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Financial Analysis of Small Finance Banks in India through CAMEL Rating

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Abstract

Banking performance is assessed by implementing a regulatory banking supervision framework. CAMEL rating system is used to evaluate the overall performance of the banks and to determine their strengths and weaknesses. Small finance banks are a result of RBI's efforts to promote niche banking. These are the financial institutions which provide basic banking service of acceptance of deposits and lending. The aim behind these to provide financial inclusion to sections of the economy such as small business units, small and marginal farmers, micro and small industries and unorganised sector entities which are not being served by other banks in unbanked and under-banked regions.

Purpose: This paper attempts to apply the CAMEL rating on ten small finance banks in India. The overall financial performance of these banks has been assessed.

Design and methodology: The study is based on secondary data based on annual reports of these small finance banks for the financial year 2019-20. Descriptive analysis was done through ranking in each of the parameters of CAMEL rating. The inferential analysis was done through ANOVA test and was further analysed through Post hoc test (Bonferroni method).

Findings: The findings of the study are that there is a difference in financial performance of the small finance banks in India. The best performer and worst performer was also assessed.

Practical implications: The study is relevant to understand the financial performance of the small finance banks in India. This research paper will provide a helping hand to the researchers for further studies in the small finance banks in India.

Keywords: Small finance banks, CAMEL rating, capital adequacy ratio, asset quality ratio, management quality ratio, earning ratio, liquidity ratio.

Introduction

Small finance banks are a result of RBI's efforts to promote niche banking. These are the financial institutions which provide basic banking service of acceptance of deposits and lending. The aim behind these to provide financial inclusion to sections of the economy such as small business units, small and marginal farmers, micro and small industries and unorganised sector entities which are not being served by other banks in unbanked and under-banked regions. In India small finance banks emerged with the announcement made by Finance Minister in the Union Budget in August 1996 and RBI decided to licence new small finance banks in the private sector. Existing non-banking financial companies (NBFC), microfinance institutions (MFI), local area banks (LAB) and urban co-operative Banks (UCBs) can apply to become small finance banks. They are established as public limited companies in the private sector under the Companies Act, 2013 and governed by the provisions of Reserve Bank of India Act, 1934, Banking Regulation Act, 1949 and other relevant statutes. CAMEL rating system is used to evaluate the overall performance of the banks and to determine their strengths and weaknesses. In India, on the recommendations of Padmanabham Working Group (1995) committee, RBI adopted CAMEL (capital adequacy, asset quality, management quality, earnings and liquidity) approach in 1996 for rating financial performance of commercial banks in India[1]. The paper attempts to apply the CAMEL rating on small finance banks in India. The study takes into account all 10 small finance banks as listed in RBI bank list and includes financial year 2019-20[2].

Review of Literature

The research study relates to the small finance banks in India therefore the literature review is done on research papers published on Indian banking sector.

The applicability of CAMEL norms on the performance of SBI Groups 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 (Siva and Natarajan (2011))[3]. The financial performance of ten Indian commercial banks during from the year 2005-06 to 2009-10 concluded that the banks had improved their performance in all the aspects. Further in comparison to public and private sector banks, the public sector banks were showing better performance as compared to the private sector banks (S. M. Tariq Zafar, Adeel Maqbool & Syed Imran Nawab Ali (2012))[4]. The public sector bank‘s performance from 2004 to 2014 analysed by CAMEL model concluded that Bank of Baroda stood first and were considered more steady banks followed by PNB, Central Bank of India, Indian bank and IDBI banks. Canara bank & SBI were considered as medium performance. Union Bank, Bank of India, Syndicate Bank & CBI were considered below average performance (Jagjeet Kaur, Dr. Harsh Vineet Kaur (2016))[5]. The evaluation of Bank of Baroda and Punjab National Bank covering the period of five years from 2011–12 to 2015–16 analyzed concluded that the financial performance of Bank of Baroda was better than Punjab National Bank (Maninder Kaur, Ritu Priya (2017))[6]. The financial performance using CAMEL framework found no significant difference between the ICICI and HDFC bank's financial performance and concluded that the ICICI bank performance is slightly less compared with HDFC (Srinivas and Saroja (2013))[7]. The different perspectives of profitability of five major private banks for a period of 2004 to 2014 were examined using ratio analysis and ANOVA technique and it was found that HDFC Bank has been the excellent performer over the decade (Garg and Kumari (2015))[8]. The performance of SBI and ICICI Bank was compared using CAMEL parameters in which it was found that ICICI bank needs to improve its position with regard to capital adequacy and asset quality while SBI need to improve its position with regard to management efficiency, earning quality and liquidity (Purohit and Bothra (2018))[9]. A strong relationship among public, private and foreign banking sectors was found with regard to return on investments, equity and advances on the profitability position The cash-deposit ratio and credit-deposit ratio have shown a positive influence on the short-term liquidity, while the net interest margin and investment ratios have not shown any response on the solvency position across the three banking sectors (Banu M (2019))[10].

