

Determinants of Managerial Effectiveness and Bank Performance – A Conceptual Study with Special Reference to Scheduled Urban Cooperative Banks in India

Mohan Kumar Mishra¹, Prof. Amit Mookerjee²

¹ Research Scholar, University School of Management & Entrepreneurship, Delhi Technological University (DTU).

Email: mohanmishra7ad@gmail.com

² HOD, University School of Management & Entrepreneurship, Delhi Technological University (DTU).

Email: amookerjee@dtu.ac.in

Abstract

Urban Cooperative Banks (UCBs) in India play a pivotal role in fostering financial inclusion, particularly in urban and semi-urban areas. However, recent events have highlighted significant challenges faced by these banks, including mounting Non-Performing Assets (NPAs), governance deficiencies, and technological lag. This research aims to investigate the intricate interplay between managerial effectiveness, governance structures, and bank performance within UCBs. Drawing upon a comprehensive literature review, the study proposes hypotheses exploring the influence of the board, external oversight, and professional management on managerial effectiveness and bank performance. The statistical design of this proposed research encompasses a multifaceted approach, incorporating a diverse range of statistical measures to meticulously analyze data and derive meaningful insights. Drawing upon primary data collected from a specified sample size, the study employs rigorous statistical analyses to ensure the reliability and validity of the variables under scrutiny. Key statistical tools such as Cronbach's Alpha, Variance Inflation Factor (VIF), and Tolerance tests are utilized to assess reliability and interrelationships among variables. Furthermore, ANOVA and Structural Equation Modeling (SEM) are utilized to analyze variance and explore intricate relationships among variables. These methodological approaches are informed by insights gathered from prior research studies, with the overarching aim of providing comprehensive insights into the determinants of managerial effectiveness and performance. Ultimately, the study endeavors to offer valuable implications for managerial decision-making processes. Accordingly, the study anticipates findings that will contribute to understanding the governance dynamics of UCBs and their impact on bank performance, with implications for policymakers, regulators, and stakeholders. By shedding light on these complex dynamics, the research seeks to enhance the resilience and sustainability of cooperative banking in India, ultimately contributing to the broader goal of financial stability and inclusive growth.

Keywords: Scheduled UCBs, Governance, Professional Management, External Control, Managerial Effectiveness and Performance.

I. INTRODUCTION AND METHODOLOGY

Urban Cooperative Banks play a great and supportive role in achieving financial inclusion especially in the urban and semi-urban areas in India. As on March 31st 2021 there are 1534 UCBs operating in India of which there are 53 Scheduled UCBs and 1481 Non-Scheduled UCBs. Most of them are single branch entities, with limited avenues to raise capital. Despite their large number, UCBs account for 3.4% of the Total Assets of Scheduled Commercial Banks (SCBs). Deposits, which accounted for 80.10% of the resource base of UCBs and the average growth rate of deposits is 5.20% achieved during 2020-21. The composition of credit to the priority sector by UCBs shows that lending to MSMEs accounted for 32.40% of the total priority sector advances, followed by advances to housing (8.10%). (Compiled from RBI Report on Trends and Progress of Banking in India 2020-21).

Need for the Study

The spate of failures among cooperative banks such as Madhavpura Cooperative Bank, PMC Bank, CKP Bank, Mumbai Mercantile Cooperative Bank, and Mumbai DCCB stresses a unrelenting concern. These failures, attributed to rising Non-Performing Assets (NPAs), weak governance, inadequate internal checks and controls, and a lack of professionalism and technological adoption, have shaken depositor confidence. The Punjab and Maharashtra Cooperative (PMC) bank crisis, in particular, led to chaotic scenes as depositors rushed to withdraw their funds. According to the Trends and Progress of

Banking in India report by the Reserve Bank of India (RBI), urban cooperative banks have witnessed significant declines in deposits and loans. In terms of loans and advances too, there has been a sharp decline from 8 per cent in 2018-19 to 0.8 per cent in 2019-20 (Times of India, 2021). This downward trend is alarming, with 21 banks currently under RBI's All-Inclusive Directions (AID), many of which have been under moratorium for years. In light of these challenges, there is a critical need to study the influence and impact of managerial effectiveness on the performance of scheduled urban cooperative banks in India. Understanding how managerial decisions, oversight, and strategic direction affect these banks' stability, growth, and ability to serve their communities is paramount. Such research can provide insights into enhancing governance practices, improving risk management, and fostering sustainable growth in the cooperative banking sector, ultimately safeguarding depositors' interests and contributing to financial stability.

