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Financial performance of selected public sector bank with application of camel model: An analytical study

[1] Geetha N, [2] Dr. Thirumal R

[1] Ph.D, Research Scholar, CMS IMS, Coimbatore, Tamil Nadu, India
[2] Principal, CMS IMS, Coimbatore, Tamil Nadu, India

Abstract

The economic importance of banks to the developing countries may be viewed as promoting capital formation, encouraging innovation, monetization, influence economic activity and facilitator of monetary policy. Performance evaluation of the banking sector is an effective measure and indicator to check the soundness of economic activities of an economy. In the present study an attempt was made to evaluate the performance & financial soundness of select Public Sector Banks in India using CAMEL approach. Top three public sector banks based on return on net worth during 2013-2015 have taken for the study. It is found that in terms of Composite Capital Adequacy parameter SBH were at the top position, while SBBJ and Syndicate Bank got next rank. In terms of Asset Quality parameter, SBH held the top rank while Syndicate Bank held the lowest rank. Under Management efficiency parameter it was observed that top rank taken by Syndicate bank and lowest rank taken by SBBJ. In terms of Earning Quality parameter the capability of SBBJ got the top rank while Syndicate bank was at the lowest position. Under the Liquidity parameter SBBJ stood on the top position and Syndicate bank was on the lowest position. Syndicate bank needs to improve its position with regard to asset quality, earning quality, liquidity and capital adequacy, SBBJ should improve its management efficiency, capital adequacy and asset quality and SBH should improve its management efficiency, earning quality and liquidity.

Keywords: SBBJ, SBH, Public Sector Bank, CAMEL, Earning Quality Parameter

1. Introduction

Banking system in our economy has been allotted a crucial and noteworthy role in financing the planned economic growth. In the 1980s, CAMEL rating system was first introduced by U.S. supervisory authorities as a system of rating for on-site examinations of banking institutions. Under this system, each banking institution subject to on-site examination is evaluated on the basis of five critical dimensions relating to its operations and performance, which are referred to as the component factors. Top three public sector banks based on return on net worth during 2013-2015 have taken for the study. 1. State Bank of Hyderabad 2. State Bank of Bikaner and Jaipur and Syndicate bank Components like Capital, Asset Quality, Management, Earnings and Liquidity used to reflect the financial performance, financial condition, operating soundness and regulatory compliance of the banking institution. Each of the component factors is rated on a scale of 1 (best) to 3 (worst). A composite rating is assigned as an abridgement of the component ratings and is taken as the prime indicator of a bank's current financial condition. The composite rating ranges between 1 (best) and 3 (worst), and also involves a certain amount of subjectivity based on the overall assessment of the institution in view of the individual component assessments. The role and importance of banking sector and the monetary mechanism cannot be under-estimated in the development of a nation.

2. Literature Review

The financial performance of banks, both public and private, has been analysed by academicians, scholars and administrators using CAMEL model in the last decade. A summary of some of the studies is given below:

Kwan and Eisenbeis (1997) observed that Asset Quality is commonly used as a risk indicator for financial institutions, which also determines the reliability of capital ratios. Their study indicated that capitalization affects the operation of financial capitalization affects the operation of financial institution. More the capital, higher is the efficiency.

Saucier (2003) evaluated the liquidity, solvency and efficiency of Japanese Banks using CAMEL rating methodology. The study assessed the capital adequacy, assets and management quality, earnings ability and liquidity position Sarker (2005) in Bangladesh examined The CAMEL model for regulation and supervision of Islamic banks by the central bank.

This study enabled the regulators and supervisors to get a Shariah benchmark to supervise and inspect Islamic banks and Islamic financial institutions from an Islamic perspective.

Siva and Natarajan (2011) empirically tested the applicability of CAMEL norms and its consequential impact on the performance of SBI Groups. The study concluded that annual CAMEL scanning helps the commercial bank to diagnose its financial health and alert the bank to take preventive steps for its sustainability.

Chaudhry and Singh (2012) analyzed the impact of the financial reforms on the soundness of Indian Banking through its impact on the asset quality. The study identified the key players as risk management, NPA levels, effective cost management and financial inclusion.

