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The Relevance of Internal Financing on Performance of Private Sector Banks

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Abstract: The main aim of the study is to study the trade-off between liquidity and profitability byanalysing the adequacy of working capital in private sector banks and forward relevant suggestions andrecommendations regarding Working Capital Management and highlight the relevance of internalfinancing on performance of private sector banks. It is concluded that the findings of the model estimatesuggest that there is a strong negative correlation and causal link between the ratios of total debt tocapital and long-term debt to capital, and the financial performance indicators of banks, namely Returnon Assets, Return on Equity, and Earnings per Share

Keywords: internal financing, performance, private sector banks, trade-off, liquidity, profitability, working capital management, adequacy, suggestions, recommendations

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INTRODUCTION

Effective working capital management is a crucial aspect of financial management within corporate organizations, as it enables the determination of the optimal allocation of cash for operational and investment purposes. An abundance of current assets within a corporation may lead to a diminished return on investment, while organizations with a scarcity of current assets may have liquidity deficiencies and encounter challenges in sustaining seamless operations. Hence, the proficient administration of working capital necessitates strategic oversight and regulation of both current assets and current liabilities, with the objective of fulfilling the immediate financial requirements of the corporate entity. Moreover, the successful management of working capital mitigates the risk of excessive investment in current assets. Working capital management pertains to the management of an organization's current assets and current liabilities, which in turn has a direct impact on the liquidity and profitability of the firm. The management of working capital involves striking a balance between the liquidity and profitability objectives of the firm while considering the associated risks. Working capital management pertains to the analysis and optimization of the differences between current assets and current liabilities, as well as the interconnectedness between managing current assets and current liabilities.

LITERATURE REVIEW

Sah, Gunja (2023) The objective of this article is to examine the impact of working capital management on the profitability of commercial banks. The study used empirical data to investigate the relationship between working capital management and indices of profitability. The calculation of various financial indicators was conducted based on empirical data. These indicators include the credit to deposit ratio, cash reserve ratio,

cash and bank balance to total deposits ratio, working capital turnover ratio, and liquidity ratios. The former set of ratios were considered as independent variables, while the latter set, consisting of return on assets, return on equity, and net profit margin, were treated as dependent variables. Out of the total of 20 commercial banks in Nepal, a sample size of seven commercial banks was selected for the purpose of this research study. The data included in this study were obtained from secondary sources, namely the annual reports of a model bank and the central bank. The data collection process employed a judgmental sampling approach, including the years 2012 to 2022. The investigation included the use of major financial ratios and statistical methods. Descriptive and inferential statistical methodologies are used to derive results. This research examined the statistical significance of three regression models, namely the Return on Assets (ROA), Return on Equity (ROE), and Net Profit Margin (NPM) models. The models of Return on Assets (ROA), Return on Equity (ROE), and Net Profit Margin (NPM) account for 41%, 52%, and 55% of the observed variability in the sample, respectively.

Jain, Yogesh (2023) The objective of this research study is to examine the efficacy of human capital management (HCM) strategies within the private sector banking industry in India. This research used the analysis of variance (ANOVA) approach to assess the effects of various human capital management (HCM) techniques on both employee performance and organizational results. The study focuses on fundamental aspects of Human Capital Management (HCM), including the areas of recruiting and selection, training and development, performance management, and pay and benefits. The results indicate notable disparities in employee performance and competencies because of different human capital management (HCM) strategies. The study's findings underscore the significance of using strategic human capital management (HCM) techniques inside private sector banks to enhance employee performance and effectively attain organizational objectives. Future study may include investigating other aspects and situations in order to further expand the comprehension of human capital management strategies within the banking industry.

