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Financial Performance of AU Small Finance Bank by using CAMEL Model

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ABSTRACT:

This research analyzes the financial performance of AU Small Finance Bank through the CAMEL model, which is a commonly accepted measure of banking institution performance. The study seeks to evaluate the bank's stability, efficiency, and health through five primary parameters: Capital Adequacy, Asset Quality, Management Efficiency, Earnings, and Liquidity. The research is grounded on secondary data gathered from the Reserve Bank of India (RBI) website, annual reports, and other financial sources. Statistical methods like the ANOVA test and ratio analysis are used to analyze financial trends over a five-year horizon (2019-20 to 2023-24). The results give insights into AU Small Finance Bank's competitive standing in the financial sector, pointing out strengths and weaknesses. The study adds to knowledge on the dynamics of performance by small finance banks in India as well as how they contribute towards financial inclusion and economic growth.

Key words: Financial Performance, AU Small Finance Bank, CAMEL Model, Capital Adequacy, Asset Quality, Management Efficiency, Earnings, Liquidity, Small Finance Banks (SFBs), Digital Transformation, Operational Efficiency, Risk Management, Non-Performing Assets (NPA), Microfinance, Financial Inclusion, Regulatory Compliance, Profitability Ratios, Return on Assets (ROA), Return on Equity (ROE), Credit Risk Management, Banking Sector Analysis, Retail Deposits, Cost-to-Income Ratio, Cybersecurity in Banking

Introduction

Financial performance is one of the critical factors for measuring an organization's overall health, and sometimes success, by giving insight into whether or not it can create profits, use its resources efficiently, and continue over time. It encompasses various financial metrics and indicators, including revenue, net income, profitability ratios, return on investment (ROI), and cash flow. These reveal how well a company is performing in meeting the expectations from its financial goals. Financial performance evaluation involves review of income statements, balance sheet, and cash flow statements about the operational efficiency, financial stability, and growth potential of a given company. Gross margin, operating margin, and EPS are some significant KPIs disclosing comprehensive views of profitability and cost management. Typically, strong financial performance indicates effective management practices, a competitive position in the market, and an ability to respond to changes in the market. On the other hand, poor performance may reflect underlying problems requiring strategic intervention. This analysis will be helpful to investors, creditors, and management in making appropriate investment decisions, lending decisions, and strategic planning to ensure long-term viability and success.

The CAMEL model is a widely recognized framework for assessing the financial health and performance of banks and other financial institutions. CAMEL stands for Capital Adequacy, Asset Quality, Management Quality, Earnings, and Liquidity. Each of the parameters represents one critical aspect of the operations of a financial institution. The CAMEL model is widely applied by central banks and other financial supervisory authorities to measure the stability, efficiency, and soundness of financial institutions. In this model, five factors are evaluated: these factors include capital, asset quality, management, earnings, and liquidity. The model allows regulators to analyze these components for potential risks and ensure that financial institutions keep up with healthy practices to safeguard their solvency and operational effectiveness.

Scope of the study

The scope of study on the financial performance of AU Small Finance Bank using the CAMEL model focuses on evaluating the bank's performance across five key areas: Capital Adequacy, Asset Quality, Management Quality, Earnings, and Liquidity. The study will begin by analyzing the bank's Capital Adequacy to determine if it maintains sufficient capital reserves to meet regulatory requirements and absorb potential losses.

Objectives of the study

- To analyze the capital adequacy and asset quality of AU Small Finance Bank in India.
- To analyze the management efficiency and earning capacity of AU Small Finance Bank.
- To analyze the liquidity position of AU Small Finance Bank.

Research Methodology

Sample method

The study employs a purposive sampling method to select AU Small Finance Bank. This method is chosen because the focus is on an in-depth analysis of a single financial institution, which is representative of small finance banks in India. The bank's publicly available financial data over a specified period is utilized to conduct the study.

Types of data

The data collection is very important task. The present study is based on secondary data. The data for sample banks has been collected from the RBI Website and annual reports of AU Small Finance bank. To supplement the data, banking Journals, Publications, IBA Bulletin, Periodicals, various books, RBI Publication etc. have also been used. Data has also been searched out from the various related websites also. Moreover, the newspapers, accounting literature and surveys have also been referred.

Statistical tools used

In order to analyze the data collected, several statistical tools and techniques were employed. The statistical tool used for the analysis is camel model and anova test.