3. Research Methodology

CAMEL is a ratio-based model to evaluate the performance of banks. It is an instrument to rate/rank the banks. The present study is a descriptive research study based on analytical research design. Out of Indian public sector banks has been selected for the purpose of present study. Top three public sector banks based on return on net worth during 2013-2015 have taken for the study. The data of the sample banks for a period of 2013-2015 have been collected from the published annual reports of the banks. Six financial ratios have been used to assess the performance of banks. Three year average has been calculated with the help of simple arithmetic mean.

3.1 Objective of the Study

The objectives of our study are:

1. To analyze the financial position and performance of the public sector banks using CAMEL model.
2. To offer suitable recommendations for improvement of performance and financial position of Public sector Banks authority.

3.2 Hypothesis of the Study

There is no significant difference in performance of SBH, SBBJ and Syndicate bank as assessed by CAMEL model.

4. Analysis and Discussion

4.1 Capital Adequacy

Capital adequacy has come forth as one of the prominent indicators of the financial health of a banking system. It is very useful for a bank to conserve & protect stakeholders' confidence and preventing the bank from being bankrupt. It reflects whether the bank has enough capital to bear unexpected losses arising in the future. Present study advance to total asset ratio and debt equity ratio is used as the indicator of capital adequacy.

4.1.1 Advance to Total Assets

This is a ratio indicates the relationship between the total advances and total assets. This ratio indicates a bank's aggressiveness in lending which ultimately produces better profitability. Higher ratio is preferred to a lower one. This ratio shows the proportion of advances in the bank with total assets. It is calculated by dividing the total advances by total assets.

Table 1: Advance to Total Assets

S. No	Name of the Bank	2013	2014	2015	Average	Rank
1	State Bank of Hyderabad	66.03	67.61	67.99	67.21	3
2	State Bank of Bikaner and Jaipur	66.78	70.48	67.85	68.37	1
3	Syndicate Bank	68.60	69.05	66.87	68.17	2

Source: Secondary data

It is found that SBBJ ranked on the top position with highest of 68.37 followed by Syndicate Bank (68.17) and SBH (67.21).

4.1.2 Debt-Equity Ratio

This ratio represents the degree of leverage of a bank. It shows how much proportion of the bank business is financed through equity and how much through debt. It is calculated by dividing total borrowings with shareholders' net worth. Higher ratio is an indication of less protection for the depositors and creditors and vice-versa.

Table 2: Debt-Equity Ratio

S. No	Name of the Bank	2013	2014	2015	Average	Rank
1	State Bank of Hyderabad	13.4	13.4	12.7	13.17	1
2	State Bank of Bikaner and Jaipur	14.2	13.2	13.5	13.63	2
3	Syndicate Bank	15.8	17.1	19.3	17.4	3

Source: secondary data

In above table, SBH is on the top position with least average of 13.17 followed by SBBJ (13.63) and Syndicate bank (17.4).

4.1.3 Composite Capital Adequacy

On the basis of group averages of two ratios of capital adequacy is expressed in table 3 i.e composite capital adequacy on Advances to Assets and Debt-Equity ratios.

Table 3: Composite capital adequacy on Advances to Assets and Debt-Equity ratios

S. No	Name of the Bank	Advances to Total Assets		Debt Equity Ratio		Group Rank	
		%	Rank	%	Rank	Average	Rank
1	State Bank of Hyderabad	67.21	3	13.17	1	2	1
2	State Bank of Bikaner and Jaipur	68.37	1	13.63	2	1.5	3
3	Syndicate Bank	68.17	2	17.4	3	2.5	2

Source: secondary data

4.2 Assets Quality

The quality of assets is an important parameter to examine the degree of financial strength. The foremost objective to measure the assets quality is to ascertain the return on advances.

4.2.1 Return on advances

The ratio represents the proportion of return on advances. Higher ratio shows higher asset quality.

Table 4: Return on advances

S.No	Name of the Bank	2013	2014	2015	Average	Rank
1	State Bank of Hyderabad	1.39	1.07	1.25	1.24	1
2	State Bank of Bikaner and Jaipur	1.27	1.14	1.12	1.18	2
3	Syndicate Bank	1.36	0.98	0.75	1.03	3

Source: secondary data

In above table, SBH is on the top position with highest average of 1.24 followed by SBBJ (1.18) and Syndicate bank (1.03).