Research Gap

The literature reviewed above indicates performances and soundness of nationalized banks, private sector banks and foreign banks in India with the help of CAMEL Model. The studies conducted till date are on public sector banks, private sector banks, comparison between public sector banks, private sector banks and the most recent one as comparison between public, private and foreign banks. In India even small finance banks have been functioning and come under the purview of RBI. There is no research on it so it gives ample opportunity for a research on financial performance of small finance banks in India with the help of CAMEL approach.

Objectives of the Study

1. To study the capital adequacy ratio of small finance banks in India.
2. To compare the asset quality ratio of small finance banks in India.
3. To study the management efficiency ratio of small finance banks in India.
4. To compare the earning ratio of small finance banks in India.
5. To compare the liquidity ratio of small finance banks in India.
6. To analyse the financial performance of small finance banks in India.

Hypotheses of the Study

1. There is no difference in capital adequacy ratio between small finance banks in India.
2. There is no difference in asset quality ratio between small finance banks in India.
3. There is no difference in management efficiency ratio between small finance banks in India.
4. There is no difference in capital earning ratio between small finance banks in India.
5. There is no difference in liquidity ratio between small finance banks in India.
6. There is no difference in financial performance between small finance banks in India.

Limitation

The study includes analysis based on financial year 2019-2020.

Descriptive Analysis & Interpretation

Table 2: Capital Adequacy Ratios

S.N.	Banks	Capital Asset Ratio (%)	Rank	Debt Equity Ratio	Rank	Advance to Asset Ratio (%)	Rank	Equity to Total Asset Ratio (%)	Rank	Composite	Overall Rank
1	Ujjivan SFB	28.82	3	3.66	1	76.28	1	17.20	3	2	1
2	Utkarsh SFB	22.19	8	8.22	7	66.79	6	10.84	6	6.75	7

3	Suryoday SFB	29.57	1	4.03	2	65.84	7	19.88	1	2.75	2
4	North East SFB	24.98	4	4.66	3	65.33	8	17.7	2	4.25	4
5	Jana SFB	19.25	9	12.56	10	70.4	3	7.38	10	8	8
6	ESAF SFB	24.03	5	7.73	6	69.14	4	11.45	7	5.5	6
7	Capital SFB	19.11	10	12.10	9	62.07	10	7.63	9	9.5	10
8	AU SFB	21.99	7	8.73	8	64.05	9	10.26	8	8	8
9	Fincare SFB	29.28	2	6.87	5	67.67	5	12.7	5	4.25	4
10	Equitas SFB	23.61	6	6.04	4	71.18	2	14.21	4	4	3

Source: Compiled from Annual Reports 2019-2020

Table 2 shows that Suryoday SFB maintains the highest CAR with 29.57% whereas Capital SFB has lowest CAR with 19.11%. All the small finance banks have maintained sufficient CAR though the BASEL II norms are to maintain 8%. Ujjivan SFB has a minimum debt equity ratio of 3:66 whereas Jana SFB has maximum debt equity ratio of 12.56. All SFBs maintain advance to asset ratio within the range of 62 -76%. Suryoday SFB maintains the highest equity to total asset ratio with 19.88% whereas Jana SFB has lowest with 7.38%. Ujjivan SFB has the best overall capital adequacy ratio.

