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INDICATIVE PERFORMANCE OF COMMERCIAL BANKS

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ABSTRACT

The objective of the paper is to evaluate the business performance of commercial banks working in private and public sector. Both are functioning in the same and similar business environment facing almost similar problems. It is a matter of curiosity to find out what are those factors cause to affect their efficiency and effectiveness.

For the purpose of this comparative study, the State Bank and the ICIC Bank prominently functioning in the public and private sector respectively were selected. Undeniably, they are not completely comparable. Nevertheless, comparables are equally rare. They were selected mostly because their rates of growth of deposits and advances were almost similar. The SBI recorded the increment of 31 per cent and the ICIC Bank 28 per cent in their deposits during the period of five years, and about 21 per cent and 20 per cent rise in advances, respectively.

For the purpose of evaluating their operational performance, five most universally accepted ratios have been applied, namely (a) interest earned to interest expended, (b) interest contribution ratio, (c) cost of deposits, (d) return on assets, and (e) advance deposit ratio.

The analysis brings home the fact that the advance deposit ratio was 77.7 and 57.12 per cent respectively in case of the State Bank of India and the ICIC Bank. The increase in the deposits during the period of five years was 25.34 per cent and 28. 1 per cent for the selected public and private sector bank. The capacity to meet the revenue expenses, as depicted by the ICR, was higher in respect of the ICIC Bank than the State Bank of India. Further, the cost of deposits in the case of the State Bank of India was far higher than the ICICN Bank. This apart, the return on assets was round 11.5 per cent in the ICIC Bank against 10.2 per cent achieved by the State Bank of India.

Key words:

Cos t of Deposits, Return on Advances
Interest Contributions Ratio, Demand and Time liabilitie

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Introduction

Banks in India heavily bank upon public trust and need. Veritably their endogenous health and hygiene has never been remained beyond apprehension. The regulatory authorities, as remote controllers, have been keeping exacting vigilance as well as guiding them for systematic development; they hardly ensure risk-free functioning of banks. Chandrakant Mehta (!) said, The Indian Commercial banks conceal more than they reveal. Their operational performance has never been what it should have been". A few decades ago, M.P. Singh, erstwhile professor at NIBM caviled at by saying, "Window dressing in financial statements of commercial banks has become an established practice in India that covers their short workings thereby sowing the seeds of functional ailments". Howsoever unreasonable it would appear, it cannot be gainsaid that the credibility of commercial banks was not the direct consequence of their operational performance. To what extent it was reasonable could likely to be verified by little in-depth analysis.

Hypothesis

This paper is based upon the hypotheses:

[a] The betterment of operational performance of a commercial bank improves its credibility in public" whether it is in public or private sector; and

[b] The profitability of the commercial banks whether in public or private sector, is the result of their effective customer relationship.

There might be many latent predilections with different priorities. They are, nevertheless, outside the scope of present study. In order to substantiate the above hypothesis, the objectives mentioned below have been pursued in a best possible manner.

Objectives

On the foundation stone of above hypothesis, the objective of this paper includes:

- The study of trends in the portfolio of deposits and advances, being the indicators of public trust in them;
- The study of effectiveness of operational performance such as cost of deposits and return on advances; and

- Examine the capacity to meet current revenue expenses.

This indicative study pertains to only two most popular commercial banks of India in two different sectors, i.e., public and private sectors, namely, State Bank of India and ICICI Bank. Credibility, public trust or acceptance, operational performance and efficiency are a few characteristics which do not change year to year, and hence, the time-related data for the study is immaterial.

The accounting parameters considered for the purpose of examination are common and normal throwing light upon the comparative operational performance of commercial banks by taking a few common performance variables into consideration. These variables would shed ample light upon the efficiency of performance not in absolute and exclusive but on comparative and inclusive terms. It is however, subject to certain assumptions set out below.

Assumptions

While examining the operational performance of both commercial banks, the following assumptions have been set out for purposive analysis.

(a) Economic, commercial as well as financial environments are common to both;
(b) Operational practices, norms and conventions in relation to business of banking are equally subject to Regulatory authorities, including Reserve Bank of India;
(c) Accounting Standards and practices, norms, conventions, guidelines, form of presentment of annual financial statements and definitions of accounting terms are common to both commercial banks;
(d) Both are operationally independent within the legal and regulatory framework; and
(e) Both enjoy public confidence and reputation.

Undeniably, the SBI has specific advantages, facilities, opportunities and preferences while the ICIC Bank has no such favours at all. Their direct influence might be perceptible in size and scale of operations but not on efficiency and effectiveness of performance.