Literature Reviews

1. Pandya Deep Navanit Kumar, Dr. Jay G. Dave (2024)

The Indian economy's growth depends heavily on the banking sector. In recent years, the banking business has undergone numerous changes. The RBI launched small finance banks as a banking initiative to encourage financial inclusion in India. Small finance banks offer services to financially excluded populations like farmers, labourers' low-income people, etc. This study is related to the period of six years from 2016-17 to 2021-22. The study uses descriptive statistics and the CAMEL model for the evaluation of financial performance. Descriptive statistics are analysed with the help of standard deviation and ANOVA.

2. Kantharaju G., Dr. Shubha A., & Naresh Babu K S. (2024)

The CAMELS model is one of the highly effective tools in measuring banking performance and future risks. It focuses on key indicators such as capital adequacy, asset quality, management, earnings, liquidity, and sensitivity. The performance of Indian private and public sector banks between 2011-12 to 2020-21 are being compared in this study. This analysis includes two private banks (Kotak Mahindra and ICICI) and two public banks (SBI and Canara). Results indicate that Kotak Mahindra took the top ranking, followed by ICICI, SBI, and Canara and no huge performance gap between public and private banks.

Data & Interpretation

1. Capital Adequacy Test(C):

Capital Adequacy Ratio (CAR):

Year	Tier 1 Capital (In lakhs)	Tier 2 Capital (In lakhs)	Risk Weighted Assets (In lakhs)	CAR (in %)
2019-2020	4,13,227.02	81,765.60	22,50,988.40	21.99
2020-2021	6,02,436.15	51,351.95	27,97,282.02	23.37
2021-2022	7,17,170.24	47,238.41	36,41,668.89	20.99
2022-2023	10,56,890.92	87,861.68	48,51,930.08	23.59
2023-2024	11,97,237.02	80,080.48	63,68,483.10	20.05

(Source: Annual Report of AU Small Finance Bank)

As per the latest RBI norms, the small finance banks in India should have a capital adequacy ratio of 15%. Higher the capital adequacy ratio stronger is considered a bank, as it ensures high safety against bankrupt. The above table shows a financial institution's Capital Adequacy Ratio (CAR) for five years, Tier 1 and Tier 2 capital, and risk-weighted assets (RWA). CAR, an important indicator of financial soundness, varies as the capital and exposure to risk of the institution change. The peak CAR of 23.59% in 2022-23 reflects good capital reserves, and the lowest of 20.05% in 2023-24 reflects high risk-weighted assets. Overall, the bank has a healthy CAR in excess of regulatory limits.

2. Asset Quality Test (A):

Gross NPA to Net Advance Ratio:

Year	Gross NPA (In Lakhs)	Net Advance (In Lakhs)	Gross NPA to Net Advance Ratio (in %)
2019-2020	45,778.37	26,99,241.54	1.70
2020-2021	1,50,282.91	34,60,891.42	4.34
2021-2022	92,437.82	46,09,525.64	2.01
2022-2023	98,131.26	58,42,154.41	1.68
2023-2024	1,23,740.04	73,16,265.47	1.69

(Source: Annual Report of AU Small Finance Bank)

The above table gives the Gross Non-Performing Assets (NPA) and Net Advances of AU Small Finance Bank for 2019-2020 to 2023-2024 and the Gross NPA to Net Advance ratio. A lower ratio means higher advance quality. The ratio was 1.70% in 2019-2020 but jumped drastically to 4.34% in 2020-2021 with a steep increase in Gross NPAs. But in the following years, the institution bettered the asset quality, lowering the ratio to 2.01% during 2021-2022 and further bringing it to the range of 1.68%-1.69% in 2022-2023 and 2023-2024, even with a rise in Gross NPAs. This reflects good credit management and enhanced recovery efforts, with a good asset quality.