Table 3: Asset Quality Ratios

S.N.	Banks	Government Securities to Total Investments (%)	Rank	Net NPA to Total Assets (%)	Rank	Gross NPA to Total Assets (%)	Rank	Net NPA to Net Advances (%)	Rank	Total Investment to Total Assets (%)	Rank	Composite	Overall Rank
1	Ujjivan SFB	99.996	4	0.15	2	0.74	3	0.20	2	13.01	8	3.8	3
2	Utkarsh SFB	100	1	0.12	1	0.47	1	0.18	1	12.68	9	2.6	1
3	Suryoday SFB	84.78	9	0.38	4	1.89	8	0.58	4	15.07	6	6.2	7
4	North East SFB	91.51	7	0.79	8	1.27	7	1.2	7	17.11	5	6.8	8
5	Jana SFB	99.996	4	0.99	9	2.27	10	1.41	9	18.73	3	7	9
6	ESAF SFB	86.92	8	0.45	5	1.07	4	0.72	5	18.31	4	5.2	5
7	Capital SFB	100	1	0.77	7	1.1	6	1.25	8	19.74	2	4.8	4
8	AU SFB	71.64	10	0.52	6	1.09	5	0.81	6	25.31	1	5.6	6
9	Fincare SFB	100	1	0.28	3	0.63	2	0.41	3	14.15	7	3.2	2
10	Equitas SFB	97.86	6	1.28	10	2.16	9	1.8	10	12.13	10	9	10

Source: Compiled from Annual Reports 2019-2020

It has been observed from Table 3 all the small finance banks have the maximum investment in government securities. Utkarsh, Ujjivan and Fincare SFB have minimum gross and net NPAs but they rank one of the lowest in total investment to total assets. AU SFB has highest total investment to total assets and also has minimum investment in government securities among these banks. Utkarsh SFB maintains the highest asset quality ratios closely followed by Fincare SFB and Ujjivan SFB.

Table 4: Management Efficiency Ratios

S.N.	Banks	Business per Employee (Rs)	Rank	Profit per Employee (Rs)	Rank	Return on Equity (%)	Rank	Cost to Income Ratio (%)	Rank	Composite	Overall Rank

1	Ujjivan SFB	12248675	8	214720	5	13.90	4	65	4	5.25	6
2	Utkarsh SFB	12600000	7	212205	6	21.18	1	57.63	5	4.75	4
3	Suryoday SFB	13588924	5	236421	4	11.3	5	47.1	1	3.75	3
4	North East SFB	9970000	10	59,834	9	3.45	9	70.4	8	9	9
5	Jana SFB	11600000	9	18,585	10	2.89	10	80.58	10	9.75	10
6	ESAF SFB	40859724	2	570540	1	17.94	2	64.91	6	2.75	1
7	Capital SFB	48424000	1	333000	3	6.24	8	75.76	9	5.25	6
8	AU SFB	31063782	3	394334	2	15.6	4	54.22	2	2.75	1
9	Fincare SFB	12860940	6	194825	7	15.87	3	55.76	3	4.75	4
10	Equitas SFB	15233855	4	151270	8	8.88	7	66.38	7	6.5	8

Source: Compiled from Annual Reports 2019-2020

Table 4 shows that business per employee is highest in Capital SFB and ESAF SFB and is lowest in North East SFB and Jana SFB. Profit per employee is highest in ESAF SFB followed by AU SFB and lowest in Jana SFB and North East SFB. Utkarsh SFB has got the maximum return on equity at 21.18% and Jana SFB has got the least with 2.89%. Suryoday SFB has the lowest cost to income ratio at 47.1% whereas Jana SFB has the highest cost to income ratio with 80.58%. Among these small finance banks ESAF SFB and AU SFB have highest management efficiency ratios on the other hand Jana SFB and North East SFB stand lowest in the same category.