Farooq, Umar & Tabash, Mosab (2023) The meticulous oversight of working capital management is crucial for corporate managers due to its significant impact on business stability. Managers were motivated by their sense of social belonging to engage in learning activities from their societal context, coworkers, and the broader industrial landscape. Additionally, they acquire knowledge from their colleagues who possess greater strategic efficiency. Aligned with these considerations, the primary aim of the present research is to investigate the impact of peer influence on the practices of working capital management inside corporations. In conducting regression analysis, we used a dataset spanning a decade (2009-2018) consisting of non-financial companies listed on the PSX (Pakistan Stock Exchange). The cash conversion cycle (CCC) was used as a surrogate variable for the assessment of working capital management (WCM). Panel fixed effect and system GMM (generalized method of moments) models were used to assess the regression relationship between the variables under investigation. The empirical evidence indicates that peer working capital management (WCM) has a significant influence on company WCM. Additionally, they propose that there are additional elements that have a substantial influence on the determination of working capital management (WCM). This paper proposes the implementation of a social learning policy for business managers. Individuals could acquire knowledge and skills in working capital management via interactions with their peers. The existing literature mostly focuses on the impact of peer influence on

various aspects such as investment choices, corporate cash holding, and finance policy. However, there is a notable gap in the literature on the examination of this relationship within the context under consideration.

Roopesh & Ganesh, Anjali (2023) The banking industry is widely recognized as a key driver of economic development. The significance of funding for all enterprises is underscored by its primary provision via banking institutions. The Indian banking industry has traditionally played a significant role in facilitating the growth of the overall economy. However, recent shifts in macroeconomic variables such as the COVID-19 pandemic, escalating inflation, political dynamics, and economic transformations have exerted a more pronounced influence on the performance of the banking sector. The present research seeks to assess the financial stability of the selected financial institutions by using Altman's Z-score model. The objective is to comprehend the financial soundness of banks by examining their bankruptcy state. The analysis reveals that a significant number of the chosen banks have had substantial impacts because of macroeconomic and structural developments, such as recent mergers within the public sector banking industry. The findings suggest that the banks are now experiencing financial difficulties and should develop strategic plans for their future operations to achieve improved outcomes. The research further emphasizes the significant technological advancements that are influencing the banking industry.

Mohanty, Sagarika (2023) The assessment of the banking industry's financial well-being necessitates a comprehensive examination within the context of the ongoing economic growth. The objective of this research is to assess the financial well-being of certain public and private sector banks in India. In this study, a total of seven important factors were carefully chosen and analyzed. The metrics under consideration include NIM%, CI%, Net NPA%, ROCE%, ROA%, ROE%, and CAR%. The study also examined the importance of banks' financial performance using the independent t-test. Based on the comparative analysis of the selected financial institution, Throughout the duration of the study, it became evident that HDFC Bank exhibits superior financial well-being in comparison to SBI. Additionally, recommendations are offered to enhance banking indicators. The research also discussed the constraints. Additional financial ratios may be explored in future research endeavors. This research will provide valuable insights for academicians, bankers, practitioners, and investors, enabling them to enhance their understanding of selected financial banking indicators and make informed investment choices.

RESEARCH METHODOLOGY

Research methodology refers to a structured and theoretical examination of the methodologies used in a particular area of research. The research technique encompasses the underlying assumptions and beliefs that serve as a foundation for the interpretation of data and formulation of findings. This research primarily examines the impact of various variables on key indicators of working capital management in both public and private sector banks. This chapter covers the procedures involved in gathering data, the research technique used, and the analytical tools utilized for data analysis. In addition, the researcher elucidates the process of deriving individual tools and calculates the recommended software programs using these statistical tools.

Research Design is theoretical framework that provide the guidelines for conducting research this research will be based on exploratory research as well as descriptive research.

The population of the research comprises all private sector banks that are currently functioning in India. The study's sample comprises banks that are listed on the national stock market and the Bombay Stock market, spanning the period from 2016 to 2022. The data used in this research were obtained from audited financial statements of publicly listed banks, as well as from the official websites of the National Stock Exchange, Bombay Stock Exchange, and the Reserve Bank of India.

DATA ANALYSIS

Private sector banks:

Table 1 Descriptive Statistics of ROA

	Mean	Std. Deviation	N
ROA	2.3355	9.41431	218
FS	11.7850	.94743	218
AG	19.5193	6.63793	218
LTDC	1.1166	.49725	218
STDC	17.6271	3.21388	218
TDC	18.0606	3.20360	218

The table presented provides descriptive information pertaining to the many aspects that influence the management of working capital. The average value of Return on Assets (ROA) is calculated to be 2.3355, with a corresponding standard deviation of 9.4341. The mean firm size is 11.785, with a standard deviation of 0.9437. The mean of asset growth is 19.51, with a standard deviation of 6.6349. The mean of LTDC is 1.11, with a standard deviation of 0.49725. The mean of the dataset is 17.621, while the standard deviation is 3.2138. The mean of the dataset is 18.0606, while the standard deviation is 3.20.

