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DECIDING FACTORS ON FINANCIAL PERFORMANCE OF BANKING SECTOR

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Abstract
Banking is an important sector and acts as a backbone of economic progress. The banks render vital services to the masses belonging to the various sectors of the economy like agriculture, industry whether small scale or large scale. The banking system is one of the few institutions that impinge on the economy and affect its performance for better or worse. They act as a development agency and are the source of hope and aspirations of the masses. Indian banking is the lifeline of the nation and its people. The present study aimed to know the deciding factors on financial performance of banking sector in Erode district. Banking has helped in developing the vital sectors of the economy and usher in a new dawn of progress on the Indian horizon. The sector has translated the hopes and aspirations of millions of people into reality. But to do so, it has had to control miles and miles of difficult terrain, suffer the indignities of foreign rule and the pangs of partition. Today, Indian banks can confidently compete with modern banks of the world. Financial analysis is a powerful tool which helps in determining the problems in the operation and financial position of the banking industries.

Introduction

Before the 20th century, usury, or lending money at a high rate of interest, was widely prevalent in rural India. Entry of Joint stock banks and development of Cooperative movement have taken over a good deal of business from the hands of the Indian money lender, who although still exist, have lost his menacing teeth. The massive and speedy expansion and diversification of banking has not been without its strains. The banking industry is entering a new phase in which it will be facing increasing competition from non-banks not only in the domestic market but in the international markets also. The operational structure of banking in India is expected to undergo a profound change during the next decade. With the emergence of new private banks, the private bank sector has become enriched and diversified with focus spread to the wholesale as well as retail banking. The existing banks have wide branch network and geographic spread, whereas the new private banks have the clout of massive capital, lean personnel component, the expertise in developing sophisticated financial products and use of state-of-the-art technology. Gradual deregulation that is being ushered in while stimulating the competition would also facilitate forging mutually beneficial relationships, which would ultimately enhance the quality and content of banking. In the final phase, the banking system in India will give a good account of itself only with the combined efforts of cooperative banks, regional rural banks and development banking institutions which are expected to provide an adequate number of effective retail outlets to meet the emerging socio-economic challenges during the next two decades. The electronic age has also affected the banking system, leading to very fast electronic fund transfer. However, the development of electronic banking has also led to new areas of risk such as data security and integrity requiring new techniques of risk management. Financial analysis is the use of financial statements to analyze a company's financial position and performance, and to assess future financial performance. Financial analysis consists of three broad areas - profitability analysis, risk analysis, and analysis of sources and uses of funds. Profitability analysis is the evaluation of a company's return on investment. It focuses on a company's sources and levels of profits and involves identifying and measuring the impact of various profitability drivers. It also includes evaluation of the two major sources of profitability - margins (the portion of sales not offset by costs) and turnover (capital

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utilization). Profitability analysis also focuses on reasons for changes in profitability and the sustainability of earnings. Risk analysis is the evaluation of a company's ability to meet its commitments. Risk analysis involves assessing the solvency and liquidity of a company along with its earnings variability. Because risk is of foremost concern to creditors, risk analysis is often discussed in the context of credit analysis. Still, risk analysis is very important to equity analysis, both to evaluate the reliability and sustainability of company performance and to estimate cost of capital of a company. Analysis of cash flows is the evaluation of how a company is obtaining and deploying its funds. This analysis provides insights into a company's future financing implications. A company requires financing to carry out its business plan. Financing activities refer to methods that companies use to raise the money to pay for these needs. Because of their magnitude and their potential for determining the success or failure of a venture, companies take care in acquiring and managing financial resources. There are two main sources of external financing—equity investors (also called owners or shareholders) and creditors (lenders). Decisions concerning the composition of financing activities depend on conditions existing in financial markets. Financial markets are potential sources of financing. In looking to financial markets, a company considers several issues, including the amount of financing necessary, sources of financing (owners or creditors), timing of repayment, and structure of financing agreements. Decisions on these issues determine a company's organizational structure, affect its growth, influence its exposure to risk, and determine the power of outsiders in business decisions. Financial Performance is the snapshot of a concern's position and ability to survive the ever-changing environment. It is the blue print of the financial affairs of the concern and reveals how a business is prospered under the leadership of its management human resources. In fact, financial performance is the medium of evaluation of management performance. According to accounting point of view financial statement are prepare by a business enterprise at the end of every financial year. Financial statements are end products of financial accounting. They are capsulate periodical reports of financial and operating data accumulated by a firm in its books of accounts and the General Ledger. The overall objective of a business is earning satisfactory returns on the funds invested in it. Consistent with maintaining a sound financial position, an evaluation of such performance is doing in order to measure the efficiency of operations or the profitability of the organization and to assess the financial strength as compared with a similarly situated concern. The present study aimed to know the deciding factors on financial performance of banking sector in Erode district.