Review of Literature and Research Gap

The literature on managerial effectiveness delves into predictors such as managerial perception, skills, and knowledge, as identified by Analoui (1995, 1997, 1999, 2007). Bamel et al. (2015) explore perceived behavioral indicators of managerial effectiveness in the Indian context. Negi & Dangwal (2021) focus on assessing managerial effectiveness in Indian banks. Studies by Dabbou & Mahjoub (2020) emphasize managerial ability's role in banking institutions' liquidity creation. Mallick & Das (2020) highlight a positive association between management ability and Non-Interest Income to Working Fund (NNIWF) but note negative relationships with Cost of Deposits (COPD) and BPE. Research by Kiong Ting et al. (2021) underscores the importance of managerial ability in firm success. Sanchez et al. (2018) and Andreou et al. (2015) investigate the interplay between governance mechanisms and managerial ability, emphasizing its role in investment efficiency. Ajit Kumar & Srivatsava (2020) examine factors influencing the failure of Urban Cooperative Banks (UCBs) in India, while Roman et al. (2020) evaluate management efficiency in Nigerian banks. Luu et al. (2021) find that banks with capable management have lower probabilities of failure. Regarding performance metrics, Muhammad Hamza (2017) and Sebayang (2020) discuss the impact of Capital Adequacy Ratio (CAR) on banking performance, while Sangmi (2010) cautions against excessively high CARs. Jadhav et al. (2021) argue that CAR isn't the sole determinant of bank profitability. Though many studies were carried out to understand bank failures worldwide, (Hawang, Lee, & K., 1997, Dwyer Jr & R.W.Hafer, 2001, Estrella, 2000, Wheelock & Wilson, 2000, Gupta, 2021) there are not many rigorous studies available to understand the failure of cooperative banks in India. Moreover, the failure of one cooperative bank will affect not only the failed bank but also the entire cooperative banking system in the States. The studies states that the failures can be attributed mainly to the management's inefficiency (Office of the Comptroller of the Currency, 1988) and poor control in the business activities (Jensen (1993), Weisbach (1988) and Brickley, Coles, and Terry (1994); (Times of India, January 5, 2002); (Sapovadia, Pleonexia and Politics over Professionalism: Collapsing Cooperative Banks, Sanusi, 2009); (Luua, Doanc, & Anh, 2021) (Ghalib, 2018). Increasing of non-performing assets and growth of financial irregularities has a major role in many of the bank's failure. In this context, it becomes important to understand the antecedents for and their inter-relationships between managerial effectiveness and performance of Urban Cooperative Banks. The literature emphasizes the importance of managerial effectiveness in organizational success, particularly in banking. However, there's a gap in correlating managerial effectiveness with the performance of scheduled urban co-operative banks in India, warranting further research and this proposed study fills the gap.

Objectives of the Study

The primary aim of this study is to examine the extent to which managerial effectiveness influences the performance of Scheduled Urban Cooperative Banks in India, along with exploring the relationships among different variables. Specifically, it endeavors to address the following objectives:

- a. Identifying the constructs that are affecting the managerial effectiveness of SUCBs.
- b. Investigating the correlation between managerial effectiveness and profitability within SUCBs.
- c. Through research into these aspects, the study aims to provide valuable insights into the dynamics of managerial effectiveness and its influence on the financial performance of Scheduled Urban Cooperative Banks.

