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## AN ANALYSIS OF THE PERFORMANCE OF SELECT FOREIGN BANKS USING CAMEL APPROACH

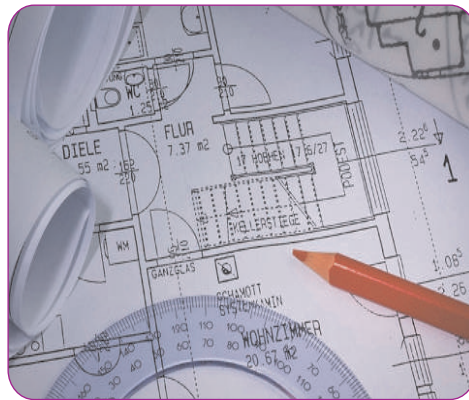
Aakash Kumar<sup>1</sup> and Dr. G. Vasanthi<sup>2</sup>

<sup>1</sup>Research Scholar, Department of Commerce, Annamalai University.

<sup>2</sup>Professor, Department of Commerce, Annamalai University.

### ABSTRACT: -

It is a truth that banks play a crucial role to the overall economic activities of any country. No economy can survive without the sound banking system. The history of banking is not very old, but yes, before some precious inventions. Today we cannot imagine the world without banks.



If we talk about Indian Banking system then it is fastest growing sector. Modern banking sector is becoming more complex than before. Evaluating Indian Banking system is a challenging task. There are so many factors while differentiating banks. Sound financial health of a bank is the guarantee not only to its

depositors but is equally significant for the many concerned of the banks. Hence time to time efforts and initiatives have been taken to measure the financial position of the banks. In this paper two major foreign banks have been taken i.e. Hong Cong and Shanghai Bank (HSBC), Standard Chartered Bank. Evaluation has been done by using CAMELS parameters, the latest model of financial analysis. Through this model, it is highlighted that the position of the banks under the study is sound and satisfactory so far their Capital Adequacy, Assets Quality, Management Capability, Earning, Liquidity and Sensitivity is concerned.

**KEYWORDS:** Capital Adequacy, Assets Quality, Management Capability, Sensitivity, Foreign Banks, Liquidity Analysis.

### INTRODUCTION :

Banking sector of India has a long history when the East India Company set up a Bank of Hindustan in 1770 followed by the General Bank of India in 1786. After that number of public sector banks was set up such as Bank of Bengal, Bank of Bombay, and bank of madras came into existence between 1800 and 1850.

After 1850's the British initiated the process of setting up foreign banks in India and it was followed by banks from countries viz. France, Germany, Japan, Holland and U.S. some of the oldest foreign banks that entered India were HSBC (then called the Mercantile Bank of India which started in 1853), and Standard Chartered Bank (then called the Chartered Bank of India which started in 1858).

At present the Standard Chartered Bank is the largest foreign bank in term of numbers, with 102 branches in 44 cities as per the RBI report on September 30, 2015. There were 46 foreign banks operating in India with 325 branches in all over India. As per the RBI guidelines foreign banks can operate in India by the set up of their branches through wholly owned subsidiary or through their representative offices.

The money market has been playing a predominant role in allocating resources in institutions in need of capital for productive & operational activities and contributing considerably to the economic development of the economy and growth. Implementation of the New Economic Policy in 1991, transformed the subdued Indian

money market into a vibrant one with increased efficiency and reduced risk and cost. After that India is fast becoming an investment destination for foreign banks.

### OPERATIONS OF FOREIGN BANKS IN INDIA

Foreign Banks were allowed to operate in India either through branches or their representative office. To obtain license for a new branch in our country a foreign bank has to function in accordance with all financial requirements and norms applicable to Indian commercial banks. Reserve Bank will grant permission to a foreign bank only after ascertaining the soundness of the bank, international and home country rating, international presence and economical and political relation between the two countries etc. Foreign Bank should be under the consolidated supervision of the home country regulation.

It has been stipulated that the minimum capital requirement for a foreign bank should be US\$25 million spread over 3 branches i.e. US\$ 10 million each for the first branch and the second branch and US\$5 million for the third branch. Additional branch will be permitted only after monitoring the performance of existing branches of the bank, their financial results, inspection findings etc. the number of licenses are fixed in conformity with India's commitment made to World Trade Organization, which is presently 12 licenses per year excluding off-site ATMs which also require licenses.

The government of India raised foreign direct investment in banking companies from 49% to 75% in the budget of 2003-04. It was aimed at facilitating the setting up of subsidiaries by foreign banks and for attracting investment in private sector banks. Accordingly the reserve bank proposed to the government of India to lift the limit on voting rights. Even though comprehensive amendments in Banking Regulation Act, 1949 suggest a immediate measures to facilitate investment.