Materials and Methods

Azhagaiah and Gejalakshmi (2012) aimed to analyze the performance of selected 36 banks in India. With 5 years data, the statistical tools like ratio analysis, correlation and regression were used for the analysis. They found that the private and public sector banks are better in translating the assets into profits. The mean of interest income indicate that the financial health of both the private and public sector banks was good. The regression analysis shows that the public sector bank is strongly and positively influenced by the operational efficiency, asset management and the interest income. The private sector banks were positively influenced by the asset utilization, operational efficiency on interest income. Panigrahi and Sharma (2013) investigated the existence of relationship between the working capital management and the profitability, inventory conversion period, average receivable period, average payment period and the cash conversion cycle which articulates the efficiency of working capital. The study found that there is a negative relationship between accounts receivable period and firm's profitability, a negative relationship between Inventory conversion period and profitability, negative significant relationship between accounts payable period and profitability but a positive relationship between firm's cash conversion cycle and its profitability. This shows that firms are selling their inventory and collecting the receivables before they have to pay for the payables.

The research validity mainly depends on the systematic method of collecting the data, and analyzing the same in a sequential order. In the present study, an extensive use of both primary and secondary data was made. For collecting primary data, field survey technique was employed in the study. First-hand information was collected from 225 customers of various banks of Erode district. The respondents were selected on a stratified random basis from the district. In order to fulfill the objectives set, a sample study was undertaken by using a well-framed questionnaire that was duly filled by the respondents. Respondents with varying background were selected based on the important aspects of their occupation, education, age, area etc. The primary data were supplemented by a spate of secondary sources of data. The secondary data pertaining to the study was gathered from the various. Structural Equation Modeling analysis was used for further analysis.

Results and Discussions

The research hypotheses have been defined on the basis of the deciding factors on financial performance of banking sector in Erode district. The following hypothesis was framed for the present study.

H_0: There is no significant relationship between value of share, increasing value of the bank, more profit than industry average, net income before tax, return on investment, gross annual turnover, return on equity, financial structure and liquidity and level of financial performance of banking sector.

H_1: There is a significant relationship between value of share, increasing value of the bank, more profit than industry average, net income before tax, return on investment, gross annual turnover, return on equity, financial structure and liquidity and level of financial performance of banking sector.

Table 1
Model Fit Indices Of The Deciding Factors On Financial Performance of Banking Sector

S.No.	Test Factor	Calculated Value	Acceptable Value
1	GFI (Goodness-of-fit-index)	0.933	>=0.90 and above satisfactory fit 0.80 to <0.9 acceptable fit (Hair et al.2006)
2	AGFI(Adjusted goodness-of-fit-index)	0.888	
3	CFI(Comparative fit index)	0.946	
4	NFI (Normed fit index)	0.914	
5	TLI (Tucker-Lewis index)	0.927	
6	RMSEA (Root mean square error of approximation)	0.08	0.08 or less would indicate a close fit of the model

It is evident from the above table which shows the model fit indices of value of share, increasing value of the bank, more profit than industry average, net income before tax, return on investment, gross annual turnover, return on equity, financial structure and liquidity and level of financial performance of banking sector. The Goodness of fit index (GFI) score is 0.933, adjusted goodness of fit index (AGFI) score is 0.888, comparative fit index (CFI) score is 0.946, normed fit index (NFI) score is 0.914, Trucker Lewis index (TLI) score is 0.927. The Root Mean Squared Error of Approximation (RMSEA) secured 0.08 that indicates that the model is a good fit with a reasonable error of approximation. From the analysis, it is inferred all the nine variables influence the financial performance of banking sector.

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Table 2
Regression Weights for Deciding Factors on Financial Performance of Banking Sector

Measured Variable		Latent Variable	Estimate	S.E.	C.R.	P
Value of share	<---	Financial Performance of Banking Sector	.604	.059	10.300	Significant at 1% level
Increasing value of the bank	<---	Financial Performance of Banking Sector	.646	.058	11.065	Significant at 1% level
More profit than industry average	<---	Financial Performance of Banking Sector	.608	.058	10.470	Significant at 1% level
Net income before tax	<---	Financial Performance of Banking Sector	.556	.061	9.047	Significant at 1% level
Return on investment	<---	Financial Performance of Banking Sector	.401	.065	6.167	Significant at 1% level
Gross annual turnover	<---	Financial Performance of Banking Sector	.458	.057	8.065	Significant at 1% level
Return on equity	<---	Financial Performance of Banking Sector	.604	.063	9.575	Significant at 1% level
Financial structure	<---	Financial Performance of Banking Sector	.738	.062	11.888	Significant at 1% level
Liquidity	<---	Financial Performance of Banking Sector	1.000			

From this result as shown in table 2, it is noted that estimates of the coefficient of financial structure (0.738) is high followed by increasing value (0.646) and it indicates that both factors are highly influencing the financial performance of banking sector. Further, the analysis indicated that all the variables are having positive relationship with the financial performance of banking sector and significant at 1% level.