II. PROPOSED HYPOTHESES AND CONCEPTUAL MODEL

1. Governance and Managerial Effectiveness

This proximity of the Board increases the influence the board in the day –to –day administration of the business. The board members are also elected through their political affixations and so the political considerations in the board's decision

making are general. (Chancharat, Detthamrong, & Chancharat, 2019). Considering the fact that bad credit policy is by itself a fall-out of the combined effects of board interference as shown by the report of the 2009 CBN-NDIC special examination of Nigeria banks that indicted the chief executive officers/managing directors and executive directors of distressed banks, leading to their being sacked (CBN, 2009; Sanusi, 2009), it follows that the combined contribution of the board members' poor conduct (by way of undue interference and unethical credit and risk management) to the distress of Financial Institutions, Commercial Banks, Community Banks and Finance Houses. The board and management of the banks used fraudulent financial statements to cover-up the negative effects of their corrupt and unethical practices. (Akhidime, 2018). The board and management of these banks had abandoned the key elements of good corporate principles of honesty, trust, and integrity, openness, performance orientation, responsibility, and accountability, mutual respect and had become corrupt, inactive and greedy, (Oghojafor, et. al 2010). Corporate governance is expected to be maintained externally through regulatory agencies (the Central Bank of Ghana and the Association of Rural Banks) and internally through the respective Boards of Directors. (Adu-Amoah, Tsamenyi, & Onumah).

H0 – There is no relation between governance and managerial effectiveness.

H1 – There is a relation between governance and managerial effectiveness.

2. Professional Management and Managerial Effectiveness

The effective management is draws from professional management. Professional management demands qualified personnel, effective policies and procedures and strong internal control system. Lack of professionalism in management will affect the quality of the decisions and financial as well as non-financial difficulties for the bank (Times of India, January 5, 2002). On the drivers of fraudulent financial reporting, this study confirms that poor and weak corporate governance as characterized by weak internal control and lax supervision are factors that drive fraudulent financial reporting (Akbar, 2017). Lack of transparency, improper human resource management and political influence leads to ignoring the legal norms. These are the root cause of deviation from the stated path of banking business. Relation matters more than the relevance and reliability check. Staff hardly gets the training to compete with other commercial banks. The knowledge required to work in bank pertains to finance, accounting, law and technology is not only poor, it is considered useless. The lack professionalism is prime cause of bank failure (Sapovadia, Pleonexia and Politics over Professionalism: Collapsing Cooperative Banks).

H0 – There is no relation between professional management and managerial effectiveness.

H1 - There is a relation between professional management and managerial effectiveness.

3. External Control and Managerial Effectiveness

The Registrar of State Cooperatives regulates or oversees 'cooperative' part of the cooperative bank while RBI regulates or oversees 'banking' part. The Registrar is concerned with registration, liquidation and adherence of operations with principles of cooperatives. Registrar is responsible to ensure shareholders rights, board and general meeting resolutions, dividend distributions, reserve, contribution to government etc. RBI is concerned with liquidity, capital adequacy, financial exposure, non-performing assets or bad loans and related matters. The Registrar of Cooperative Societies (RCS) is in control of management elections and many administrative issues as well as auditing. And the RBI brought them under the Banking Regulation Act as applicable to cooperative societies, which included all the regulatory aspects (Sapovadia, Pleonexia and Politics over Professionalism: Collapsing Cooperative Banks).

H0 – There is no relation between external control and managerial effectiveness.

H1 – There is a relation between external control and managerial effectiveness.