Table 2 Model Summary for ROA

Model	R	R Square	Adjusted R Square	Change Statistics				Durbin-Watson
				F Change	df1	df2	Sig. F Change	
1	0.622	.386	.32	3.235	5	212	.000	2.054

The table shown provides a model summary, indicating the significance of the chosen model. It displays the values of the correlation coefficient and coefficients of determination. The coefficient correlation value of 0.622 indicates a strong degree of connection between the return on assets (ROA) and all the independent components. The coefficient of determination (R2) has a value of 0.386, suggesting that about 38.60% of the variations in the return on assets (ROA) can be attributed to the independent variables included in the analysis. The remaining 61.40% of the changes in ROA are influenced by factors not accounted for in the model. Typically, this statistical data suggests a minimal level of effect. However, when other variables come into play and affect the entire performance of banking sectors, it aligns with the benchmark set by prior outcomes. The observed significance level of 0.000, which is less than the predetermined threshold of 0.05, indicates that there exists a statistically significant difference in the explained variance due to the

independent variables. Hence, the statistical significance of the multiple regression model is established. The Durbin-Watson statistic is calculated to be 2.054, a value falling within the range of 1 to 3.

Table 3 ANOVA for ROA

Model	Sum of Squares	Df	Mean Square	F	Sig.
Regression	11992.65	5	2398.53	69.95	.000
Residual	7269.90	212	34.29		
Total	19232.55	217			

The observed p-value is 0.000, which is less than the predetermined significance level of 0.05. As a result, the researcher rejects the null hypothesis, indicating that there is a statistically significant effect of the combined influence of all independent components, namely TDC, FS, LTDC, AG, and STDC, on ROA.

Table 4 Individual Impact of Independent Variables on ROA:

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Correlations		
	B	Std. Error	Beta			Zero-order	Partial	Part
(Constant)	-34.317	10.488		-3.272	.001			
FS	.577	.705	.259	3.656	.000	.233	.244	.242
AG	.116	.098	.082	1.190	.003	.065	.081	.079
LTDC	-.519	1.301	-.027	.399	.000	.016	.027	.026
STDC	-.18	.253	-.006	.072	.12	.029	.005	.005
TDC	-.272	.249	-.093	1.092	.004	.050	.075	.072

The researcher has gathered secondary data by examining the balance books of many well-established institutions. Subsequently, this panel data has been transformed into pool data. Hence, the use of standardized coefficients beta is preferred over un-standardized coefficients beta. The FS beta value is 0.259, accompanied by a t-statistic of 3.656 and a significance value of 0. This finding suggests that there is a positive relationship between FS and ROA. Specifically, a one-unit change in FS is associated with a 0.577-unit change in ROA. A zero-order correlation is used to assess the association between two variables. In this case, the correlation coefficient of 0.233 suggests a moderate amount of connection between the variable FS and the variable ROA. The partial correlation coefficient of 0.244 indicates that, holding all other independent variables constant, there is a relationship between FS and changes in ROA.

Table 5 Descriptive Statistics of ROE

	Mean	Std. Deviation	N
ROE	9.7667	5.37121	218
FS	11.7850	.94743	218
AG	19.5193	6.63793	218
LTDC	1.1166	.49725	218
STDC	17.6271	3.21388	218
TDC	18.0606	3.20360	218

The descriptive data reveal that the mean return on equity (ROE) is 9.7667 with a standard deviation of 5.37121. Additionally, the mean firm size is 11.7850 with a standard deviation of 0.9437. The mean asset growth is 19.51 with a standard deviation of 6.6349. The mean long-term debt coverage is 1.11 with a standard deviation of 0.49725. The mean short-term debt coverage is 17.621 with a standard deviation of 3.2138. Lastly, the mean total debt coverage is 18.0606 with a standard deviation of 3.20.

