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A Panel Data Analysis of Profitability Determinants: Empirical study of Indian Public and Private Sector Banks

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ABSTRACT

The present paper empirically analyses the determinants of profitability of 26 Public and 19 Private sector banks in India for the period from the year 2011-2016. The theoretical framework is based on the Market Power Theory (Bain, 1951) and Signalling Theory (Arrow, 1972 and Spence, 1973). A secondary source of data has been used. Return on Assets (ROA) has been used as a predictor of profitability of the Indian banks. Independent variables, namely spread ratio, provision and contingencies, credit-deposit ratio, operating expenses ratio, profit per employee, business per employee, non-interest income, investment deposit ratio, capital adequacy ratio, non-performing asset ratio, type of bank have been used. Correlation and panel data regression analysis has been used. Multicollinearity has also been checked with the help of VIF values. Various hypotheses have been developed on the basis of the review of the literature to test the association between the profitability of respective banks and other independent variables. The results show that 64.94% variation in return on assets is explained by variations in the independent variables. The study also reveals an interesting result that provision and contingencies (negative) significantly influences the profitability of banks @ 10%, non-interest income (positive), business per employee and capital adequacy ratio (positive) @ 5%, profit per employee (positive) and investment deposit ratio (negative) @ 1% respectively. Various variables, namely spread and the credit-deposit ratio has a positive insignificant association with profitability and operating expenses; non-performing assets have a negative insignificant association with profitability.

KEYWORDS: Public sector banks, Private sector banks, Profitability, ROA, Panel data.

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