4. Managerial Effectiveness and Bank Performance

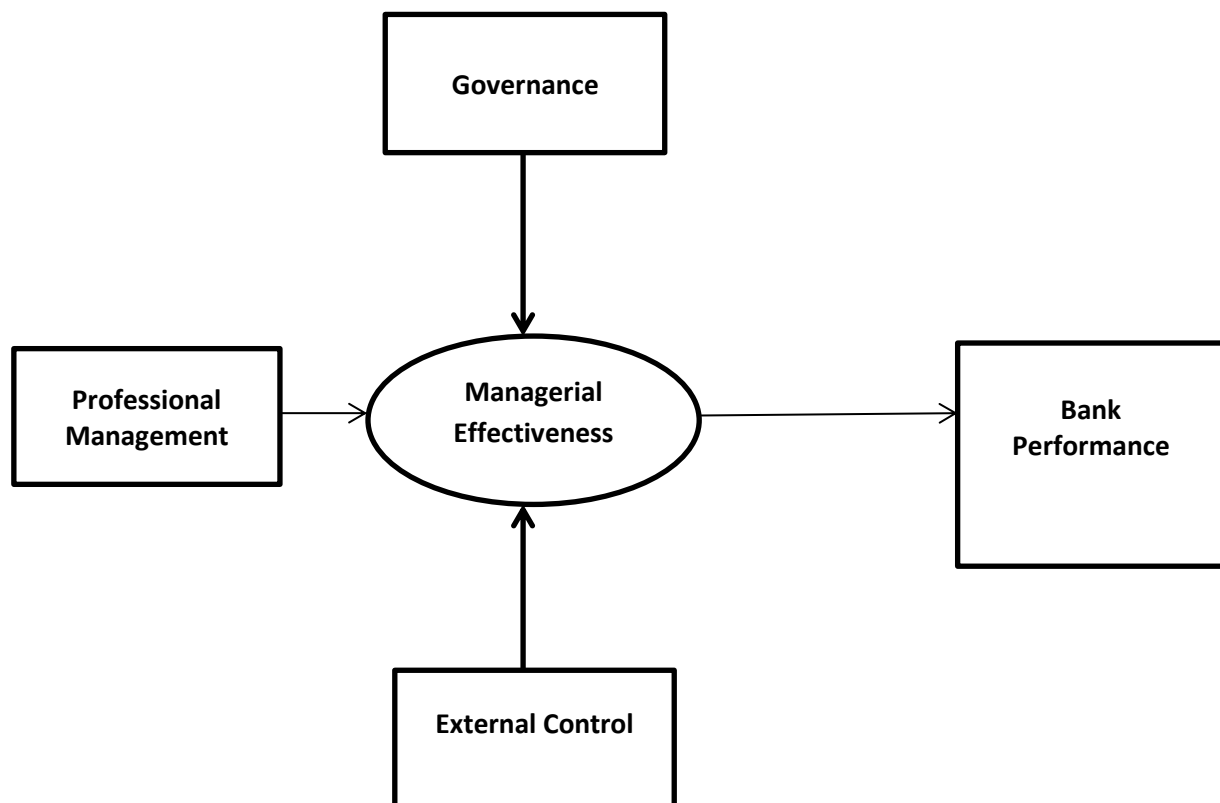
The performance of the bank is influenced by the managerial effectiveness. Managerial effectiveness is determined by extent of influence of Board of Directors, external control and professional management. Ineffective decisions in sanctioning of loans and advances leads to poor repayment and recovery of loans from the customer that in turn increase the non-performing assets of the bank. Accumulation of non-performing assets leads to financial loss those results in failure. In the same vein, the banks were accused of having displayed excessively high level of non-performing loans

which was attributable to, lax administration processes, non-adherence to the banks' credit risk management practices and poor corporate governance practices (Sanusi, 2009). (Luua, Doanc, & Anhc, 2021) find that more ably managed banks experienced lower failure probability. Further analyses provide support to this finding and reveal that more ably managed banks are associated with more adequate capital, better asset quality, and greater efficiency in the allocation of resources, higher liquidity and lower risk. (Ghalib, 2018) This finding implies that improving the practice of GCG and combining it with better credit risk management and the right business strategy are the best way to improve banks' profitability. Poor managerial effectiveness means lose control that weakens the effectiveness of the management of business. Lose control leads to weak internal control system. This provides scope for financial irregularities, misappropriation of bank funds and frauds that results in failure of bank.

H0 – There is no relation between managerial effectiveness and performance.

H1 - There is a relation managerial effectiveness and performance.