Table 5: Earning Ratios

S.N.	Banks	Earning per Share (Rs)	Rank	Operating Profit to Total Assets Ratio (%)	Rank	Net Interest to Total Income (%)	Rank	Net Profit to Total Assets (%)	Rank	Composite	Overall Rank
1	Ujjivan SFB	2.18	9	9.27	2	54.00	2	1.9	5	4.5	3
2	Utkarsh SFB	2.49	7	3.72	8	51.79	4	1.98	4	5.75	5
3	Suryoday SFB	13.38	3	5.68	7	57.49	1	2.07	1	3	2
4	North East SFB	0.43	10	2.7	10	51.89	3	0.61	8	7.75	10
5	Jana SFB	6.21	5	8.91	4	41.71	8	0.21	10	6.75	8
6	ESAF SFB	4.45	6	3.43	9	51.22	5	2.01	3	5.75	5
7	Capital SFB	8.18	4	6.34	6	34.45	10	0.48	9	7.25	9
8	AU SFB	22.78	2	8.48	5	38.24	9	1.6	6	5.5	4
9	Fincare SFB	24.43	1	11.09	1	50.89	7	2.02	2	2.75	1
10	Equitas SFB	2.39	8	9.05	3	51.07	6	1.26	7	6	7

Source: Compiled from Annual Reports 2019-2020

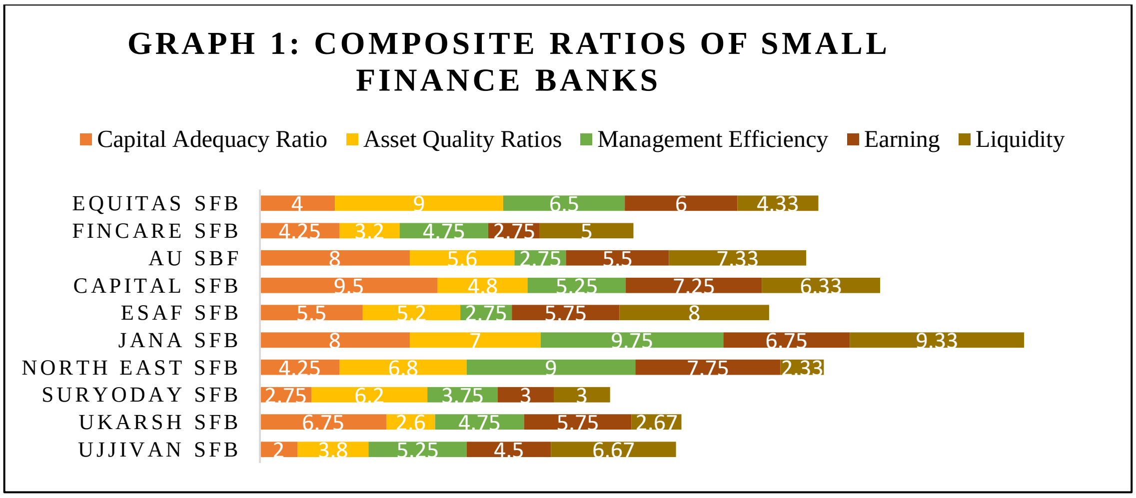
Table 5 shows that Fincare SFB has the maximum earning per share Rs 24.43 followed by AU SFB at Rs 22.78 and lowest is of North East SFB at Rs 0.43. The operating profit to total asset ratio is best maintained by Fincare SFB and lowest is again by North East SFB. Net interest to total income and Net profit to total asset ratios are highest for Suryoday SFB and lowest in Capital SFB and Jana SFB respectively. Fincare SFB has the maximum earning ratio and North East SFB has the minimum.

Table 6: Liquidity Ratios

S.N.	Banks	Liquid Assets to Total Assets (%)	Rank	Liquid Assets to Total Deposits (%)	Rank	Credit Deposit Ratio (%)	Rank	Composite	Overall Rank
1	Ujjivan SFB	7.29	9	12.46	9	130	2	6.67	7
2	Utkarsh SFB	17.76	1	30.83	2	120	5	2.67	2
3	Suryoday SFB	15.61	2	29.4	3	124	4	3.00	3
4	North East SFB	13.38	5	31.02	1	151.47	1	2.33	1
5	Jana SFB	6.93	10	10.15	10	103	8	9.33	10
6	ESAF SFB	9.53	7	12.84	8	93.16	9	8.00	9
7	Capital SFB	15.31	3	18.35	6	74.40	10	6.33	6
8	AU SFB	8.00	8	12.88	7	103.17	7	7.33	8
9	Fincare SFB	15.22	4	23.27	5	103.47	6	5.00	5
10	Equitas SFB	13.33	6	23.51	4	127	3	4.33	4

