survey by Millward and Parker (1983) observed that there is no systematic evidence to support the perception that public enterprises are less effective than private enterprises. Further, Berle and Means (1932) observed that the separation of ownership and control may lead to conflict of interests between owners and managers. Jensen and Meckling (1976) concluded that as managers' equity decreases and ownership becomes more dispersed as a result, the agency cost of deviation from value maximization will increase. Fama (1980) argued that if capital market is efficient and the dispersed ownership goes along with the public trading of the firm's securities, that is likely to discipline the firm's management. Regarding the nature of owners, Shleifer and Vishney (1997) were of the opinion that state-owned enterprises that are technically controlled by the public, and hence are run by bureaucrats who may think of having very controlled rights rather than significant cash flow rights. A study by Bhattacharya et al. (1997) on Indian banks observed that Government owned banks performed better than foreign banks and private banks. In contrast, Sarkar et al. (1998) in their study on Indian banks observed that FBs are more profitable and efficient than traded private banks that are more profitable than non-traded private banks. Among non traded banks, the study could not find any significant differences in performance. They also observed out that political bureaucrats aim to maximize personal goals which often results in conflict with public interests, as it is dictated by political interests. Mishra et al (2011) found that Banks and Financial Institutions in India have experienced a phenomenal change in the levels of competition after the advent of liberalization in the 90s and the entry of private players. However, Sahoo et al (2011) in their study of the performance of the Indian banking sector during the post transition period (1997-2005) suggested that the nationalized banks are yet to exercise their cost minimizing principles compared to the other banks. Similarly, Cheema et al (2002) found that commercial banks operating in India are below the average level of efficiency. Again, Sathye (2001) has observed that the mean efficiency score of Indian banks compares well with the world mean efficiency score. He also observed that the efficiency of private sector banks as a group is paradoxically lower than that of public sector banks in India Chambers (2007) made an assessment whether investment banks can maintain their good fundamentals 2007 based on the views of several investment bank executives. Banks continued to ride high in 2006 on good fundamentals and the added boost of strong hedge fund and private equity activity, proprietary trading and continuing globalization.

Ramudu et al (2006) analyzed the profitability of the three major banks in India: SBI, ICICI, and HDFC for the period 2000-2005 and brought out the comparative efficiency of SBI, ICICI, and HDFC. Hammond (2012) reports that Morgan Stanley recommends raising exposure to Indian bank credit despite deteriorating fundamentalism the sector. According to Morgan Stanley, attractive technical's, low capital deficits and fair sector valuations make Indian bank credit attractive. Morgan Stanley credit analyst Desmond Lee admits that Indian banks have been the biggest underperformers in the region for the past 18 months leading to June 2012, but he claims that opportunities exist within the sector.

## Need for the Study

Various studies have attempted to capture the relationship between ownership pattern and firm's performance over the time. But this study aims to capture impact of ownerships pattern on the profitability of nationalized in Indian context by taking all 19 nationalized banks operating in India over the years 2013-14 and 2014-15.

## Objectives of the Study

Ownership pattern is to said to have significant influence on the performance of a firm. The main aim of the paper is

- To examine the impact of pattern of ownership on the ROA and net profits of the public sector banks
- To explore the possible reasons for the observed impact

## Research Methodology

The study is based on the data of 19 public sector banks operating in India for the financial year 2013-14 and 2014-15. The ownership pattern includes ownership by Government and RBI, Financial Institutions, Corporate entities and Individuals. The data is taken from RBI website. Dependent variables are the extent of ownership by Government and RBI, Financial Institutions, Corporate entities and Individuals. Independent variables are Return on Assets and Net profits. The impact of dependent variables is considered by taking one independent variable at a time.

**Hypotheses**

**H01:** There is no influence of extent of ownership by Government of India and RBI on ROA and Net profits of public sector banks in India.

**H02:** There is no influence of extent of ownership by Financial Institutions on ROA and Net profits of public sector banks in India.

**H03:** There is no influence of extent of ownership by Corporate Entities on ROA and Net profits of public sector banks in India.

