



Analysis on Performance evaluation of Kotak Bank and State Bank of India using CAMELS Model with Reference to Capital Adequacy Ratios

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ABSTRACT:

CAMELS model is an important tool in assessing the performance of financial institutions mainly Banks. This approach was adopted by RBI in the year 1996 following the recommendations of Padmanabham working committee (1995). This method evaluates parameters like Capital Adequacy ratio, Asset Quality, Management Efficiency, Earnings, Liquidity, and Sensitivity. In this study we have selected one commercial bank and one government Bank and evaluated using CAMELS model. The banks were ranked based on their score. The banks under the study are Kotak Mahindra Bank and State Bank of India. The present analysis primarily focuses on capital adequacy ratios to estimate the performance of banks during last 5 financial years.

Keywords: CAMELS, performance, financial institution, banks, committee, method, liquidity and sensitivity.

1. Introduction

With the liberalization and Economic reforms during early 1990's, there were many private players who entered banking business. These economic reforms aimed at improving competition, productivity, efficiency among the banks and also to make them follow international accounting standards. Since then the banking industry remained the backbone of economy as it pools all the small savings from individuals and pumps it into the capital market thus contributing the development of economy.

Indian government's Scheme Pradhan Mantri Jan Dhan Yojana (PMJDY) aimed at making every Indian citizen own a bank account. Recently RBI has even allowed for establishing Payments Banks by framing new guidelines to monitor them. So, it is very important to evaluate the banks every quarter to know how well they are utilizing the governments schemes, and market opportunities and also their performance. So, a method to assess the banks performance was developed by USA, by the name CAMELS which is a 6-Dimensional approach. In this approach the bank is given ratings on a scale of 1 to 5 where 1 being good and 5 being poor.

2. Literature Review

Dr. Srinivasan (2016), have evaluated a total of 41 banks in India using CAMEL model and found the strategically significant difference in scores among private, public and foreign banks. He used the evaluation to rank them and allow for improvement by covering or working on their weaknesses.

Karthik (2017), has evaluated 3 Indian Banks (ICICI, HDFC, and AXIS) for the period of 5 years 2012 to 2016 and ranked them along with pointing the risks that might lead them to failure. They found that HDFC bank was having highest operating ratios, and axis bank has the least in every parameter.

Vijay and Shiram (2017), have evaluated 11 commercial banks for a period from 2012 to 2016 and found that Kotak bank and HDFC bank are top 2 commercial banks in India. Their study also evaluated their financial position and soundness. They found that private sector banks have clearly outperformed public sector banks in every parameter of CAMEL model.

Wirnkar and Tanko (2008), Suggested the model to be renamed to CLEAM to reflect the weightage of importance of each factor. Suggested the best Capital adequacy ratio is the ratio of shareholders' funds to total risk weighted assets. They also suggested that the best liquidity ratio is the ratio of demand liabilities to total deposits. They also suggested that other than CAMELS model, more research need to be done before judging a bank on its performance.

3. Objective of study

1. To Evaluate the performance of Kotak Mahindra and SBI banks in India.
2. To use the statistical methods, CAMELS Model, and Secondary data.

3. To give recommendation based on their Ratings.

4. Components of CAMEL Model

Table. No. 1 Detailed Description of CAMELS model Components.