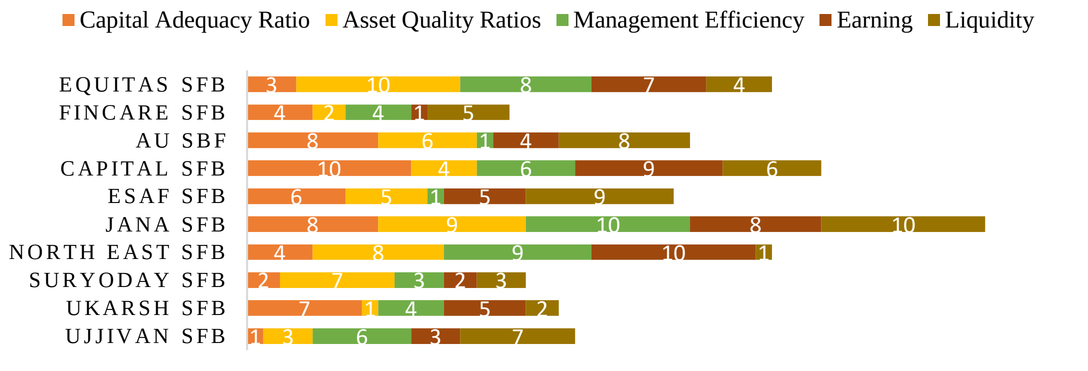
Source: Compiled from Annual Reports 2019-2020

Table 6 shows that liquid assets to total assets are highest of Utkarsh SFB with 17.76% and lowest of Jana SFB at 6.93%. Liquid assets to total deposits and credit deposit ratio are highest for North East SFB and lowest in Jana SFB and Capital SFB respectively. North East SFB has the highest liquidity ratio and Jana SFB has the lowest liquidity ratio.



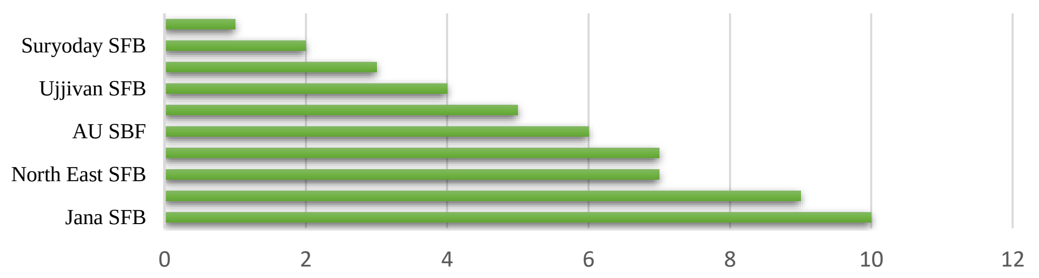
Graph 1 shows a comparison in the composite ratios of the small finance banks. Low values represent best performance and high values show worst performance in the five parameters of CAMEL rating.

GRAPH 2: CAMEL RANK OF SMALL FINANCE BANKS



Graph 2 shows the financial performance of the 10 small finance banks operating in India based on CAMEL rating.

Graph 3: Overall Rank



	Jana SFB	Capital SFB	North East SFB	Equitas SFB	AU SBF	ESAF SFB	Ujjivan SFB	Ukarsh SFB	Suryoday SFB	Fincare SFB
Overall Rank	10	9	7	7	6	5	4	3	2	1

Graph 3 represents the overall financial performance is best for Fincare SFB followed by Suryoday SFB and Jana SFB and Capital SFB stand at lowest level.

Inferential Analysis & Interpretation

One-way analysis of variance (ANOVA) is used to determine whether there is any significant difference in CAMEL ratios and financial performance between the small finance banks in India. The samples are drawn from a normal population which has the same variance. For follow up of the significant results post-hoc test was conducted by applying Bonferroni method.