**H04:** There is no influence of extent of ownership by Individuals on ROA and Net profits of public sector banks in India.

The data is collected on the extent of ownership by ownership by Government and RBI, Financial Institutions, Corporate entities and Individuals, Return on Assets and Net profits of 19 public sector banks operating in India for 2013-14 and 2014-15. The banks include

UCO Bank, Union Bank of India, United Bank of India, Vijaya Bank.

The statistical tools used for analysis purpose includes descriptive statistics like mean, standard deviation and regression model.

## Results of Analysis

Public Sector Banks (PSBs) refers to the banks where a majority of stake (i.e. more than 50%) is held by the government of India. The shares of these banks are also listed on stock exchanges. There are a total of 27 Public Sector Banks in India. It includes 19 Nationalized banks, 6 State bank group (State bank of India and 5 associates, IDBI bank nationalized in 2011 and Bharatiya Mahila Bank nationalized in 2014. The nationalization was aimed to achieve numbers objectives like:

- To take away the ownership and control of banks by a few business families,
- To prevent the concentration of wealth and economic power in the hands of few,
- To mobilize savings from all quarters,
- To cater to the needs of the priority and weaker sectors

The following table gives us an idea about the pattern of ownership of these banks :

**Table 1: Ownership pattern of nationalized bank for the year as on 31-03-2014**

| Sr. No. | Name of the Bank | Total Government and RBI-Resident | Financial Institutions | Corporates | Individuals | ROA | Net Profit (Cr) |
|---|---|---|---|---|---|---|---|
| 1 | Allahabad Bank | 58.9 | 25.93 | 2.06 | 13.11 | 0.57 | 1172.02 |
| 2 | Andhra Bank | 60.14 | 22.43 | 2.35 | 15.08 | 0.29 | 435.58 |
| 3 | Bank of Baroda | 56.26 | 34.2 | 3.85 | 5.69 | 0.75 | 4541.08 |
| 4 | Bank of India | 66.7 | 25.64 | 1.66 | 6 | 0.51 | 2729.27 |
| 5 | Bank of Maharashtra | 85.21 | 7.54 | 0.82 | 6.43 | 0.3 | 385.97 |
| 6 | Canara Bank | 69 | 23.13 | 2.12 | 5.75 | 0.54 | 2438.19 |
| 7 | Central Bank of India | 88.63 | 6.83 | 0.71 | 3.83 | -0.47 | -1262.84 |
| 8 | Corporation Bank | 63.33 | 28.93 | 1.36 | 6.38 | 0.29 | 561.7186 |
| 9 | Dena Bank | 58.01 | 16.94 | 2.86 | 22.19 | 0.51 | 551.66 |
| 10 | Indian Bank | 81.51 | 12.61 | 2.23 | 3.65 | 0.67 | 1158.945 |
| 11 | Indian Overseas Bank | 73.8 | 17.33 | 0.72 | 8.15 | 0.23 | 601.74 |
| 12 | Oriental Bank of Commerce | 59.13 | 33.93 | 1.91 | 5.03 | 0.56 | 1139.41 |
| 13 | Punjab & Sind Bank | 81.42 | 7.54 | 1.66 | 9.38 | 0.35 | 300.63 |
| 14 | Punjab National Bank | 58.88 | 35.85 | 1.24 | 4.03 | 0.64 | 3342.57 |
| 15 | Syndicate Bank | 67.39 | 16.89 | 2.03 | 13.69 | 0.7 | 1711.46 |
| 16 | UCO Bank | 77.2 | 13.17 | 1.66 | 7.97 | 0.7 | 1510.54 |
| 17 | Union Bank of India | 60.13 | 25.09 | 5.26 | 9.52 | 0.52 | 1696.25 |
| 18 | United Bank of India | 87.99 | 5.55 | 1.62 | 4.84 | -0.99 | -1213.45 |
| 19 | Vijaya Bank | 74.06 | 9.94 | 2.25 | 13.75 | 0.35 | 415.91 |
| | Mean | 69.9 | 19.4 | 2.0 | 8.7 | 0.4 | 1169.3 |
| | Standard Deviation | 11.06 | 9.86 | 1.09 | 4.88 | 0.43 | 1413.51 |