Table 6 Model Summary for ROE

Model	R	R Square	Adjusted R Square	Change Statistics				Durbin-Watson
				F Change	df1	df2	Sig. F Change	
1	.595	.354	.29	5.836	5	212	.000	1.53

The table shown above provides a summary of the model, indicating whether the chosen model is statistically significant or not. The coefficient of correlation in this case is 0.595, which above the threshold of 0.50. The data demonstrates a significant correlation coefficient between the dependent and independent variables. The coefficient of determination (R2) has a value of 0.354, indicating that 35.4% of the variation in the dependent variable, ROE, can be explained by the independent variables. The remaining 64.6% of the variation is attributed to other factors not included in the analysis. The F ratio has a value of 5.836, and the significance value is 0.000, which is below the threshold of 0.05. This indicates a significant difference between the explained variance resulting from all independent variables and the unexplained variance. Hence, the statistical significance of the multiple regression model is established. The Durbin-Watson statistic is calculated to be 1.53, a number that falls within the range of 1 to 3.

Table 7 ANOVA for ROE

Model	Sum of Squares	Df	Mean Square	F	Sig.
Regression	3724.95	5	744.99	62.34	.000[b]
Residual	2535.47	212	11.95		
Total	6260.420	217			

The objective of doing an analysis of variance (ANOVA) is to determine whether there exists a statistically significant influence of independent variables on the department variable. Based on the analysis of variance (ANOVA), it is evident that the obtained p-value is less than 0.05, indicating statistical significance. In this analysis, the null hypothesis is rejected in Favor of the alternative hypothesis, indicating a statistically significant influence of the independent variables on the dependent components.

Table 8 Individual Impact of Independent Variables on ROE Coefficients

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Correlations		
	B	Std. Error	Beta			Zero- order	Partial	Part
(Constant)	-1.062	5.820		-.183	.855			
FS	.601	.391	.106	1.536	.000	.083	-.105	.099
AG	.268	.054	.331	4.950	.000	.314	.322	.319
LTDC	-.358	.722	-.033	-.496	. 000	-.065	-.034	-.032
STDC	-.163	.140	-.097	-1.159	.248	-.042	-.079	-.075
TDC	-.099	.138	-.059	-.714	.001	-.037	-.049	-.046
STDC	-.163	.140	-.097	-1.159	.248	-.042	-.079	-.075
TDC	-.099	.138	-.059	-.714	.001	-.037	-.049	-.046

The beta value for FS is determined to be 0.106, with a t-statistic of 1.536. The significance value is reported as 0.00, suggesting a strong indication that FS positively contributes to the return on equity (ROE). When the financial leverage ratio (FS) increases by 1 unit, the return on equity (ROE) changes by about 0.601 units. Zero-order correlations are used to assess the association between two variables. In this case, a correlation coefficient of 0.083 suggests a moderate degree of connection with Return on Equity (ROE). The partial correlation coefficient of 0.105 indicates that, holding all other independent variables constant, there is a relationship between FS and changes in ROE. The beta value for AG is determined to be 0.331, with a t-statistic of 4.95 and a significance value of 0.00. These results suggest that AG has a positive impact on ROE. Specifically, for every 1 unit change in AG, there is a corresponding change of 0.268 units in ROE. Zero-order correlations are used to assess the association between two variables. In this case, a correlation coefficient of 0.314 suggests a moderate degree of connection with Return on Equity (ROE). The partial correlation coefficient of 0.322 indicates that, while holding all other independent variables constant, there is a relationship between AG and changes in ROE.

CONCLUSION

The study's results indicate that both public sector and private sector banks in India exhibit a greater reliance on debt financing as opposed to equity financing. This suggests the existence of a negative trade-off between a firm's leverage and its performance. The effect was not detected in relation to the short-term debt-to-equity ratio, hence suggesting a favorable influence on the performance of private banks in India when using client deposits and other forms of short-term financing. Conversely, there exists a positive correlation between Firm Size and Asset Growth with variables such as Return on Assets (ROA), Earnings per Share (EPS), and Return on Equity (ROE).

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