Limitations

(1) The study concerns with only two major commercial banks representing public and private sectors .i.e. the State Bank of India and the ICICI Bank
(2) It is limited to external variables published for publish consumption,
(3) Critical and significant internal information was never made available,

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(4) The period of the study was limited to five years i.e. from March 2011 to 2015.

Research Methodology

(a) Selection of Sample banks

These two banks have been selected for the purpose of substantiating the hypothesis on account of the following significant features of performance. Table 1 depicts the figures relating to their performance over the period of five years, i.e March 31, 2011 to March 31, 2015.

Table 1: Fundamental Financial Variables (Rs. In Crores)

NO.	Particulars	SBI 2011	SBI 2015	ICICI 2011	ICICI 2015
01	Share Capital	643	746	812	965
02	Deposits	12,34,666	16,53,751	6,,45,971	8,98,951
03	Advances	09,43,114	12,64,278	3.60.222	5,13,173
04	EPS (Rs.)	10.34	11.74	13.52	13.09

General Features of Performance:

- The share capital of the SBI increased by 14.11per cent as against 16.1per cent increase registered by ICIC Bank during the period under review;
- The SBI being the premier public sector bank of long standing has had huge public deposits amounting to Rs. 16.53 lakhs Crores by the end of March 2015 recording the increment of not less than 25.34 per cent in the quinquennium under study;
- As against the performance of SBI, the ICIC Bank had raised deposits from Rs.6.45 lakh Crores to Rs. 8.98 lakh Crores, recording the net increment of about 28.14 per cent;
- Rs. .9.43 lakh Crores of advances by the SBI in the year 2011 went up to Rs. 12.64lakh Crores, marking the rise of 21 per cent;
- The ICIC Bank expanded its advance portfolio by 16.1 per cent from Rs. 3.60lakh Crores to Rs. 5.13lakh Crores,; and

- Interestingly, while the earnings per share in case of the SBI enhanced from Rs.10.34 in 2011 to Rs. 16.23 in 2015, it considerably diminished to Rs. 13.09 in 2015.

Thus, the operational performance of both the banks was almost similar; but their financial results only were at large variance.

(b) Tools of Analysis

Spencer Trucker (3) strongly advocated the application of ratio in measuring and comparing the business performance. He said, "Ratio is a secular indicator which remains unconcerned to the quality and quantity of its participating variables. It only reveals a causal relationship between the cause and its effect". And so, It has become a worldwide practice to make use of certain relevant ratios for analysis of performance.

For the purpose of assessing the efficiency and effectiveness of operational performance of a commercial bank a few common ratios are normally applied which include:

1. Interest Received to Interest Paid Ratio.
2. Interest Contribution Ratio
3. Cost of Deposits and Return on advances

   Advance Deposit Ratio

(1) Interest received to interest paid Ratio

The fundamental business of a commercial bank is to accept public deposits to lend for the purpose of profits. The business of accepting deposits from the public and granting loans and granting loans and advances as been carried on in compliance with the normal banking laws and conventions. Average rate of interest on deposits is always lower than the average rate of interest on loans and advances.

According to N. Vaghul,(4) the erstwhile chairman of NIBM, " the Ratio of interest earned to interest paid is a perfect indicator of efficiency of banking business and that evinces the capacity to take risk". This important indicator carries the impact of market and credit risks.

(2) Interest Contribution Ratio

The uncommon ratio has been formulated on the basis of contribution ratio, normally adopted by financial managers for selection of products. It compares contribution i.e., excess of income over direct expenses, to income. For its application in case of banking business, it is modified as under:

Interest Contribution Ratio = (Interest Received – Interest paid) / (Interest Received)

Seemingly it indicates:

- Capacity nor incapacity to bear additional risks by a commercial bank,
    - The limits for making provisions for uncertainties.

(3) Cost of Deposits

The ratio of total annual interest paid on all deposits to the total deposits is normally called the cost of deposit. Finer variations and micro-level calculations, many a time, influence the cost of deposits. However, for external analysis, the cost of deposits is an approximate of performance efficiency. Deposit mobilization, the most significant aspect of banking business, certainly affects the cost of deposits. Another aspect having important impact on the cost of deposits has been proportion of demand and time liabilities. It is a matter of observation that whenever the proportion of demand liabilities exceeds that of time liabilities, the cost of deposits is likely to taper down.

