The relationship between the bank profitability and bank specific, industry specific and macroeconomic factors has important implications for a host of public policy questions. In current study, unbalanced panel data on 51 scheduled banks and 6 DFIs over a period of 2001 to 2013 has been used to provide novel estimates of bank profits and it influential factors. The empirical strategy exploits the relationship between the current profits with previous year profits to identify the dynamic characteristics of the model of bank profitability in addition to the bank specific, industry specific and macroeconomic estimates. The continuity in bank profits in Pakistan allows the current study to model the lagged profitability as determinants of bank profitability.

Further this study modeled the structure-conduct-performance hypothesis (SCP); it reflects the setting of prices that are less favorable to consumers (lower deposit rates, higher loan rates) in more concentrated markets as a result of competitive imperfections in these markets and lead supernormal profits. A related theory is also modeled by the current study, the relative-market-power hypothesis (RMP), which asserts that only firms with large market shares and well differentiated products are able to exercise market power in pricing these products and earn supernormal profits.

The results for current study has been obtained by us two-step generalized method of moments (GMM) technique, it deals well with the dynamic panel data sets. The results for the current study are significant and supported by the previous literature. In bank specific characteristics, lagged bank profitability, capital ratio and size found to have positive relationship with bank profits while management inefficiency and credit risk variable found to have negative and significant relationship with bank profits. In industry specific variables concentration ratio found positively associated with bank profitability.

In macroeconomic factors like inflation, GDP growth rate and market capitalization have positive while money supply growth rate found to have negative effects on bank profits.