Chapter - IX

FINDINGS AND SUGGESTIONS

This chapter summarises the major findings and offers a few suggestions for improving the overall performance of the select banks in Tamilnadu.

Findings

Based on the analysis of each element of CAMEL, the major findings are listed below, under the following heads.

1. Capital adequacy
2. Assets quality
3. Management efficiency
4. Earnings quality
5. Liquidity management and
6. Overall ranking of CAMEL ratings.

Capital adequacy

- In the initial periods of introduction of prudential norms, the importance attached to T II capital base was not at the significant level in CUB and LVB whereas IOB maintained a consistency throughout the period of study among T I and T II capitals. IOB ranged between 34.28 per cent and 48.41 per cent regarding its dependence on T II capitals on CAR over the study period. Whereas, the range of CUB rose from 0.42 per cent to 21.51 per cent and of LVB from zero per cent to 49.91 per cent. This
showed that T II capitals rendered maximum support to IOB and minimum to CUB. Even though LVB had no T II capital in 1998-99, its share on CAR reached the mark of 49.91 per cent during 2004-05 and gradually it reduced the dependence to 17.28 per cent in 2007-08. During the study period the average of the CAR of IOB was 11.66 per cent, while it stood at 13.21 per cent in the case of CUB and the same was 11.43 per cent in LVB.

- The new avenue ‘Innovative Perpetual Debt Instrument’ for enhancing the Tier I capital was utilized by IOB during 2006-07 to the tune of Rs.1000 crores.

- The trend related to the sources of working fund of the banks projected a manifold increase in terms of accumulated total funds and trend percentage. The differences in the degree of movement of trend in the banks referred to were gradual till 2004-05 whereas it spurted heavily during the last three years because of aggressive deposit mobilization.

- The accumulation of working funds of IOB was notable touching the mark of 93.65 per cent in the year 2007-08 and in the same year CUB’s percentage in this regard stood at 140.94. In case of LVB it was 48.99 per cent in the year of 2006-07. All the above year’s figures had crossed the respective previous year’s performance by percentage. This spectacular performance was due to aggressive deposit mobilization.

- Though the share capital is the base source of working funds, almost all the banks utilized more or less 1 per cent of it. But the banks are holding
deposits around 87 per cent. The other three sources viz., borrowings, reserves and other liabilities share the remaining 12 per cent of working funds.

- The averages of debt to total funds ratio revealed that their mobilization was utilized to the larger extent to enhance the profitability. This leads to the perception that the owned funds possessed by the banks were 4.22 per cent, 7.08 per cent and 6.23 per cent IOB, CUB and LVB respectively.

- From the analysis of investment in government securities to total investments ratio, all the three banks heavily depended on risk-free government investment. During the last three years of the study period, the performance of all the study units varied heavily in proportion to others years.

- All the banks’ sources revealed that their share capital holdings are very meagre and minimum when compared with debt content. The manifold debt proportion with equity exhibited its strength of the financial base. The averages of debt equity ratio of IOB, CUB and LVB during the decade fetched 2099.99 per cent, 1112.93 per cent and 1342.57 per cent respectively. Thus, all the banks are sufficiently levered by means of debt

**Assets quality**

- The analysis of deployment of working funds revealed that the averages of cash holdings were around 10 per cent for CUB and LVB. For
IOB, it was around 12 per cent. The averages of advances were ranged between 47.93 per cent and 55.67 per cent and also it was inferred that CUB and LVB utilized more than 52.84 per cent. The fund allocated in IOB was limited to 47.93 per cent. Regarding investments averages during the study period IOB achieved 36.68 per cent, CUB had 33.08 per cent and LVB’s figure stood at 29.75 per cent. All the three select study units’ averages on fixed assets were less than 1 per cent. Their other assets holdings were between 2.24 per cent to 3.82 per cent which was around three times of fixed assets.

- The loanable funds and actual lending ratio revealed that the intensity and interest in utilizing funds were augmented during the later part of study period. But, the averages revealed that 72.82 per cent, 78.35 per cent and 83.50 per cent were the respective lending achievements made by IOB, CUB and LVB. Further it indicates that the remaining portions of the funds were utilized for other purposes.

