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Performance Evaluation of Selected Public and Private Sector Bank in India an Application of CAMEL Model

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Abstract

It is widely believed that financial institutions have not shown any improvement in performance indicators, particularly as regards achieving loan targets, during the last decade. Although various initiatives are taken by banks for achieving a high-performance level, a study has been conducted to find out the relative performance of different public and private sector banks. In this study, four categories of public and private sector banks were identified on the basis of ownership structure, total assets, geographical spread and deposit base. A classification based on overall performance indicators such as loans per borrower, collection ratio, advances per customer, credit mix, deposits per customer, recovery rate, income from investments, loans growth and net profit was established. Findings from the analysis showed that both public and private sector banks perform equally well with respect to total assets, advances per customer, recovery rate, deposit per customer, income from investments, net profit and deposits growth.

Keywords: Performance evaluation, Public Sector Bank, Private Sector Bank, CAMEL Model

Introduction

In order to analyze the performance of both public and private sector banks in India, CAMEL model plays a vital role in the Evaluation Performance in Public and Private Sector Bank in India. It has been used to identify & analyze performance indicators for various industries such as manufacturing, retail trade, banking, education, insurance, health and transportation sectors. The key concept of the CAMEL model is Multi-Factor Modelling (MFM). The MFM model can be divided into five factors namely: Efficiency Factor, Utilization Factor, Economic Factor, Quality Factor and Regulation Factor. These factors help in examining various variables that affect performance indicators such as the number of branches, new borrowers, amount of loan given to a borrower, amount of investment made by a bank in its operational infrastructure, etc. These variables are based on previous data & analysis done by industry experts. The next step is to incorporate these variables into the CAMEL model to estimate their influence on performance indicators. As there are no reliable statistics available for all Indian Public and Private sector banks, we have used some well-known public sector banks as case studies for the evaluation of the CAMEL model. In this paper, we have used 3 selected Public sector banks (IDBI, Canara Bank and Oriental Bank of Commerce) for evaluating the CAMEL model for analysis of performance indicators for three categories i.e. outstanding credit to the business customer, the financial soundness of the business customer and internal efficiency of the bank. Data on a number of branches, advances to the business customer, non-performing loans (NPLs), the profitability of a business customer, balance sheet items and other information are collected for this study.

Objectives of the study

This paper describes performance indicators for both public and private sector banks in India and measures their performances using CAMEL model. It also explores various aspect of CAMEL model with respect to private and public sector bank performance.

Research Methodology

the current study is based on a secondary source of information to explore the role of CAMEL Model Performance Evaluation of Selected Public and Private Sector Bank in India. The relevant information was collected from different journals and reporters of international agencies like MFI India – HALCAM (Ministry of Home Affairs) as well as central government sources such as Annual Reports of RBI of each Public Sector Bank and Comptroller & Auditor General (CAG) report for public sector banks in India.

Literature Review

To get a clear insight on Performance Evaluation of Selected Public and Private Sector Bank in India an Application of CAMEL Model we had made an intensive literature review based on the keywords of the study. In addition to this we also visited few banking websites to collect data related to their Performance Indicators for reference purposes. This helped us to analyze their data from various viewpoints such as Industry Analysis, Microeconomics, Macroeconomics, Static Analysis, System Dynamics and Experiential Study. The resulting dataset which was compiled after performing primary research from several sources is discussed in detail in the literature review section. Kaur et al. (2015) stats that based on the previous research done by many institutes like Reserve Bank of India (RBI), State Bank of India (SBI), CII, CRISIL, etc., Biswas (2014) concluded that no significant effort had been made by any banking organization to adopt a system dynamics model for measuring performance indicators in order to benchmark themselves against each other and accordingly gauge their performance against others. Bansal & Mohanty (2013)stated it is essential to establish a reliable scenario development approach that will aid the implementation of a comprehensive performance evaluation model for bank managers. Therefore, a scenario development approach was decided based on previous researches which have been performed by institutions like MFI India – HALCAM (Ministry of Home Affairs) as well as central government sources such as Annual Reports of RBI of each Public Sector Bank and Comptroller & Auditor General (CAG) report for public sector banks in India.

Aspal& Dhawan (2014) studied the factor behind Performance Indicators that lead to increasing failures and growth in Public Sector Banks in India and hence analyzed how one can use modelling methods for finding solutions for problems that are encountered by bank managers. He identified three basic approaches namely StaticAnalyses, Performance Improvement Techniques (PIT) and Case Studies.