(4) Return on Advances

In case of banking business, major and predominant portion of assets comprise loans and advances outstanding. The annual interest thereon cannot be deemed as profit but merely as return. The return on assets, being greater than the cost of deposits, is subject to a number of risks like credit and interest risks. For external analysts, the impact of these risks is not assessable.

(5) Advance Deposit Ratio

This is another most common indicator of volume of business taking both deposits and advances into consideration. It is more realistic and factual than credit-deposit ratio. Dr. Kaveri (5) in his appreciation of this ratio observed, “The ratio of advances to deposits describes the key factors of banking business wherein both the deposits and advances require hard work for long time by banking personnel. Without customer relationship banks cannot collect deposits not can viably advance money to the borrowers”. Its numerator and denominator need be seriously taken into account for proper planning and control.

Data Analysis and Interpretation

Secondary data relating to operational performance of these two commercial banks was culled from the financial statements published in the NSE websites since both are the listed companies in both exchanges. Hence, reliability and authenticity of figures are beyond question. The ratios discussed earlier now have been dealt with for assessing their financial performance.

(1) Interest Received to Interest Paid Ratio (IRIPR)

Unquestionably, a profit earning commercial bank has the interest received to interest paid ratio higher than the unity. This is rightly evident from the figures presented in Table 2. The observations are as under.

able: 2 IRIPR

NO	Year	INTEREST RECEIVED/ INTEREST PAID		ADVANCES / DEPOSITS	
		SBI	ICICIB	SBI	ICICIB
01	**2011**	**1.23**	**1,45**	**0.73**	**0.69**
02	**2012**	**1.39**	**1.52**	**0.70**	**0.65**
03	**2013**	**1.41**	**1.61**	**0.72**	**0.68**
04	**2014**	**1.40**	**1.68**	**0.75**	**0.69**
05	**2015**	**1.23**	**1.74**	**0.72**	**0.64**

- In the case of the State Bank of India, IRIPR was as good as 1.23 which started declining in subsequent years; during 2012,2013 and 20115 it went down marginally; a steep fall to 1.34 was recorded in the year 2015 quite before the outbreak of Covid-19;

- On the other hand, the ICIC Bank had IRIPR little higher than that of the State Bank of India in the year 2011 which was about 1.45 with continuous upward trend, and passed over the SBI ratio;
- The rate of increment in the IRIPR of the State Bank of India was certainly the matter of deep concern, and if it was not timely controlled, it may be disastrous for the bank;
- The rate of enhancement in the IPIPR of the ICIC Bank was obviously gratifying, and if the spree continued, it would make a history when it would touch the figure of 2;
- The quinquennium mean of IRIPR in case of the State Bank of India arrived at 1.38, while in the case of ICIC Bank it was 1.65
- As regards, Advances to Deposit Ratio (ADR) is concerned it was about 0.75 in the year 2011 for the state Bank of India and 0.69 for the ICIC Bank; the latter was lower as compared to the former;
- The ADR in respect of the State Bank of India continued to remain by and large stagnant as it varied between 0.73 in 2011 to 0.72 in 2015 indicating that its advancing activities were in corresponding with the deposit mobilization
- The ICIC Bank, on the other hand, had the ADR as high as 0.69 in the year 2011 and started continuously falling in the following years, and touched the figure of 0.67 in the year 2015, demonstrating the similar business strategy with SBI,;
- The ADR of ICIC bank had been, during the period under review, always lower than that of State Bank of India;
- The quinquennium average of the ADR in respect of the State Bank of India was approximately 0.73 as against 0.68 of the ICIC Bank.

Interpretations

The stability of the ADR in respect of both the banks clearly shows that both deposit mobilization and credit dispensation had been nicely tuned with each other in both banks.. In the light of observations made earlier that the percentage increase in the deposits

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during the period under study in respect of both the commercial banks had been higher than their respective percentage increases in advances, as depicted below:

Change in percentage	SBI	ICIC B
Increase in Deposits (%)	25.3	22.2
Increase in Advances (%)	21.8	20.5

(2) Interest Contribution Ratio

In evaluating the operational performance of a commercial bank this ratio has never been put into the use. Verily, this ratio formed on the line of contribution ratio in management accounting has been deemed to be reasonable useful. It ostensibly indicates to what extent revenue income is available to meet the expenses. M.V. Kamath (6) the erstwhile CEO Corporation Bank, remarked, "The current cash capacity to meet monthly revenue expenses banks should have to measure the interest contribution ratio on monthly basis. It provides a measure to plan for current liquid resources". As the ratio moves upward, the bank garners sufficient margin to meet current expenses.. The Table 3 patently shows the ratio in respect of both ten State Bank of India and the ICIC Bank.