4.3 Management Efficiency

Management efficiency is another essential component of the CAMEL model that guarantee the growth and survival of a bank. Management efficiency means adherence with set norms, ability to plan and respond to changing environment, leadership and administrative capability of the bank.

4.3.1 Return on Net worth

The ratio represents the proportion of return on total resources. Higher ratio shows higher profitability.

Table 5: Return on Net worth

S. No	Name of the Bank	2013	2014	2015	Average	Rank
1	State Bank of Hyderabad	17.7	12.74	14.66	15.03	2
2	State Bank of Bikaner and Jaipur	16.36	14.46	13.67	14.83	3
3	Syndicate Bank	22.78	16.73	13.22	17.58	1

Source: secondary data

In above table, Syndicate bank is on the top position with highest average of 17.58 followed by SBH (15.03) and SBBJ (14.83).

4.4 Earning Quality

The quality of earnings is a very important criterion which represents the quality of a bank's profitability and its capability to maintain quality and earn consistently. It primarily determines the profitability of bank and explains its sustainability and growth of future earnings.

4.4.1 Operating Profit to Total Assets

This ratio reflects how much a bank can earn profit from its operations for every rupee invested in its total asset. In this ratio operating profit are expressed as percentage of total assets.

Table 6: Operating Profit to Total Assets

S. No	Name of the Bank	2013	2014	2015	Average	Rank
1	State Bank of Hyderabad	-.69	-1.28	-3.30	-1.76	2
2	State Bank of Bikaner and Jaipur	-1.68	-0.87	-1.17	-1.24	1
3	Syndicate Bank	-2.42	-2.20	-2.17	-2.26	3

Source: secondary data

In above table SBBJ is on the top position with highest average followed by SBH and Syndicate Bank.

4.5 Liquidity

Risk of liquidity can have an effect on the image of bank. Liquidity is a crucial aspect which reflects bank's ability to meet its financial obligations. An adequate liquidity position means a situation, where organization can obtain sufficient liquid funds, either by increasing liabilities or by converting its assets quickly into cash. Cash deposit ratio has consider to calculate the liquidity of the firm.

4.5.1 Cash Deposit Ratio

The ratio shows the proportion of cash in hand and the total deposit. Higher cash in and show the higher liquidity.

Table 7: Cash Deposit Ratio

S. No	Name of the Bank	2013	2014	2015	Average	Rank
1	State Bank of Hyderabad	5.71	5.59	4.98	5.43	2
2	State Bank of Bikaner and Jaipur	7.85	8.84	9.19	8.63	1
3	Syndicate Bank	4.92	5.23	5.28	5.14	3

Source: secondary data

In above table, SBBJ is on the top position with highest average of 8.63 followed by SBH (5.43) and Syndicate bank (5.14).

4.6 Major findings of the study

- SBBJ ranked on the top position with highest of 68.37 followed by Syndicate Bank (68.17) and SBH (67.21).
- SBH is on the top position with least average of 13.17 followed by SBBJ (13.63) and Syndicate bank (17.4).
- SBH is on the top position with highest average of 1.24 followed by SBBJ (1.18) and Syndicate bank (1.03).
- Syndicat bank is on the top position with highest average of 17.58 followed by SBH (15.03) and SBBJ (14.83).
- SBBJ is on the top position with highest average

followed by SBH and Syndicate Bank.
- SBBJ is on the top position with highest average of 8.63 followed by SBH (5.43) and Syndicate bank (5.14).

4.7 Recommendation of the study

The researchers has recommended the following point through CAMEL Approach. They are as follows.

1. SBH should improve its management efficiency, earning quality and liquidity.
2. SBBJ should improve its management efficiency, capital adequacy and asset quality.
3. Syndicate bank needs to improve its position with regard to asset quality, earning quality, liquidity and capital adequacy,

5. Conclusion of the study

During the process of evaluation of performance of public sector banks our study highlighted that, the different banks have obtained different ranks with respect to CAMEL ratios. The present study also depicted that though ranking of ratios is different for different banks. But there is no statistically significant difference between the CAMEL ratios. It signifies that the overall performance of bank is same; this may be because of adoption of modern technology, banking reforms and recovery mechanism. The present study is limited in scope as it relates to three public sector banks only.

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