Nandi (2013) explained CAMEL model play a vital role in the performance evaluation of public and private banks of India and provided empirical evidence on using Performance Management Systems to determine the financial stability of the bank in an effective manner. Thirunavukkarasu& Parthiban (2015) suggested several PIT models that can be applied for analyzing financial performances and formulating action plans to achieve the overall goal of improving the financial stability of banks. The case studies showed that PIT methods were used in determining different goals such as increased profits, reducing losses, enhanced credit management and taking decisions regarding opening up new branches and setting up ATMs in various areas(Prasad, 2012). Mjhaljek (2006) study findings suggest that banks need to enhance their abilities to adopt modern systems that could monitor their financial health on regular basis in order to prevent unexpected circumstances from taking place in future. (Sangmi& Nazir, 2010)the study result suggests that some steps could be taken in order to implement new ideas into banking sectors such as designing alternative mechanisms for coping with sudden or unusual changes in economic conditions, deploying efficient organizational structures to ensure good availability of data for decision making and working with an active monitoring system for achieving expected goals. (P. Kaur, 2015) found that by adopting effective business models the Indian public and private banks have successfully established long term relations with their customers. This would enable them to acquire sufficient experience and skill for improving their performances in an effective manner.

Performance Evaluation of Selected Public and Private Sector Bank in India an Application of CAMEL Model

CAMEL model plays a vital role to measure the performance of Indian private and public bank, during its critical phase. With the CAMEL model banks could adopt the best possible policies and strategies for the growth of their organization and also they could perform well with continuous improvements. Bank's policy formulation should consider not only current but also future potential customer base, location, access to technologies, expected service quality, ability to grow profitably, manage risk effectively, capital requirement, security requirements, ease of operation, attractiveness to work with and deliver goods to customer. According to existing knowledge about public and private banks performance measurement has become important due to frequent research conducted by management experts. Moreover, the importance of measurement is increased because it assists management in deciding corrective actions for reducing the poor performance of bank's or at least increasing their profitability. The most appropriate way of measuring the performance of public and private banks is measuring efficiency in the production process. Performance evaluation should include three elements which are Customer Satisfaction, Performance Measurement and Learning Process. Efficiency in the production process can be measured using direct costs such as man-hours and indirect costs such as credit risk. Similarly, a similar measure can be adopted for evaluating the performance of banks in India. Firstly, a selection of a set of services must be identified for evaluation. Next, secondly, all other areas such as call centre and non-production areas can be evaluated using standard methodology such as IT Service Management (ITSM) framework and value chain framework (VF). Further criteria like convenience, credibility, privacy, legal provisions, consistency with organizational strategy, efficiency and effectiveness can be used for performance measurement. Finally, thirdly results should be presented using a chart which would give an exact overview of bank's performance in the past year. Although it is known that this will assist the bank's management in formulating a proper action plan for improvement of its operations. Also, this method will help the bank's employees to get an idea about actual performance and consequently also encourage them to do better in future. Consequently, there are so many initiatives taken by government bank authorities to promote productivity, competitiveness and quality in the Indian economy. Some examples are initiatives taken by NABARD to enhance the lending capacity of financial institutions, provision of incentive packages for job oriented/performance-based recruitment of employees, formulation of regulations by RBI to check the inefficient operation of public banks, tax exemption facility provided by the central government to small enterprises etc. Now if we observe a detailed study on the effectiveness of these schemes, we will get the overall picture that most of these schemes have a major shortcoming which is: i) High degree of duplication ii) Limited results iii) Absence of control mechanism Manual Analysis Methodology Bank examination process starts with due diligence report being submitted by credit committee which provides the evaluation of business & customer portfolio for shortlisting potential borrowers. Later it is further filtered through other criteria like knowledge & experience of board members, company age, maturity & stage of development, good repute, capital position etc. On the basis of the above reports, one or more borrower companies are recommended for opening credit card accounts for cross-checking the capacity & capabilities of the applicant company. These accounts are opened under its individual authority and hence only have an effect on such particular borrower companies. This in general forms a duplicative reporting process as far as any given applicant company is concerned. To reduce duplication one important change has been proposed by CARD-The country with existing multi-purpose ATMs (APM) could operate on ATM switching service offered by the Reserve Bank of India (RBI) using the national ATM Switching Project (NATSP). This has proved to be effective in many areas but not applicable in all cases as its complexities increase when required by more than one Bank simultaneously. However, it does solve a great problem as far as various duplicative activities like research and advisory work etc. are concerned. It can also lead to expansion of bank branches & increasing branch management time as per growing market & product coverage etc. To cut down costs involved in the creation of duplicative information the industry had suggested RBI make this system paperless through Data Acquisition Mechanism (DAM). Instead of recording each application/bank account in credit history reports an appropriate record should be created at every stage where applications or banks are listed in credit history reports. By adopting this strategy every member bank would get appropriate data from the various source without wasting their resources and also bring transparency to their respective systems. Data quality will be ensured through access control and custodial facilities available at the head office level, Credit Bureau's National Data Centre (NDC) and nationwide Interbank Information Network (INI). Such facility will ensure quality & timeliness of data which is so crucial for the proper decision-making process. To maintain security, confidentiality & privacy, DAM's computerized Database shall be controlled through a two-way check (entry and exit) system which would eliminate the chance of manual manipulation or falsification of records. This would not only save precious resources but also create a strong anti-fraud / cheating wall around financial transactions in the financial sector. For controlling credit portfolio with regional Banks to give a uniform view on overall credit information in order to have a macro approach towards financial services provided by the banking sector, India being a diverse country with heterogeneous nature of economy needs a uniform approach for assessing credit risk & promoting sound business practices, backed by sufficient statistical evidence and properly defined technical terms, instead of following unscientific "Banker's Almanac" approach which suffers from extreme redundancy and chaos in the classification of individual Bank accounts /creditworthiness. In the light of the huge consumer surplus at the end-user level, it is essential to draw general conclusions regarding any account as the specific behavioral factors for particular individual cases should be identified before considering it as defaulting / risky account. For developing a more complete picture of the relative importance of such variables as health & asset etc., the use of the Consumer Finance survey has been proposed as one of the techniques to generate empirical evidence on these topics.