Table 3: Interest Contribution Ratio (ICR)

NO	Year	(IR – IP)/ IR x100	
		SBI	ICICIB
01	**2011**	**32. 1**	**35,8**
02	**2012**	**32.5**	**35.1**
03	**2013**	**33.9**	**38.2**
04	**2014**	**36.3**	**40.5**
05	**2015**	**38.1**	**44.4**

Observations

- In case of the State Bank of India the ICR was 32.1per cent in 2011 that marginally surged up to 38.1 per cent in the year 2015;

- The ICR relating to the ICIC Bank moved from 35.8 per cent in 2011 to 44.4 per cent at the end of 2015;
- For all the years under study, the ICR in respect of the ICIC Bank had always been marginally higher than that in respect of the State Bank of India;
- The quinquennium average of ICR for the State Bank of India was around 34.6 per cent with the associated standard deviation of 1.4, while ICIC Bank had achieved the ICR of 38.8 per cent with associated standard deviation of 4.7 showing higher variability.

Interpretation

The ICR of the State Bank of India was far from satisfactory and had been, by and large, remained stagnant. Seeing its resources, its ICR should have been more than 50 per cent. In contrast, the ICIC Bank have had comfortable cushion due to high ICR.

(3) Cost of Deposits

On account of non-availability of information relating to the structure, periodicity, and kinds of deposits, interest rate structure, etc., it would not be feasible to work out the cost of deposits (COD) as exactly as possible. Hence, on the basis of published data, the COD was worked out by a ratio of interest paid on deposits to total deposits outstanding. Table 4 furnishes its percentages in respect of both the banks,

Table 4: Cost of Deposits and Return on Advances

NO	Year	IP/ DEPOSITS		IR/ ADVANCES	
		SBI	ICICIB	SBI	ICICIB
01	**2011**	**8.6**	**5.7**	**9.8**	**11.6**
02	**2012**	**8.3**	**4.7**	**10.1**	**11.9**
03	**2013**	**9.1**	**6.3**	**10.8**	**12.5**
04	2014	**9.7**	**6.9**	**10.1**	**11.6**
05	201 5	**9.5**	**6.1**	**9.5**	**10.3**

Observations:

- COD in respect of the State Bank of India was to the tune of 8.6 per cent in the year 2011 and surged marginally to 9.5 in the year 2015; it touched the mark of 9.7 per cent in the year 2014 but receded in the following year;
- In respect of the ICIC Bank, it was about 5.7 per cent in the initial year and remained more or less stagnant during the quinquennium;
- Interestingly, the five year mean 0f COD of the ICIC Bank was 5.9 per cent which was comparatively lower than that of the State Bank of India showing the mean of 9.1 per cent ; however, the rate of change over the period was minimal;
- Thus low cost of funds in the case of the ICIC Bank appears salutary; and
- The five-year average of COD in respect of the State Bank of India was around 9.1 and that of ICIC Bank, 5.9 per cent..

Interpretations

The average percentage of COD of the State Bank of India was almost double of the average of the ICIC Bank, The former obtains funds by way of deposits at double the cost of the ICIC Bank. The possible reason behind the high cost was relatively high proportion of long term time deposits.

(4) Return on Advances

Table 4 given above contains the data regarding the return on advances (ROA) which was calculated by dividing the annual interest earned with the total advances outstanding. What the Table 4 tells that the five-year mean return on advances in respect of the State Bank of India was 10.2 per cent while it was 11.5 per cent for the ICIC Bank ;

		COD		ROA
State Bank of India	(%)	9.1	<	10.2
ICIC Bank	(%)	5.9	>	11.5

It is fascinating to note that the average cost of deposits in respect of the State Bank of India was around 9.1 per cent as against 5.9 per cent in case of the ICIC Bank. But the State Bank of India had the return on advances as low as10.2 per cent against 11.5 per cent gained by the ICIC Bank. Finally, it appears anomalous that the COD was greater than ROA in the State Bank of India and less than ROA in the ICIC Bank. The operational performance of the private sector bank, thus, had been highly viable than the public sector bank.

Conclusions and Suggestions

The performance of the State Bank of India from the angle of cost of deposits and return on advances provides a little consolation as compared to the ICIC Bank. In addition, The latter could develop adequate resources for meeting the revenue expenses since its contribution was around 43.77 per cent as against 35.69 per cent of the State Bank of India. All this happened when both the banks registered almost similar rates of increment in their deposits and advances.

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