Table 1 gives us an idea about the pattern of ownership of these banks. A look at the ownership pattern of nationalized banks in India for the year ended 2014 indicate that Government holds around 69.9% of stake in nationalized bank, followed by financial institutions at 19.4%, individuals at 8.7% and corporate entities at 2% respectively. The average RoA and net profits of the nationalized banks in the financial year 2015 stand at 0.4 and 1169.3 crores.

**Table 2 : Ownership pattern of nationalized bank for the year as on 31-03-2015**

| Sr. No. | Name of the Bank | Total Government and RBI- Resident | Financial Institutions | Corporate | Individuals | ROA | Net Profit (Cr) |
|---|---|---|---|---|---|---|---|
| 1 | Allahabad Bank | 60.8 | 26.1 | 1.4 | 11.7 | 0.29 | 621 |
| 2 | Andhra Bank | 61.0 | 23.5 | 1.9 | 13.6 | 0.38 | 638 |
| 3 | Bank of Baroda | 57.5 | 34.3 | 2.7 | 5.5 | 0.49 | 3,398 |
| 4 | Bank of India | 64.4 | 26.7 | 2.1 | 6.8 | 0.27 | 1,709 |
| 5 | Bank of Maharashtra | 100.0 | 0.0 | 0.0 | 0.0 | 0.33 | 451 |
| 6 | Canara Bank | 69.9 | 23.8 | 0.9 | 5.4 | 0.55 | 2,703 |
| 7 | Central Bank of India | 81.5 | 14.2 | 1.7 | 2.6 | 0.21 | 606 |
| 8 | Corporation Bank | 63.3 | 29.2 | 1.5 | 6.0 | 0.28 | 584 |
| 9 | Dena Bank | 59.8 | 15.6 | 2.3 | 22.3 | 0.22 | 265 |
| 10 | Indian Bank | 76.5 | 14.2 | 1.3 | 8.1 | 0.54 | 1,005 |
| 11 | Indian Overseas Bank | 73.8 | 16.9 | 0.9 | 8.4 | -0.16 | -454 |
| 12 | Oriental Bank of Commerce | 59.1 | 33.4 | 2.5 | 5.1 | 0.23 | 778 |
| 13 | Punjab & Sind Bank | 79.6 | 12.5 | 1.3 | 6.6 | 0.13 | 121 |
| 14 | Punjab National Bank | 59.9 | 34.6 | 0.9 | 4.6 | 0.53 | 3,062 |
| 15 | Syndicate Bank | 69.2 | 18.7 | 1.9 | 10.2 | 0.58 | 1,523 |
| 16 | UCO Bank | 72.8 | 18.6 | 1.3 | 7.3 | 0.48 | 1,138 |
| 17 | Union Bank of India | 60.5 | 26.8 | 3.7 | 9.0 | 0.49 | 1,782 |
| 18 | United Bank of India | 82.0 | 13.5 | 1.2 | 3.3 | 0.21 | 256 |
| 19 | Vijaya Bank | 74.1 | 11.1 | 1.6 | 13.2 | 0.33 | 439 |
| | Mean | 69.8 | 20.7 | 1.6 | 7.9 | 0.3 | 1085.5 |
| | Standard Deviation | 10.96 | 9.14 | 0.80 | 4.94 | 0.18 | 1038.60 |

**Source: www.rbi.org.in**

From the ownership pattern of nationalized banks in India for the year 2015, it is observed that on an average Government holds around 70% of stake in nationalized bank, followed by financial institutions at 20.7%, individuals at 7.9% and corporate entities at 1.9% respectively.

The average RoA and net profits of the nationalized banks in the financial year 2015 stand at 0.3 and 1085.5 crores. This indicates a fall in both RoA and net profits which stood at 0.43% and 1413.5 crores1in the financial year 2014 respectively. Now, we have tried to study the impact of ownership pattern on profitability by taking both RoA and net profit after tax as dependent variable and the extent of ownership as independent variable.