3. Management Efficiency Test (M):

Profit Per Employee Ratio:

Year	Net Profit (in crores)	No. of Employees	Profit Per Employee Ratio
2019-2020	674.78	17,112	0.04
2020-2021	1,170.68	22,484	0.05
2021-2022	1,129.83	27,817	0.04
2022-2023	1,427.93	28,320	0.05
2023-2024	1,534.72	29,738	0.05

(Source: Annual Report of AU Small Finance Bank)

The above table provides the Net Profit, Number of Employees, and Profit Per Employee Ratio for a company over five years of finance (2019-2024). The Net Profit has improved continuously from ₹674.78 crores in 2019-2020 to ₹1,534.72 crores in 2023-2024, portraying business growth. The Number of Employees has also increased considerably from 17,112 to 29,738, showing expansion. The Profit Per Employee Ratio has also been fairly consistent at 0.04 to 0.05, which indicates that even though the manpower has increased, profitability and efficiency per employee have been kept at a steady rate. This shows balanced growth and effective use of resources.

4. Earning Quality Test (Q):

Interest Income to Total Income Ratio:

Year	Interest Income (In Crores)	Total Income (In Crores)	Interest Income to Total Income Ratio (in %)
2019-2020	4,285.88	4,991.98	85.86
2020-2021	4,950.05	6,370.98	77.70
2021-2022	5,921.73	6,915.43	85.63
2022-2023	8,205.41	9,239.87	88.80
2023-2024	10,554.71	12,300.61	85.81

(Source: Annual Report of AU Small Finance Bank)

The Interest Income to Total Income Ratio for five years (2019-2024) is provided in the table, which shows the ratio of income earned due to lending operations. Interest income has seen a uniform rise from ₹4,285.88 crores for the year 2019-20 to ₹10,554.71 crores for 2023-24, which shows business expansion. Correspondingly, total income has also increased considerably, registering at ₹12,300.61 crores for the year 2023-24. The ratio varies, reaching a high of 88.80% in 2022-23 shows more income from lending activities. A stable high ratio (over 77%) reflects that revenue to a large extent is generated from interest-based income, reflecting effective management of loans and profitability of core banking business.

5. Liquidity Management Test (L):

Liquid Assets to Total Assets Ratio:

Year	Liquid Assets (in crores)	Total Assets (in crores)	Liquid Assets to Total Assets Ratio (in %)
2019-2020	11,005	42,143	26.11
2020-2021	11,294	51,591	21.89
2021-2022	15,899	69,078	23.02
2022-2023	21,015	90,216	23.29
2023-2024	27,771	1,09,426	25.38

(Source: Annual Report of AU Small Finance Bank)

The above table shows the Liquid Assets to Total Assets ratio for five successive financial years with special focus on its impact on financial solidity. Even though there is a rising trend in liquid assets from ₹11,005 crores in 2019-20 to ₹27,771 crores in 2023-24, the total assets have increased at an even greater level, decreasing the ratio of liquid assets. The low Liquid Asset to Total Assets ratio is risky because it restricts a company from fulfilling short-term obligations. Yet, the Return on Assets (ROA) varies, reflecting efficiency in asset utilization. Even though the greater total assets are responsible for the expansion of a business, liquidity is required in order to avoid financial risk.

Conclusions

1. Evolution of Small Finance Banks in India

The research brings to the fore the remarkable development of Small Finance Banks (SFBs) in India, with an emphasis on financial inclusion and catering to underbanked populations. Support from the RBI in terms of regulation has been instrumental in their growth, enabling them to service small enterprises, farmers, and low-income groups efficiently.

2. Digital Transformation of AU Small Finance Bank

AU Small Finance Bank has significantly progressed in digital transformation, introducing programs like AU 0101 mobile banking, digital payment offerings, and AI-based financial services. These have enhanced customer accessibility, operational efficiency, and competitive standing in the banking industry.

3. Capital Adequacy and Asset Quality

The bank has been able to sustain a solid capital foundation, guaranteeing financial stability and regulatory compliance. The decline in Net Non-Performing Assets (NPAs) over time indicates better asset quality and risk management practices. The implementation of rigorous borrower screening and diversified lending practices has added to its healthy financial condition.

4. Management Efficiency and Earnings Capacity

AU Small Finance Bank has exemplified strong management efficiency by way of strategic decision-making, cost effectiveness, and productivity by the employees. Profit per employee has not fluctuated with the expansion of the workforce and the bank has kept a competitive cost-to-income ratio, supporting steady profitability.

5. Liquidity Position

The bank has been in a stable liquidity position with a solid retail deposit base. The liquid assets to total deposits ratio have been well managed to ensure the capacity to cover short-term obligations. In spite of volatility, the bank's liquidity management policies have helped ensure financial resilience.

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