With the liberalization of Foreign Direct Investment regime in Banking Sector was brought under the automatic route. According to the government of India announcement of May 21, 2001 FDI up to 49% from all sources was permitted in private sector banks under the automatic route, provided it is in true with the guidelines issued by the Reserve Bank of India from time to time.

### OBJECTIVES OF THE STUDY

**The main objectives of the study are as follows:**

- (I) To analyze the financial performance of the banks under study.
- (II) To undertake the factors which have led to the current financial performance; and
- (III) To suggest measures on the basis of the study results to improve further the financial performance of the banks under study.

### METHODOLOGY OF THE STUDY

Present study is based on the secondary source of information which has been collected from the official website of Reserve Bank of India, different journals and the sites of concerned banks. For the purpose of the study, the research instrument used is the CAMELS Model which is the recent innovation in the area of financial performance evaluation of banks; this model is explained as under:

### CAMELS PARAMETERS

The CELS ratings or Camels rating is a supervisory rating system originally developed in the U.S. to classify a bank's overall condition. It's applied to every bank and credit union in the U.S. (approximately 8,000 institutions) and is also implemented outside the U.S. by various banking supervisory regulators. The ratings are assigned based on a ratio analysis of the financial statements.

**The components of a bank's condition that are assessed:**

- (C)apital adequacy
- (A)ssets
- (M)anagement Capability

- (E)arnings
- (L)iquidity (also called asset liability management)
- (S)ensitivity (sensitivity to market risk, especially interest rate risk)

### SAMPLES OF THE STUDY

The present study seeks to evaluate the financial performance of two oldest foreign banks (i.e. Hong Cong and Shanghai bank, HSBC & Standard Chartered Bank). These two banks are purposely selected for the study, keeping in view their role and involvement in shaping the business conditions, specifically in terms of advances, deposits, manpower employment and branch network etc.

### DATA AND TOOLS

The present study is mainly based on secondary data drawn from the annual reports of the respective banks. These data are related to 5 years (2010-2015). For analysing of the data, two important statistical tools viz. Mean and Standard Deviation has been uses to arrive at conclusions in a scientific way.

**The results and discussions of the study are described under the following heads:**

- + Capital Adequacy Analysis
- + Assets Quality Analysis
- + Management Capability Analysis
- + Earning Analysis
- + Liquidity Analysis

### Analysis of Components of CAMEL Framework

#### (a)CAPITAL ADEQUACY

Capital base of financial institutions facilitate depositors in forming their risk perception about the organization. Also, it is a significant structure for financial managers to maintain adequate levels of capitalization. Capital adequacy is very useful for banks to conserve and protect stakeholder's confidence and prevent the bank from bankruptcy. Reserve Bank of India prescribes banks to maintain a minimum capital to risk-weighted Assets Ratio (CRAR) of 9% with regard to credit risk, market risk and operational risk on an ongoing basis, as for the study.

**The following ratios have been used to measure capital adequacy:**

- Capital Adequacy Ratio
  - Debt Equity Ratio
  - Government Securities to Total Investment
  - Advances to Assets Ratio
- Capital Adequacy Ratios of Hong Cong and Shanghai Banking Corporation (HSBC)

**Table 1.1**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Capital Adequacy Ratio	18.03	16.04	17.10	17.36	14.84	16.67	1.250
Debt Equity Ratio	4.32	4.80	4.90	5.84	5.92	5.16	0.696
Govt. Securities to Total Investment	0.55	0.52	0.61	0.82	0.84	0.67	0.151
Advances to Assets	0.30	0.33	0.30	0.34	0.30	0.31	0.019

- Capital Adequacy Ratios of Standard Chartered Bank

**Table 1.2**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Capital Adequacy Ratio	13.41	11.43	13.43	12.88	12.85	12.8	0.814
Debt Equity Ratio	5.30	5.41	4.18	4.28	3.29	4.49	0.877
Govt. Securities to Total Investment	0.87	0.81	0.89	0.88	0.85	0.86	0.031
Advances to Assets	0.46	0.46	0.52	0.52	0.52	0.49	0.032

The position of capital adequacy of HSBC and SCB has been measured with the help of Capital Adequacy Ratio, Debt Equity Ratio, Government Securities Ratio and Advance to Assets Ratio. Introspection in Table 1.1 and Table 1.2 reveal that the Capital Adequacy Ratio HSBC bank is good, the average of CAR of this bank is 16.67 which is good indicator, on the other hand the CAR of SCB is comparatively less than HSBC, it is 12.8 although it is satisfactory. Debt Equity Ratio of SCB is comparatively better than HSBC it is 4.49. The ratio of Government Securities is increasing in HSBC bank while it is moderated in SCB. The condition of Advances to Assets is better in HSBC as it shows the average of 0.31 as compare to 0.49 in SCB bank.