**Table 3 : Regression Statistics for RoA for 2014**

| | | | *Coefficients* |
|---|---|---|---|
| Multiple R | 0.61 | Intercept | 3.70 |
| R Square | 0.38 | Government and RBI stake | -0.04 |
| Adjusted R Square | 0.18 | Financial Institutions stake | -0.02 |
| Standard Error | 0.37 | Corporate entities stake | 0.00 |
| Observations | 19.00 | Individualstake | -0.02 |

The R square value is 0.38 which indicates that RoA is affected by extent of ownership by different stakeholder to a considerable extent. From the table 3 it can be interpreted that the coefficient of all the dependent variable except corporate entities are negative which indicates that there is a adverse relationship between stake of these entities and RoA. It is also observed that the extent of stake by corporate has no impact on RoA.

**Table 4 : Regression Statistics for RoA for 2015**

| | | | *Coefficients* |
|---|---|---|---|
| Multiple R | 0.28 | Intercept | -0.08 |
| R Square | 0.08 | Government and RBI stake | 0.00 |
| Adjusted R Square | -0.17 | Financial Institutions stake | 0.01 |
| Standard Error | 0.19 | Corporate entities stake | 0.03 |
| Observations | 19.00 | Individual stake | 0.00 |

The results of analysis for the financial year 2015, shows a very less value of R square compared to the previous financial year. This is very obvious as there are many other factors (other than extent of ownership by different entities) which affect RoA. Here it is found that extent of ownerships and extent of individual ownership has no impact on the RoA of the public sector banks. However, both extent of ownerships by financial institutions and corporate entities has found to have a direct impact on the RoA.

**Table 5 : Regression Statistics for net profit for 2014**

| | | | *Coefficients* |
|---|---|---|---|
| Multiple R | 0.82 | Intercept | 0.00 |
| R Square | 0.67 | Government and RBI stake | -8.00 |
| Adjusted R Square | 0.54 | Financial Institutions stake | 101.73 |
| Standard Error | 1162.26 | Corporate entities stake | -196.86 |
| Observations | 19.00 | Individual stake | -7.62 |

Table 5 indicates a R Square value of 0.67 which indicates that net profit is affected by extent of ownership by different stakeholder to a significant extent. From table 5, the coefficient of all the dependent variable except by financial institution are negative which indicates that there is a adverse relationship between stake of these entities and RoA. It is only the extent of ownership by financial institutions which has a direct impact on the net profits for the year 2014.

**Table 6 : Regression Statistics for net profit for 2015**

| | | | *Coefficients* |
|---|---|---|---|
| Multiple R | 0.86 | Intercept | 0.00 |
| R Square | 0.74 | Government and RBI stake | - 0.04 |
| Adjusted R Square | 0.62 | Financial Institutions stake | 67.97 |
| Standard Error | 850.07 | Corporate entities stake | 61.06 |
| Observations | 19.00 | Individual stake | -53.35 |

The regression statistics for the net profit for the year 2015, it is found that R square is 0.74. The extent of ownership by financial institutions and corporate entities have found to have a direct impact on the net profit for the year 2015 whereas the extent of ownership by Govt and RBI and individuals have found to have negative impact on the net profits of the banks.

## Conclusion

The following observations are made from the above analysis,

- In the year 2014, we saw corporate ownerships had no impact on the RoA of public sector banks.
- In the year 2015, we can see that RoA is positively impacted by the extent of ownership by FIs and individuals.
- As far as net profit is concerned, except ownerships by financial institutions, all other had negative impact in the year 2014.
- In the year 2015, ownership by FIs and corporate entities had positive impact on the net profits whereas ownerships by Govt. and individuals had negative impact.

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## About the Author

**Dr. P. Hanumantha Rao** is an Assistant professor in Finance, NICMAR, Hyderabad. He can be reached at hanu_finance@yahoo.com