Prof. Sultan Singh et… Journal of Management Research and Analysis (JMRA)
Available online at http://jmraonline.com
ISSN: 2394-2770, Impact Factor: 6.303, Volume 6 Issue 1(2), March -2019, Pages:141-146

Impact of Foreign Direct Investment Policy on the Productivity of Selected Indian Private Sector Banks

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ABSTRACT
The present study was conducted to examine the impact of foreign direct investment policy on productivity of selected Indian private sector banks during fourteen years from 2004-05 to 2017-18. The required data were collected from secondary sources like RBI Data-warehouse, Report on Trends and Progress of Banking in India, IBA Bulletins, Journals, and Online databases. The collected data were analyzed through inferential statistical techniques like correlation, t-test and Analysis of Variance (ANOVA) with the help of PASW (18.0 version). The study concluded that there is a significant correlation among Total Advances to Total Deposits (dependent) and FDI, Staff and Expenditure (independent variables). Hence, it is recommended that FDI in banking sector should assure better capitalization and also offer financial stability in India.
Keywords: RBI, Productivity, Expenditure, Correlation, Capitalization.

INTRODUCTION
The banking system in India is significantly different from other Asian nations mainly due to the country's unique geographic, social, and economic characteristics. India has a huge population and land size, a diverse culture and extreme disparities in income, which are noted among its regions. There is high level of illiteracy among huge part of population, but at the same time, the country has a large reservoir of managerial and technologically advanced talents (*Sharma and Krishna, 2013*). Today, Indian economy having a fairly well developed banking system with different classes of banks *viz.* public sector banks, foreign banks, private sector banks, regional rural banks and co-operative banks. In 1991, the Government opened the doors for foreign banks to start their operations in India and provide a wide range of facilities to customers, thereby providing a strong competition to the domestic banks and helping the customers in availing the best services (*www.choiceindia.com*).
Foreign Direct Investment (FDI) plays a significant role in the process of economic development. According to international guidelines based on the recommendation by the IMF (Balance of Payments Manual, 1993), FDI is defined as international investment that reflects the objective of a resident entity in one economy (foreign direct investor or parent enterprise) obtaining a lasting interest and control in an enterprise resident in an economy other than that of the foreign direct investor. "Lasting interest" implies the existence of a long-term relationship between a direct investor and the enterprise and a significant degree of influence on the management of the enterprise (*Malhotra, 2018*).

FDI flows (inflows and outflows) have occupied a prominent place in the global economy. It is an important avenue through which investment takes place in any country. The importance of FDI extends beyond the financial capital that flows into the country. FDI flows are vital for accelerating desired degree of growth and development. If this is so, then it is essential to known FDI's position of the world (*Laghane, 2007*). The world in general experienced a dramatic FDI boom beginning in the early 1990s, a trend that continues today, despite the financial crisis, which hit portfolio flows but not FDI. International flows of private capital to most developing countries rose sharply over this period. The surge in global FDI that began in the late nineties gain momentum in the 21st century. The average annual investment rose from US$ 93.8 billion in the 1980s to $388.3 billion in the 1990s, and averaged $541 billion in the latter half of the decade. Developing countries' FDI per GDP is found more than twice in comparison to developed countries. The major recipients of FDI are China, Brazil, Singapore, Thailand, Poland, Chile and Venezuela (*Paul, 2011*).

REVIEW OF LITERATURE

Marco and Lucia (2001) examined the various determinants for the growth of multinational banks and its effects on the foreign markets at micro level. They found that the availability of resources and international experience by the parent banks had positive impact on their decision to foreign direct investments. *Ghosh and Phani (2004)* examined the foreign direct investment limits, which were liberalized in India to allow more than 51 per cent ownership of private sector banks on February 2002. They found that the price increased higher than the smaller banks that have less debt, less efficient, less productive, and burdened with non-performing assets (NPA) and their valuation reflect the vulnerability to the premium of potential takeover of the ineffective banks, followed by liberalization. *Laifi (2007)* studied the impact of the Regional Integration Agreement (RIAs) on the location of the banking sector and the FDI. The results indicated that the impact of RIAs vary depending on different kinds of regional integration. *Tanna (2008)* stated that the aggregate inflows of the FDI yield productivity changes in the banking sector's effect on the economy and this may have a positive or negative effect on banks' technological progress and established the association between inward foreign direct investment (FDI) and bank level productivity changes. The results indicated that inward FDI has a negative short-term effect, but a positive long-term effect on total factor productivity change. *Ilgun and Coskun (2009)* analyzed the factors affecting the FDI inflows and focus in particular on the FDI in Bosnia and Herzegovinian banking sector. The study found that most of the banks and other financial institutions in financial services sector in Bosnia and Herzegovina (BIH) influenced by the foreign investors, especially from the European countries. *Kumari and Gupta (2012)* analyzed the impact of FDI in Indian banking sector and developing countries, and concluded that over the last decade, the fast pace of economic growth and progressive policy liberalization has made India an attractive destination for World's investments. *Garg (2013)* discussed the role of FDI in Indian banking sector and recognized that FDI in banking can address several issues pertaining to the sector such as encouraging development of innovative financial products, improving the efficiency of banking

