

# Corporate Governance in the Indian Banking Sector: A Critical Comparative Analysis of Public and Private Sector Banks in the Post-Liberalization Era

Ankita Tyagi<sup>1</sup>, Dr. Anumesha Sahai<sup>2</sup>

Amity University

**Abstract:** *Corporate governance has become a central pillar in ensuring transparency, accountability, and efficiency in the banking sector. In India, the post-liberalization period (after 1991) witnessed significant transformations in banking governance structures, regulatory frameworks, and operational efficiency. This paper critically examines corporate governance practices in public and private sector banks, highlighting key differences in ownership structure, board composition, regulatory compliance, risk management, and performance outcomes. The study also evaluates the role of the Reserve Bank of India (RBI) and government reforms in strengthening governance norms. The findings reveal that while private sector banks exhibit relatively stronger governance practices due to market discipline and autonomy, public sector banks continue to face challenges due to political interference and structural rigidities. The paper concludes with policy recommendations aimed at strengthening governance frameworks in both sectors.*

**Keywords:** Corporate Governance, Indian Banking Sector, Public Sector Banks, Private Sector Banks, RBI, Liberalization, Transparency, Accountability

## 1. Introduction

Corporate governance has emerged as a cornerstone of modern financial systems, particularly in the banking sector where institutions operate as custodians of public funds and facilitators of economic growth. In its broadest sense, corporate governance refers to the framework of rules, relationships, systems, and processes within and by which authority is exercised and controlled in corporations. In the context of banks, it assumes heightened significance due to their systemic importance, high leverage, and direct impact on financial stability.

The Indian banking sector has undergone a profound transformation over the past few decades, especially following the landmark economic reforms of 1991. Prior to liberalization, the sector was characterized by state dominance, limited competition, and a relatively weak governance framework. Public sector banks (PSBs), which accounted for the majority of banking assets, operated under significant government control, often prioritizing social banking objectives over efficiency and profitability. While this approach facilitated financial inclusion, it also led to issues such as inefficiency, poor asset quality, and weak accountability mechanisms.<sup>1</sup>

The liberalization reforms initiated in 1991 marked a decisive shift towards a market-oriented economy. These reforms introduced private sector participation, enhanced competition, and emphasized prudential regulation. As a result, corporate governance gained prominence as a critical tool for ensuring transparency, accountability, and efficiency in banking operations. The entry of new private sector banks brought with it modern management practices, technological advancements, and a stronger focus on shareholder value.<sup>2</sup>

In the post-liberalization era, the role of regulatory institutions, particularly the Reserve Bank of India (RBI), has been instrumental in strengthening corporate governance norms. The RBI has introduced various guidelines aimed at improving board effectiveness, risk management, and disclosure standards. These include the “fit and proper” criteria for directors, the establishment of audit committees, and the adoption of international best practices such as the Basel norms.<sup>3</sup> Such measures have contributed to enhancing the overall governance framework within the banking sector.

Despite these developments, significant differences persist between public and private sector banks in terms of governance practices. Public sector banks continue to face challenges arising from their ownership structure, including government interference in managerial decisions, lack of operational autonomy, and bureaucratic inefficiencies. These factors often hinder timely decision-making and weaken accountability mechanisms. Moreover, PSBs have historically been more vulnerable to the problem of non-performing assets (NPAs), which has raised concerns about the effectiveness of their governance structures.<sup>4</sup>

On the other hand, private sector banks are generally perceived to have stronger governance frameworks due to their ownership patterns, professional management, and market discipline. The presence of institutional investors and the need to meet shareholder expectations create incentives for greater transparency and efficiency. Additionally, private banks tend to adopt advanced risk management practices and leverage technology to enhance operational performance. However, it is important to note that private sector banks are not immune to governance failures, as evidenced by

<sup>1</sup> Narasimham Committee Report I (1991), Government of India.

<sup>2</sup> Sarkar, J. & Sarkar, S., *Banking Sector Reforms in India*, Oxford University Press, 2018.

<sup>3</sup> Reserve Bank of India, *Report on Trend and Progress of Banking in India*, various issues.