Proposed Research Model



III. RESEARCH DESIGN

In preparation for analyzing the determinants of managerial effectiveness, a structured questionnaire comprising 42 statements rated on a five-point scale (ranging from 5 for strongly agree to 1 for strongly disagree) has been developed. This questionnaire is set to be administered to a sample size of 300 board of directors and chief executives drawn from 50 SUCBs, with each SUCB contributing 6 participants. The forthcoming study is also centered on examining Scheduled Urban Cooperative Banks (SUCBs) within the Indian context through secondary data. It will rely on secondary data obtained from two primary sources: the RBI Database on Indian Economy – Primary (Urban) Cooperative Banks' Outlook and the annual reports of the respective scheduled UCBs. This data spans an extensive eight-year period, ranging from 2014-15 to 2021-22. The annual reports of the banks were sourced directly from their official websites. As of March 31st, 2022, the total count of SUCBs stood at 53. However, three banks have been excluded from the study for specific reasons: Punjab-Maharashtra Cooperative Bank due to its failure, and Kapol Co-operative Bank Limited, Mumbai, and Rupee Co-

operative Bank Limited, owing to unfavorable performance metrics such as negative Net Interest Margin (NIM) and Capital to Risk (Weighted) Assets Ratio (CRAR). Consequently, the study's focus narrows down to a universe of 50 SUCBs for analysis.

i. Definition of Constructs

Central to the performance of any banking entity is the pivotal role played by sound management practices. These practices fortify the very essence of efficient operations and strategic decision-making within a bank's framework. (Purohit & Mazumdar, 2003) assert that evaluating the performance of management capacity often entails qualitative assessments, relying on subjective evaluations of management systems, organizational culture, and control mechanisms. However, with the support of the analysis by Purohit, et.al-2003, management capability has been carried out by (Mohi-ud-Din & Tabassum, 2010) in their analysis with the help of six productivity ratios as explained in integral part of the CAMEL model. In the line of the above, also a study by (Trivedi) highlights that the efficacy of a bank's management extends beyond conventional oversight and encompasses the administrative competence to navigate and respond proficiently to diverse and challenging circumstances. Trivedi's examination of a scheduled Urban Co-operative Bank employs six meticulously chosen ratios as a constituent part of the CAMEL model, an established framework for assessing the overall health of financial institutions, supports the investigation into the potential dynamics of management efficiency within the bank. Given the intricate nature of assessing managerial effectiveness, the present study exercises meticulous care and consideration in its approach. The utilization of specific ratios serves as a thoughtful methodology aimed at quantifying and evaluating the various facets of managerial effectiveness within the banking context. These selected ratios are carefully chosen to measure and portray the nuanced aspects of managerial proficiency and effectiveness within the banking environment and they are; (i) Expenditure to Income Ratio (EIR), (ii) Total Advances to Total Deposits Ratio (TATDR), (iii) Diversification Ratio (DR), (iv) Business Per Employee (BPE) and (v) CRAR.

Through a comprehensive literature review, the determinants of managerial effectiveness have been thoroughly examined. Key factors such as Governance, Professional Management, and External Control have been clearly delineated through relevant constructs, as outlined in the Annexure. Given the dearth of comprehensive investigations in this field, this study aligns with the trajectory established by prior research efforts. It focuses on employing ROA, and NIM as the chosen performance measures within the framework of managerial effectiveness and performance analysis in Urban Cooperative Banks. By utilizing these established performance indicators, this study aims to contribute to the ongoing discourse on governance-related factors and their impact on the financial performance of UCBs, building upon the limited yet notable groundwork laid by previous scholarly inquiries (*Annexure-1, describes the key variables to be examined in this study*).

ii. Statistical Design for Proposed Study

The study employs a robust array of statistical tools to ensure the reliability and validity of the gathered primary data. Reliability analysis will be conducted using Cronbach's Alpha, while collinearity tests, including Variance Inflation Factor (VIF) and Tolerance, will assess variable interrelationships. Statistical measures such as Arithmetic Mean (AM), Standard Deviation (SD), Coefficient of Variation (CV), Skewness, and Kurtosis will be computed, with Shapiro-Wilk-W and Shapiro-Wilk-p tests ensuring data normality. Correlation analysis will explore relationships between variables using the correlation coefficient (r), and multiple regression analysis will identify key drivers of financial success, with the coefficient of determination (R²) measuring the predictive power of the model. These methodologies are grounded in the works of Purohit et al. (2003), Mohi-ud-Din & Tabassum (2010), Mallick & Das (2020), and Kumar et al. (2021).