Parameter	Ratios	Formulae	Significance	Evaluation Criteria
Capital Adequacy	Capital Risk Adequacy Ratio	(Tier-I + Tier-II)/RWA	It measures the ability of a bank to absorb its losses from its risk assets.	Higher the better
	Debt/Equity Ratio	Total Outside Liabilities/ total assets	It indicates the banks financial leverage	Lower the better
	Coverage Ratio	Total Advance/Total Assets	It indicates the capital availability to meet the loss assets in NPA's	Higher the better
Asset Quality	Net NPA/Net Advance ratio	NPA/Net advance	It indicates the level of NPA in net advance	Lower the better
	Govt. Securities/ investment ratio	Government Securities / Total Investments	It indicates the banks risk appetite in investments.	Higher the better
	Gross NPA/ Net Advances	Gross NPA/ Net Advance	It reflects the quality of advances made by the bank.	Lower the better
Management Efficiency	Total advances / Total Deposit Ratio	Total Advance / Total Deposit	It indicates the banks ability to convert its deposits into higher earning advances	Higher the better
	Asset Turnover ratio	Total Income/ Total Assets	It measures the banks efficiency in using its assets to generate income.	Higher the better
	Business per employee ratio	Total Income/ number of employees.	It measures the banks employee strength.	Higher the better
Earning Ability	Return on Asset	Net Profit after tax / Total Assets	It indicates the returns earned on the assets used.	Higher the better
	Return on Equity	Net income / Avg. Shareholders Equity	It measures the earnings of the shareholders from their investment	Higher the better
	Cost to income ratio	Operating expenses / Net income	It measures the banks ability to meet its operating expenses from the income	Lower the better
Liquidity	Cash Assets / Total Assets Ratio	Cash Assets / Total Assets	It measures the cash as a proportion on total assets.	Higher the better
	Liquid assets / Total deposit ratio	Liquid assets/ total deposits	It indicates the bank's ability to meet its deposit obligations.	Higher the better
	Cash to deposit ratio	Total cash / total Deposit	It measures the availability of cash.	Lower the better.
Sensitivity	Demand deposits / deposits	Demand deposits / deposits	It shows the obligations of the bank.	Lower the better

5. Data Analysis and Interpretation

The data is collected for select two banks of last five financial years and estimated the capital adequacy ratios and compare the performance of two banks based on capital adequacy ratios.

Table-2: Analysis on Capital Adequacy Ratios

	Kotak Bank						SBI					
	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	Average	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	Average
CRAR (%)	18.83	17.17	16.34	16.77	18.22	17.47	12.96	12	13.12	13.11	12.6	12.76

Debt Equity Ratio	4.5	4.7	5.4	5.3	4.9	4.96	14	14.2	14.5	13.5	13.4	13.92
Coverage Ratio	0.6	0.62	0.62	0.63	0.64	0.62	0.68	0.63	0.65	0.58	0.56	0.62

After comparing the last five year's data, both the banks have decent capital risk asset ratio. Kotak bank has a little higher CRAR ratio compared to SBI, but the amount of tier I and tier II assets are higher in SBI being a largest government bank in India but risk assets are also higher. The volumes of Tier I and Tier II are higher in SBI than Kotak Bank but the ratios of Kotak Bank are Dominating those of SBI. So, it is found that both the banks will be able to absorb losses without disturbing the trading operation as well as meeting their liquidation requirements. Both the banks are safer for deposits. The ratios of Kotak Bank are found to have a higher deviation when compared to that of SBI's.

The debt equity ratio is considerably low for Kotak Mahindra Bank, and particularly when compared to SBI, the Debt Equity Ratio of SBI is dangerously High, SBI is aggressively focusing on growth through its risk linked debt assets. But again, the concept of high risk, high rewards apply. Since the assets are managed by debt, the earnings will be high, the bank can pay less taxes, and need not distribute any extra dividends. On the other hand, Kotak Bank is playing safer game with low risk but due to its efforts and it is still earning decent earnings even after paying more taxes and distributing dividends.

In terms of advances to assets, Both the banks are more or less performing uniquely. But in a closer look Kotak Bank is on steady inclination and growth. While SBI is not maintaining a stable ratio. The advance to asset ratio also proves the aggressiveness of a bank in lending. If an average of last five year's data is collected and calculated, then both the banks have same average of 0.62.

6. Conclusion

CAMELS model is a very useful too in evaluating the banks performance. It helped us identify the banks weakness and areas of improvement. From the study Kotak bank is found to be highly efficient in maintaining capital adequacy, the quality of assets is also good, management efficiency is also good but should work on business per employee. The earnings are also high in Kotak bank. So, to conclude, Kotak bank has performed well as of now. While SBI is avoiding all risk and playing it safe with all other ratios being maintaining at moderate levels.

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