<sup>4</sup> Acharya, V.V., “The Future of Indian Banking,” RBI Lecture Series, 2017.

instances of corporate fraud, mismanagement, and leadership conflicts in recent years.<sup>5</sup>

The importance of corporate governance in the banking sector is further underscored by the increasing complexity of financial transactions, globalization of financial markets, and the growing reliance on digital technologies. In this dynamic environment, weak governance can lead to serious consequences, including financial instability, loss of public confidence, and systemic crises. Therefore, strengthening governance mechanisms is not merely a regulatory requirement but a strategic necessity for ensuring sustainable growth and resilience in the banking sector.<sup>6</sup>

Another crucial dimension of corporate governance in Indian banking is the balance between regulatory oversight and managerial autonomy. While stringent regulations are essential to prevent misconduct and ensure stability, excessive control can stifle innovation and efficiency. This is particularly relevant for public sector banks, where the dual control of the government and the RBI often creates ambiguity in accountability and decision-making processes. In contrast, private sector banks enjoy relatively greater autonomy, enabling them to respond more effectively to market dynamics.<sup>7</sup>

Furthermore, the post-liberalization period has witnessed several reforms aimed at improving governance in public sector banks, including recapitalization initiatives, consolidation through mergers, and the introduction of performance-based evaluation systems. These measures have yielded positive results to some extent, as evidenced by improvements in asset quality and profitability indicators. However, structural challenges remain, necessitating further reforms to align governance practices in PSBs with global standards.<sup>8</sup>

This research paper seeks to undertake a critical comparative analysis of corporate governance practices in public and private sector banks in India during the post-liberalization era. It aims to examine the key determinants of governance, evaluate their impact on performance, and identify the challenges faced by each sector. By analyzing the differences and similarities in governance frameworks, the study intends to provide insights into the effectiveness of existing regulatory mechanisms and suggest measures for improvement.

In conclusion, corporate governance in the Indian banking sector represents a complex interplay of regulatory policies, ownership structures, and market forces. While significant progress has been made since liberalization, the journey towards achieving robust and uniform governance standards remains ongoing. A comprehensive understanding of these dynamics is essential for policymakers, regulators, and

stakeholders to ensure the stability, efficiency, and integrity of the banking system.

Corporate governance refers to the system of rules, practices, and processes by which a company is directed and controlled. In the banking sector, governance assumes critical importance due to the fiduciary role banks play in managing public deposits and maintaining financial stability.

The Indian banking sector underwent a paradigm shift after the **1991 economic liberalization reforms**, which introduced competition, deregulation, and private participation. These reforms necessitated stronger corporate governance mechanisms to ensure efficiency and prevent systemic risks.

Banks differ from other corporate entities due to their high leverage, complexity, and regulatory oversight, making governance more crucial.<sup>9</sup>

## 2. Evolution of Corporate Governance in Indian Banking

### 2.1 Pre-Liberalization Era

Before 1991, Indian banks were predominantly state-controlled, with limited emphasis on governance. Public sector banks (PSBs) dominated the sector, and decision-making was often influenced by political considerations.

### 2.2 Post-Liberalization Reforms

Post-1991 reforms led to:

- Entry of private sector banks
- Strengthening of regulatory frameworks
- Adoption of international standards such as Basel norms

The Reserve Bank of India (RBI) introduced several governance guidelines focusing on:

- Board independence
- Risk management
- Disclosure and transparency

These reforms significantly improved governance structures across the sector.<sup>10</sup>

## 3. Conceptual Framework of Corporate Governance in Banks

Corporate governance in banks is based on the following principles:

- Transparency
- Accountability
- Fairness
- Responsibility

Key components include:

- Board of Directors

<sup>5</sup> Sen, S., "Corporate Governance in Banking: Issues and Challenges," *Indian Journal of Corporate Governance*, 2019.

<sup>6</sup> Basel Committee on Banking Supervision, *Principles for Enhancing Corporate Governance*, 2015.

<sup>7</sup> Ministry of Finance, Government of India, *Banking Reforms Report*, 2020.

<sup>8</sup> RBI, *Financial Stability Report*, 2022.

<sup>9</sup> Agarwal, B.K., "Corporate Governance in Indian Banking Sector," *Journal of Allied Education*.

<sup>10</sup> Vibha Singh, "Analysis of Indian Public and Private Sector Banks," 2023.