**b) ASSETS QUALITY**

Assets quality determines the healthiness of financial institutions against loss of value in the assets as assets impairment risks the solvency of the financial institutions. The weakening value of assets has a spillover effect, as losses are eventually expose the earning capacity of the institution. With this framework, assets quality is assessed with respect to the level and severity of non-performing assets, adequacy of provisions, distribution of assets etc.

**For the study, the following ratios have been used to measure asset quality:**

- (i) Net NPA to NET Advance (%)
- (ii) Net NPA to Total Assets (%)
- (iii) Total Investment to Total Assets
- (iv) Standard Advances to Total Advances

- Assets Quality Ratios of Hong Cong and Shanghai Banking Corporation (HSBC)

**Table 1.3**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Net NPA to Net Advance (%)	0.91	0.62	0.33	0.27	0.51	0.53	0.255
Net NPA to Total Assets (%)	0.0002	0.002	0.001	0.0008	0.001	0.001	0.0006
Total Investment to Total Assets	0.41	0.37	0.43	0.43	0.36	0.4	0.033
Standard Advances to Total Advances	57.05	58.01	60.46	52.42	53.59	56.3	3.285

- Assets Quality Ratios of Standard Chartered Bank

**Table 1.4**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Net NPA to Net Advance (%)	0.27	0.7	1.63	0.45	0.34	0.68	0.556
Net NPA to Total Assets (%)	0.001	0.003	0.008	0.002	0.001	0.003	0.003
Total Investment to Total Assets	0.22	0.22	0.26	0.22	0.25	0.23	0.019
Standard Advances to Total Advances	54.26	62.62	64.82	63.34	63.36	61.68	4.224

The analysis in Table 1.3 and Table 1.4 reveal that the HSBC bank has been successful to manage its NPAs. The Net NPA which was 0.91% of total net advances of the bank in 2010-11 have come down to 0.53% in 2014-15. While the Net NPA of SCB is showing increasing trend. Table 1.4 shows that it was 0.27 in 2010-11 but it has been increased up to 0.68% In 2014-15. The mean of Total Investment to total assets is also low in SCB. The ratio of standard advances which indicates the ratio of most secured loans in the banks SCB is indicating better (Average 61.68) than HSBC (Average 56.3). In case of NPA to Net advances HSBC is in better position.

### c)MANAGEMENT EFFICIENCY

Management Efficiency, another indispensable component of the CAMELS framework, means adherence to set norms, knack to plan and be proactive in the dynamic environment, leadership, innovativeness and administrative competence of the bank.

The following is the analysis of the various ratios used to measure management efficiency.

- (i)Business Per Employee
- (ii)Profit per Employee
- (iii)Credit Deposit Ratio
- (iv)Return on Net Worth

- Management Efficiency Ratios of Hong Cong and Shanghai Banking Corporation (HSBC)

**Table 1.5**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Business Per Employee	1221.70	165.79	188.99	227.44	267.83	414.35	452.98
Profit Per Employee	23.20	3.47	4.04	3.10	3.43	7.44	8.812
Credit Deposit Ratio	50.64	57.82	62.70	56.07	54.68	56.38	4.414
Return on Net Worth (%)	11.83	13.88	12.84	9.48	9.66	11.54	1.938

- Management Efficiency Ratios of Standard Chartered Bank

**Table 1.6**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Business Per Employee	1345.62	154.67	168.77	207.13	190	413.24	521.60
Profit Per Employee	26.36	2.31	3.67	2.39	4.18	7.78	10.416
Credit Deposit Ratio	84.22	86.88	99.69	94.88	93.90	91.91	6.279
Return on Net Worth (%)	16.70	12.76	17.78	8.19	13.41	13.77	3.773

The performance of Management Capacity is generally qualitative and can be understood through the subjective evaluation of Management System, Central mechanism and organizational culture or so on. However, the capacity of the management of a bank can also be determined with the help of certain ratios of off site evaluation of a bank. Table 1.5 and 1.6 reveals about the Management Efficiency of HSBC and SCB. In this, business per employee shows that, in 2010-11 it was very much high, 1221.70 for HSBC and 1345.62 for SCB. But for the succeeding years it is declining. Profit per employee which is also another important factor of Managerial Efficiency is declining in both the banks. The credit deposit ratio is very high in SCB (average 91.91) while it is low in HSBC (Average 56.38). Return on Net Worth shows the up and downs in the given years but satisfactory in both the banks.

#### **d) EARNING QUALITY**

The quality of earnings represents the sustainability and growth of future earnings, value of bank's curativeness and its competency to maintain quality and earn consistently. Earnings and profitability are examined as against interest rate policies and adequacy of provisioning. The single best indicator used to gauge earning is the Return on Assets (ROI), which is net income after taxes to total asset ratio.