Table 3
Variances for Deciding Factors on Financial Performance of Banking Sector

Variable	Estimate	S.E.	C.R.	P
Financial Performance of Banking Sector	.922	.136	6.763	Significant at 1% level
Value of share	.396	.042	9.418	Significant at 1% level
Increasing value of the bank	.354	.039	9.094	Significant at 1% level
More profit than industry average	.380	.041	9.353	Significant at 1% level
Net income before tax	.494	.050	9.795	Significant at 1% level
Return on investment	.671	.065	10.283	Significant at 1% level
Gross annual turnover	.457	.046	10.006	Significant at 1% level
Return on equity	.496	.051	9.654	Significant at 1% level
Financial structure	.351	.041	8.614	Significant at 1% level
Liquidity	.562	.068	8.325	Significant at 1% level

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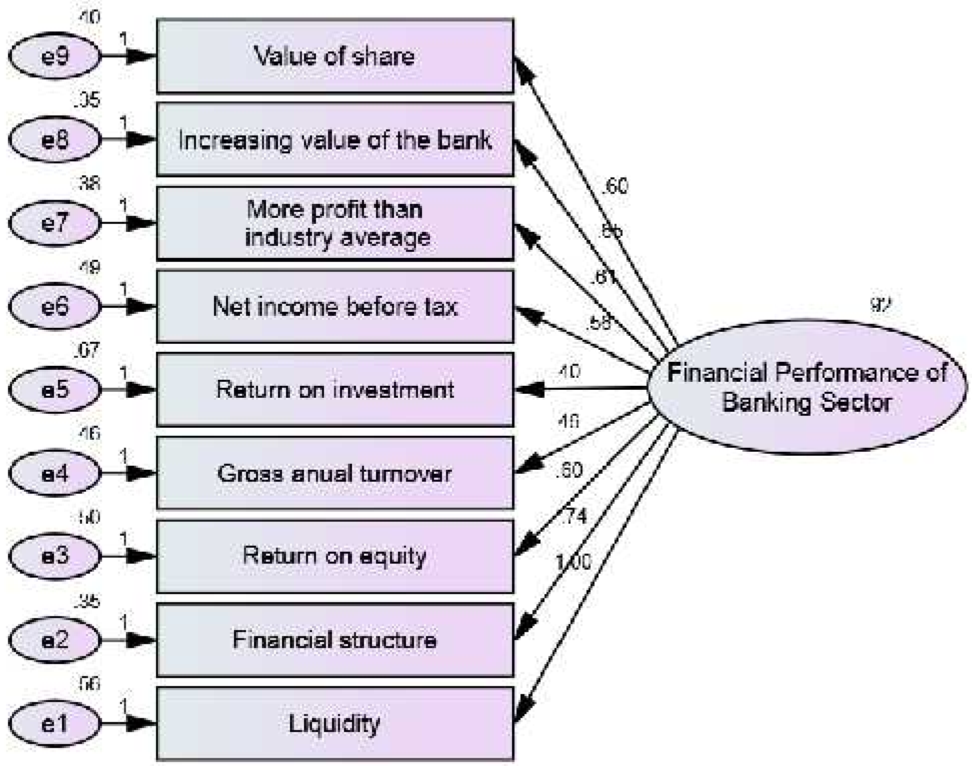
From this result as shown in table 3, it is noted that estimates of the coefficient of return on investment (0.671) is high followed by liquidity (0.562) and it indicates that both factors are highly influencing the financial performance of banking sector.

Chart 1
Path Diagram Of Deciding Factors On Financial Performance Of Banking Sector



The above path diagram shows that there is a significant relationship between the value of share, increasing value of the bank, more profit than industry average, net income before tax, return on investment, gross annual turnover, return on equity, financial structure and liquidity and level of financial performance of banking sector.

Recommendations and Conclusion
In recent years, there have been considerable pressures on the profitability of the banks and financial institutions, profitability is considered to be an index of financial health. Banks has to introduce modern marketing strategies and improve their credit and deposit proportion and also to generate non interest income. Today, the success of banking sector largely depends upon the financial performance of the firm. The importance of financial performance of banking sector can hardly be over emphasized. Much other business failure takes place due to poor financial performance. Hence, financial performance is considered as the lifeblood and the controlling nerve centre of a banking sector. Poor financial performance is a business ailment. Therefore, banking sector has to maintain the better financial performance. It is as important as blood circulation in our body to maintain life and flow of funds is very necessary to maintain business. New private sector Banks can improve their performance by identifying and concentrating on the relevant areas where the attention is much needed and there is scope for improvement. Poor financial performance affects the bank's solvency and the bank's profitability

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adversely. Profitability is a key result area where performance and results directly and virtually affect the survival.

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