- Audit Committees
- Risk Management Systems
- Disclosure Mechanisms

Effective governance ensures better financial performance and reduces risks such as non-performing assets (NPAs).

#### 4. Comparative Analysis: Public vs Private Sector Banks

##### 4.1 Ownership Structure

- **Public Sector Banks (PSBs):** Majority ownership by the Government of India
- **Private Sector Banks:** Owned by private shareholders and institutional investors

Ownership structure significantly influences governance practices. PSBs often face government interference, while private banks operate with greater autonomy.

##### 4.2 Board Composition and Independence

Private sector banks generally have:

- Higher proportion of independent directors
- Professional management

In contrast, PSBs often have:

- Government-appointed directors
- Limited autonomy in decision-making

This difference impacts efficiency and strategic decision-making.

##### 4.3 Transparency and Disclosure

Private banks tend to maintain higher transparency due to:

- Market pressure
- Investor expectations

PSBs, although regulated, sometimes lag in timely disclosures and accountability mechanisms.

##### 4.4 Risk Management Practices

Private sector banks:

- Use advanced risk assessment tools
- Focus on profitability and asset quality

Public sector banks:

- Historically faced higher NPAs
- Depend on government support during crises

##### 4.5 Financial Performance

Studies show that governance quality directly impacts performance indicators such as:

- Return on Assets (ROA)
- Return on Equity (ROE)
- Asset Quality

Comparative research indicates that private banks generally outperform PSBs in efficiency and profitability.<sup>11</sup>

#### 5. Role of RBI in Strengthening Corporate Governance

The Reserve Bank of India plays a crucial role in regulating governance practices through:

- Prudential norms
- Fit and proper criteria for directors
- Risk-based supervision

Recent initiatives include:

- Enhanced disclosure norms
- Governance audits
- Cybersecurity guidelines

RBI has continuously emphasized improving governance standards to prevent systemic risks and fraud.<sup>12</sup>

#### 6. Challenges in Corporate Governance

##### 6.1 In Public Sector Banks

- Political interference
- Bureaucratic decision-making
- Weak accountability mechanisms
- High NPAs

##### 6.2 In Private Sector Banks

- Excessive risk-taking
- Corporate frauds
- Leadership conflicts

Recent developments have shown that even private banks face governance challenges, especially related to internal management and oversight.

#### 7. Impact of Corporate Governance on Banking Performance

Corporate governance significantly affects:

- Profitability
- Asset quality
- Investor confidence

Empirical studies indicate a positive correlation between governance mechanisms and bank profitability, though results may vary depending on variables used.<sup>13</sup>

#### 8. Case-Based Insights

##### 8.1 Public Sector Banks

- Improved performance post-recapitalization
- Government-led reforms helped reduce NPAs

<sup>11</sup> Behura & Meher, "Comparative Analysis Using RBI Data," 2025.

<sup>12</sup> Kundu, S.T., "Corporate Governance in Indian Banks," 2019.

<sup>13</sup> Sandhya & Parashar, "Governance Practices in Banks," 2018.

## 8.2 Private Sector Banks

- Strong technological adoption
- Better customer service
- Higher efficiency levels

However, governance failures in some private banks highlight the need for stricter oversight.

## 9. Comparative Findings

Parameter	Public Sector Banks	Private Sector Banks
Ownership	Government-controlled	Privately owned
Autonomy	Limited	High
Efficiency	Moderate	High
Transparency	Moderate	High
Risk Management	Traditional	Advanced
Governance Quality	Improving	Relatively Strong

## 10. Recommendations

- Reducing Government Interference in PSBs
- Strengthening Board Independence
- Enhancing Disclosure Standards
- Adopting Advanced Risk Management Tools
- Uniform Governance Framework for all banks
- Capacity Building and Training for directors

## 11. Conclusion

Corporate governance remains a critical determinant of stability and efficiency in the Indian banking sector. While private sector banks demonstrate stronger governance due to market discipline and operational flexibility, public sector banks are gradually improving through regulatory reforms and recapitalization measures.

The post-liberalization era has significantly enhanced governance standards, but challenges persist. A balanced approach involving regulatory oversight, institutional reforms, and accountability mechanisms is essential to ensure sustainable growth and financial stability.