**For the study, the following ratios have been used to measure earning quality:**

- (i) Return on Assets
- (ii) NIM to Total Assets
- (iii) Operating Profit to Total Assets
- (iv) Interest Income to Total Income

- Earning Quality Ratios of Hong Cong and Shanghai Banking Corporation (HSBC)

**Table 1.7**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Return on Assets	1.68	1.98	1.81	1.26	1.33	1.61	0.309
NIM to Total Assets	3.67	3.74	3.75	3.24	2.97	3.47	0.351
Operating Profit to Total Assets	3.23	3.52	3.06	2.30	2.19	2.86	0.586
Interest Income to Total Income	5.72	6.18	6.53	6.27	6.21	6.18	0.292

- Earning Quality Ratios of Standard Chartered Bank

**Table 1.8**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Return on Assets	2.44	1.49	2.43	1.20	2.42	1.99	0.603
NIM to Total Assets	4.09	3.73	4.15	4.30	4.25	4.1	0.224
Operating Profit to Total Assets	3.97	3.95	4.07	4.25	4.50	4.14	0.229
Interest Income to Total Income	6.50	6.97	7.53	7.96	7.72	7.33	0.593

Earnings are considered as the conventional parameter of measuring financial performance. It is exhibited in Table 1.7 and Table 1.8. The Average of Return on Assets is better in SCB which indicates 1.99 while it is lower in HSBC (1.61) as compare to SCB. Net Interest Margin, Operating Profit to Total Assets and Interest Income to Total income is comparatively high in SCB then HSBC.

### e) LIQUIDITY

In case of an adequate liquidity position, the institution can obtain sufficient funds, either by increasing liabilities or by converting its assets to cash quickly at a reasonable cost. Here liquid assets include Cash in Hand, Balance with RBI, Balance with other Banks and Money at call and Short Notices.

#### The following ratios have been used to measure liquidity:

- (i) Liquid Assets to Total Assets (%)
- (ii) Government Securities to Total Assets (%)
- (iii) Liquid Assets to Total Deposits (%)
- (iv) Liquid Assets to Demand Deposits (%)

- Liquidity Ratios of Hong Cong and Shanghai Banking Corporation (HSBC)

**Table 1.9**

Ratios	2010-11	2011-12	2012-13	2013-14	2014-15	Mean	S.D
Liquid Assets to total Assets (%)	0.09	0.10	0.08	0.11	0.18	0.11	0.039
Government Securities to Total Assets (%)	0.27	0.19	0.26	0.35	0.30	0.27	0.058
Liquid Assets to Total Deposits (%)	0.15	0.19	0.16	0.21	0.30	0.20	0.059
Liquid Assets to Demand Deposits	0.52	0.67	0.61	.0008	1.38	0.79	0.394

- Liquidity Ratios of Standard Chartered Bank



**Table 1.10**

<b>Ratios</b>	<b>2010-11</b>	<b>2011-12</b>	<b>2012-13</b>	<b>2013-14</b>	<b>2014-15</b>	<b>Mean</b>	<b>S.D</b>
Liquid Assets to total Assets (%)	0.64	0.03	0.04	0.05	0.06	0.16	0.266
Government Securities to Total Assets (%)	0.19	0.18	0.21	0.18	0.21	0.19	0.015
Liquid Assets to Total Deposits (%)	0.12	0.07	0.09	0.10	0.12	0.10	0.021
Liquid Assets to Demand Deposits	0.43	0.30	0.49	0.60	0.43	0.45	0.108

Above Table 1.9 and Table 1.10 show the liquidity position of both the banks which is also an important measure of CAMEL analysis. Transferability and Liquidity are the key ingredients for such transitions. It means that financial assets must be available to owners on short notice. In table 1.9 liquid assets which consist of cash is not showing drastic changes in both the banks but the average position of SCB is better than HSBC. The investment in Government securities held by the banks visa viz. to total assets are clear indicators of banks liquidity position, as this investment ratio has remained consistent around an average of 0.27 in HSBC and 0.79 in SCB. The total liquid assets to depositors has brought the fact to the forefront that the bank has the ability to meet any eventuality in case of depositors demand liquid assets, as this ratio has also remained by and large consistent at an average of 0.20 (HSBC) and 0.10 (SCB) with the standard deviation 0.059 (HSBC) and 0.021 (SCB). Consistency of the next ratio is also same. The average shows 0.79 for HSBC and 0.45 for SCB.

## CONCLUSION

Both HSBC and SCB are the oldest foreign banks in India. Their performance on CAMEL analysis is satisfactory as they are competent with all test of this model. In future they can do their branch expansion and can get the advantages of Foreign Direct policies of the Government of India. It has also been observed that these banks are also the source of inspiration for other Foreign banks which are working in India and as well as our domestic banks also.

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