Further, linear regression equations will model variable relationships, with t-tests assessing the significance of regression coefficients. ANOVA will analyze variance among groups, evaluating the overall significance of the regression model. Structural Equation Modeling (SEM) will explore complex variable relationships and their impacts, providing a comprehensive understanding of underlying dynamics. This combination of statistical techniques aims to elucidate managerial effectiveness and performance determinants, offering valuable insights for managerial decision-making within the designated segments.

(a) Managerial Effectiveness and Performance

In the context of examining the relationship between managerial effectiveness and performance, the proposed study employs multiple regression analysis. This analytical approach investigates the combined impact of various managerial

effectiveness indicators on performance metrics, specifically focusing on Net Interest Margin (NIM) and Return on Assets (ROA) as separate dependent variables.

(i) Model estimation for the dependent variable NIM

For NIM as the dependent variable, the regression model used in this study is:

$$\text{NIM} = \alpha + \beta_1 \times \text{EIR} + \beta_2 \times \text{TATDR} + \beta_3 \times \text{DR} + \beta_4 \times \text{BPE} + \beta_5 \times \text{CRAR} + \epsilon$$

In this study, NIM is the dependent variable, α is the intercept term. $\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ are the coefficients associated with the predictors EIR, TATDR, DR, BPE, CRAR respectively.

Hypothesis:

H0: There is no significant relationship between managerial effectiveness and performance (NIM).

H1: There is a significant relationship between managerial effectiveness and performance (NIM).

(ii) Model estimation for the dependent variable ROA

For ROA as the dependent variable, the regression model employed in this study is:

$$\text{ROA} = \alpha + \beta_1 \times \text{EIR} + \beta_2 \times \text{TATDR} + \beta_3 \times \text{DR} + \beta_4 \times \text{BPE} + \beta_5 \times \text{CRAR} + \epsilon$$

Similarly, in this equation, ROA denotes the dependent variable, where α is the intercept term. $\beta_1, \beta_2, \beta_3, \beta_4, \beta_5$ are the coefficients correspond to the predictors EIR, TATDR, DR, BPE, CRAR respectively.

Hypothesis:

H0: There is no significant relationship between managerial effectiveness and performance (ROA).

H1: There is a significant relationship between managerial effectiveness and performance (ROA).

IV. PROPOSED OUTCOME AND PROSPECTIVE CONTRIBUTION OF THE STUDY

The proposed study aims to investigate the governance structures and managerial effectiveness within Urban Cooperative Banks (UCBs) in India, examining their impact on bank performance and failures. Key hypotheses include the relationship between board influence in daily administration, external control mechanisms, professional management practices, and their collective effect on managerial effectiveness and bank performance. The study explores how regulatory oversight from bodies like the Registrar of State Cooperatives and the Reserve Bank of India (RBI) impacts managerial effectiveness, and investigates the role of professional management in fostering effectiveness within UCBs. The findings aim to enhance understanding of the factors driving bank failures in the cooperative sector, offering valuable insights for policymakers, regulators, and stakeholders to strengthen governance practices, improve managerial effectiveness, and mitigate bank failure risks. This study will also provide a foundation for future research on cooperative bank failures and policy interventions to address systemic weaknesses, contributing to the resilience and sustainability of cooperative banking in India.

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Annexure - 1:

Table – 1: Key Variables Examined

Sl. No.	Variables	Description
1.	Expenditure to Income Ratio (EIR)	Refers to the share of total expenses on the total income of a bank.
2.	Total Advances to Total Deposits Ratio (TATDR)	Measure of bank’s competence to convert the deposits available with the bank into high earning advances.
3.	Diversification Ratio (DR)	Measure of banks income other than the interest income in total income.
4.	Business Per Employee (BPE)	Indicates the efficiency of bank in terms of doing business with lesser number of employees.
5.	Capital to Risk-weighted Assets Ratio (CRAR)	An indispensable metric, serving as a vital indicator of a bank’s financial health and stability.
6.	Net Interest Margin (NIM)	Reflects the difference between the interest income generated from loans and investments and the interest paid on deposits and borrowings.
7.	Return on Assets (ROA)	Indicates the efficiency of a bank in utilizing its assets to generate profit.