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sector and better ability to adapt to changing financial market conditions. *Sharma and Krishna (2013)* discussed the history of banking system, necessity of FDI in banking system, guidelines for FDI and shows the statistics of FDI in Indian banking sector. They concluded that since India is a developing country and the people who are working in non-government organisations have less social security after their retirement. To encourage the saving habits among them, our banking sectors are introducing various schemes. Since the capital raising capacity in India is very less to take the Indian banking sector to worldwide, India require investment from abroad and suggested that RBI should make such policies that FDI should not over ride the regulations of RBI and should result in the growth of Indian economy. *Patil (2014)* investigated the performance of Indian FDI and non-FDI banks and found that the productivity of Indian banks had increased to some extent in the FDI liberalized period and showed a significant positive impact on return on assets (ROA) and total business of the banks, but showed a negative impact on the total net profits and income of the banks. *Tsaurai (2014)* investigated the causal relationship between banking sector development and FDI inflows in Botswana. Some of studies have found that there is no directional causality between banking sector development and FDI inflows into the host country. The results of the study shows that there is no direct causality relationship between banking sector development and FDI net inflows. *Patil (2017)* evaluated the productivity performance of Indian banks in the post liberalization era with FDI contents and found that the new private sector banks are mainly the banks with more FDI than other sub-groups, it is showing mixed effects of FDI time and content dummy that could be mainly due to the staff components of the productivity parameter as staff for these banks is continuously growing since they are new entrants to the business.

Induced by the previous revelations and reviews of earlier studies, this paper is an attempt to study the impact of Foreign Direct Investment policy on productivity of selected Indian private sector banks.

RESEARCH OBJECTIVE

The objective of the study is to examine the impact of foreign direct investment policy on the productivity of selected private sector banks.

RESEARCH HYPOTHESIS

The following hypotheses were formulated to achieve the objective and validate of the results of the study:

H_{01}: There is no significant relationship between the TATD and FDI, Staff and Expenditure of the selected private sector banks.

H_{02}: There is no significant contribution of FDI, Staff and Expenditure in the prediction of TATD in the selected private sector banks.

H_{03}: There is no significant impact of FDI, Staff and Expenditure on the productivity of selected private sector banks.

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RESEARCH METHODOLOGY

The present study used exploratory research design and includes sixteen old and new private sector banks *i.e.* Axis Bank, Catholic Syrian Bank Ltd., City Union Bank Limited, Dhanlaxmi Bank, Federal Bank, HDFC Bank, ICICI Bank, Indusind Bank, Jammu & Kashmir Bank Ltd, Karnataka Bank Ltd., Karur Vysya Bank, Kotak Mahindra Bank Ltd, Lakshmi Vilas Bank, South Indian Bank, Tamilnad Mercantile Bank Ltd. and Yes Bank Ltd. in India and considered a time span of fourteen years *i.e.* from 2004-05 to 2017-18. Foreign Direct Investment, Staff and Expenditure are the independent variables (*Patil, 2014 & Reddy, 2016*) and Total Advances to Total Deposits (TATD) is the dependent variable. The study used secondary data collected mainly from RBI Data warehouse, Report on Trends and Progress of Banking in India, IBA Bulletins, Journals and Online database. Multiple Regression technique was used to know the relationship among the variables and examine the impact of the independent variables on dependent variable. Further, ANOVA and independent Sample t-test have been used to test the research hypotheses and validate the results of the study.