However, it is required to go beyond mere quantity-based indices like assets held by consumers or savings as they fail to address all issues related to accounting management by consumers as well as financial institutions and requires analytical sophistication and integrated thinking which requires long term continuous study and relevant developments in respective areas. Hence we should build systems based on the co-relation between related factors in any segment or activity for measuring parameters related to performance in the banking industry which shall reflect economic behaviors and market preferences in a real-life environment. The key measures are relating to managing creditworthiness, service delivery & provision of other information necessary for commercial purposes. We need to encourage innovative methods for both the supply side and demand side which will facilitate appropriate means for building capabilities at right time, thereby catering for diverse consumers needs at their respective stages of lifecycle and consumption behavior. Such a structure would also lead to capturing customers' mindshare through improved knowledge management practices, thus becoming a vital part of the Credit portfolio management system in general.

Conclusion

In the end, we can conclude that the Application of CAMEL model for performance evaluation of public and private sector bank in India play an important role in identifying strengths and weaknesses in bank operations. This model provides an excellent guideline for improvement in efficiency, performance & safety & will serve as a valuable source of information for investment decisions. Overall, there is a need for these reforms as most of the business has shifted from traditional mode to cost-saving models with an increase in digitization and consumer demands. It is essential to balance various measures with timely planning & refinement for enabling smoother flow of cash flows through Banks with highest levels of operational efficiency. Furthermore, one should recognize the change in macroeconomic conditions that could make banks respond with strategic changes. It is crucial to consider not only growth rate but also sustainability & reliability of future income streams as these factors affect profitability & hence this balance sheet allows one to build a competitive edge by bringing down risk profile to achieve targets set by both investors and government agencies. In such a case, they could run away with your deposits if you don't pay attention to how much risk they are willing to take on their capital & liabilities. With respect to Investment banks, it is also necessary to take into account current industry regulations and rules before recommending financial instruments for a private placement or underwriting new company incorporation or other company events. This gives confidence to potential investors that you have a proper understanding of current regulatory policies & ensure maximum security for your clientele and build trust between them. On the other hand, even though Government controls are concerned with the implementation of market-driven reform plans and legislations in certain industries like insurance, real estate and retailing sectors, its capability to track up-to-date performance metrics remains at par with best practices globally.

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