1. There is no difference in capital adequacy ratio between small finance banks in India.

Capital Adequacy Ratio

ANOVA

Source of Variation	***SS***	***df***	***MS***	***F***	***P-value***	***F crit***
Between Groups	221	9	24.55556	6.75841	3.04E-05	2.210697
Within Groups	109	30	3.633333			
Total	330	39				

From ANOVA test results it was observed that the calculated P value is less than 0.05 (5% level of significance), so we reject the null hypothesis and conclude that there is a difference in capital adequacy ratio among small finance banks in India.

Asset Quality Ratio

ANOVA

Source of Variation	***SS***	***df***	***MS***	***F***	***P-value***	***F crit***
Between Groups	168.98	9	18.77556	2.810712	0.011744	2.124029
Within Groups	267.2	40	6.68			
Total	436.18	49				

It was observed that the calculated P value is less than 0.05 (5% level of significance), so we reject the null hypothesis and conclude that there is a difference in asset quality ratio among the small finance banks in India.

Management Efficiency Ratio

ANOVA

Source of Variation	***SS***	***df***	***MS***	***F***	***P-value***	***F crit***
Between Groups	202.9	9	22.544444	5.2428941	0.0002619	2.210697
Within Groups	129	30	4.3			
Total	331.9	39				

It was observed that the calculated P value is less than 0.05 (5% level of significance), so we reject the null hypothesis and conclude that there is a difference in management efficiency among the small finance banks in India.

Earning Ratio

ANOVA

Source of Variation	***SS***	***df***	***MS***	***F***	***P-value***	***F crit***
Between Groups	99.5	9	11.055556	1.4389009	0.2161865	2.210697
Within Groups	230.5	30	7.6833333			
Total	330	39				

It was observed that the calculated P value is greater than 0.05 (5% level of significance), so we accept the null hypothesis and conclude that there is no difference in earning ratios among the small finance banks in India.

Liquidity Ratio

ANOVA

Source of Variation	***SS***	***df***	***MS***	***F***	***P-value***	***F crit***
Between Groups	156.8333	9	17.42593	3.843954	0.005824	2.392814
Within Groups	90.66667	20	4.533333			
Total	247.5	29				

It was observed that the calculated P value is less than 0.05 (5% level of significance), so we reject the null hypothesis and conclude that there is a difference in liquidity ratios among the small finance banks in India.

Composite Performance (Overall Ranking)

ANOVA

Source of Variation	***SS***	***df***	***MS***	***F***	***P-value***	***F crit***

Between Groups	154.58	9	17.17556	2.630254	0.017159	2.124029
Within Groups	261.2	40	6.53			
Total	415.78	49				

It was observed that the calculated P value is less than 0.05 (5% level of significance) which indicates a difference in financial performance among the small finance banks in India. Thus the null hypothesis is rejected.

Since the null hypothesis is rejected which implies that there is significant difference in financial performance of small finance banks in India. To find out in which banks there is difference in financial performance, a post-hoc test was necessary. In this study Bonferroni correction was used.

Bonferroni correction = α / Number of SFB
= 0.05/ 10
= 0.005

It has been observed that overall differences in the financial performance of small finance banks are due to differences in the financial performance of Ujjivan SFB, Jana SFB, Utkarsh SFB, Suryoday SFB and Fincare SFB. Since P-value of Ujjivan & Jana SFB, Utkarsh & Jana SFB, Suryoday & Jana SFB and Jana & Fincare SFB are less than the Bonferroni corrected value of .005, signifies that the overall differences in the financial performances are due to these banks.

Conclusion

By applying the CAMEL rating on small finance banks it was found that there is a difference in capital adequacy, asset quality, management efficiency and liquidity but no difference was observed on earning ratios. Overall earning positions of all the small finance banks were similar. There is a difference in financial performance of the small finance banks in India. The overall financial performance is best for Fincare SFB followed by Suryoday SFB and Utkarsh SFB whereas Jana SFB is worst performer. The performance of Capital SFB and North East SFB were not satisfactory. On further analysis of the data it was found that this difference due to the variation in performance of these banks.

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