RESULTS AND DISCUSSION

The impact of FDI on TATD for the period under the study from 2004-05 to 2017-18 is examined with the help of the following equation:

$$\mathbf{TATD = \beta_0 + \beta_1 \times FDI + \beta_2 \times Staff + \beta_3 \times Exp + e_1}$$

Where, **TATD** = Total Advances to Total Deposits of Private Sector Banks for the period under study, **FDI** = Foreign Direct Investment for the period under study, **Staff** = Staff for the period under study, **Exp** = Expenditure for the period under study, β_0 = Intercept (Constant), $\beta_1, \beta_2, \beta_3$ = The slope represents the degree with which bank's productivity changes as the independent variable changes by one unit of variable, and $e_{i,t}$ = error component.

Table-1 shows the coefficients of correlation of TATD with independent variables *i.e.* FDI, Staff and Expenditure are 0.578, 0.532 and 0.610 respectively. The *p*-values of correlation coefficients show that there is a significant relationship between dependent (TATD) and independent variables (FDI, Staff, and Expenditure). Further, there is a moderate degree of correlation between dependent and independent variables.

Table 1: Coefficients of Correlations among the Variables

Variables		**TATD**	**FDI**	**Staff**	**Exp**
Pearson Correlation	TATD	1.000			
	FDI	0.578	1.000		
	Staff	0.532	0.662	1.000	
	Exp	0.610	0.689	0.968	1.000
Sig.	TATD				
	FDI	0.010*			
	Staff	0.017*	0.003*		
	Exp	0.006*	0.002*	0.000*	

Source: Reports of RBI and IBA (various issues).

Note: *Significant at 5 percent level of significance.

Table-2 shows the coefficients of TATD, in which all the independent variables have been included in the model for prediction of dependent variable. The unstandardized beta values have been used to compare the contribution of each independent variable. The negative unstandardized beta coefficient shows an opposite relationship between dependent (TATD) and independent variable (Staff). The largest beta value *i.e.* 0.155 for FDI shows that the FDI contributed maximum in explaining the dependent variable. The result of t-test depicts that the contribution of independent variables is not significant for the prediction of the dependent variable as the *p*-values of all the independent variable (FDI, Staff and Expenditure) are greater than 0.05. Further, the results conclude that the dependent variable (TATD) is explained by the independent variables (FDI, Staff and Expenditure) to the level of 47.1 percent.

Table 2: Coefficients of TATD and Model Summary

Model		**Unstandardized Coefficients**		**t-value**	***p*-value**	**R-Square**
		beta	**Std. Error**			
1	(Constant)	65.969	4.564	14.456	0.000	0.471
	FDI	0.155	0.153	1.011	0.332	
	Staff	-0.001	0.000	-1.087	0.298	
	Exp	0.000	0.000	1.489	0.162	
a. Dependent Variable: TATD						

Source: Reports of RBI and IBA (various issues).

The ANOVA results shown in Table-3 depicts that there is a significant impact of independent variables on dependent variable (p=0.047). Therefore, the null hypothesis **(H_{01})** *i.e.* there is no significant impact of FDI, Staff and Expenditure on TATD, is rejected at 5 percent level of significance.

Table 3: ANOVA Results

Model	**Sum of Squares**	**Df**	**Mean Square**	**F**	**Sig.**
Regression	647.535	3	215.845	3.568	0.047*
Residual	725.880	12	60.490		
Total	1373.415	15			

Source: Reports of RBI and IBA (various issues).

Note: *Significant at 5 percent level of significance.

CONCLUSION AND RECOMMENDATIONS

The study concluded that there is a significant relationship between dependent (TATD) and independent variables (FDI, Staff and Expenditure). The results of t-test show that the contribution of independent variables is not significant in the prediction of the dependent variable. The dependent variable (TATD) is explained by the independent variables (FDI, Staff and Expenditure) to the level of 47.1 percent. Further, it is found that there is a significant impact of FDI, Staff and Expenditure (independent variables) on TATD (dependent variable). Therefore, it is suggested that bank should focus on the supportive liberalization FDI policy to change the productivity in banking sector. The study also recommended that RBI should introduce the policy related to pure efficacy, scale efficacy and technological change so that FDI in banking sector may ensure the better capitalization and financial stability.

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