- It is perceived from the investible funds and actual investments ratio that the interest of all the study units during the initial years was lower than the same in the middle years and it reduced during the later years because of increasing trend of advances and cash balances. It was also clear that from 2004-05, the investible percentages of all the banks were reduced which had an impact on advances. The average of the decade of IOB was 180.42 per
cent and it was 140.35 per cent for CUB. The same was 129.16 per cent for LVB.

- The averages of fixed assets ratio of the study units were 18.62 per cent, 10.88 per cent and 11.90 per cent for IOB, CUB and LVB respectively. This revealed that only a meagre portion of long-term funds were utilized for fixed assets and the remaining amounts were diverted towards current assets and to meet out timely demands of deposit holders.

- From the analysis of gross NPAs to total assets it is perceived that private sector banks started to implement the prudential norms from 2001-02 only whereas IOB strictly implemented it from the time when the concept of prudential norms were introduced in India. The inverse movement of gross NPAs with total assets showed the right managerial attitude of banks to move ahead with RBI.

- Analysis of net NPAs to net advances revealed that the intention to curtail the NPAs movement got hold of its importance from 2003-04 in the case of IOB and from 2004-05 onwards in the cases of CUB and LVB. This movement revealed that in spite of aggressive lending policy and huge amount of advances, the cautious approach from 2004-05 onwards can also be understood.

- Gross NPAs to total assets, gross NPAs to gross advances and net NPAs to net advances showed that the awareness on controlling the NPAs developed after 2001-02 only whereas acute competition and enormous
advances during the last three years hiked these ratios to some considerable extent.

**Management efficiency**

- The branch expansion was positively correlated with total deposits and total advances which exhibited their development in the regular banking activities. In the case of net profits, except LVB, the other two banks positively correlated. The negative correlation that occurred between branch expansion and net profits of LVB was disturbed due to competition and operational inadequacy.

- The overall averages of ratios of advances to deposits stood at 55.15 per cent, 60.35 per cent and 64.45 per cent in case of IOB, CUB and LVB respectively. This tends to propagate their cautious steps towards allocating funds for granting advances. The performances from 2004-05 onwards were notable. The nature of such performance can be considered in the future for extending their services.

- The analysis revealed that the total business and business per employee increased during that decade irrespective of number of employees. The study period average of IOB was Rs.2.80 crores and CUB was Rs.3 crores, while LVB's average was 2.74 crores. These averages were achieved by the concerned banks during the second half.

- It is perceived from the analysis of profit per employee that the averages of the decade for IOB (Rs.2.05 lakhs), CUB (Rs.2.79 lakhs) and
LVB (Rs.1.24 lakhs) reveal that CUB performed in a better way. IOB and CUB were able to exceed the decade’s average from 2003-04 onwards whereas LVB achieved this from 1999-00 to 2003-04 and in the remaining period its ratio was less than the averages. From 2004-05 onwards, profits of LVB declined with a range from Rs.334 lakhs to Rs.2527 lakhs which is due to the changes in interest expended and operating expenses.

- Spread per employee of IOB and CUB showed its positive progress but some marginal shortages were found in the trend of LVB. Being a big nationalized bank, the quantum of IOB’s spread amounts was high when compared with the other two bank’s spread amount. Apart from this, from 2003-04 onwards decades’ averages were crossed by IOB and CUB and the LVB chased it during 2004-05 and onwards.

- It is known by the tri-segment analysis of interest on deposits per employee that initially the liberalization impact did not change the course of regular business but during the second segment, fluctuations were found to be the result of competition and in the last segments were led to a remarkable performance owing to the acute stress on the mobilization of deposits. The average figures of IOB, CUB and LVB are of Rs.9.54 lakhs, Rs.1.83 lakhs and Rs.10.64 lakhs respectively. The suggestions got from these figures make CUB eligible for first place and IOB for third place.

- Ratio of interest on borrowings per employee revealed that IOB’s dependence on borrowings was increased from 2003-04 onwards. LVB’s
borrowings were high and stooped down to some extent during the other years. The managerial ability of LVB to meet out its contingencies is revealed by this trend.

- The accumulation of operating expenses of three banks witnessed an increasing trend during the decade except the LVB’s operating expenses by Rs.9.43 crores during 2006-07 over the year 2005-06. As regards ratios, LVB’s position during the last two years declined marginally over 2005-06. All the three banks’ averages were attained during the last four years only.

- During the study period the average ratio of employees’ expenses per employee for IOB was Rs.3.05 lakhs. Rs.1.84 lakhs was the average of CUB and Rs.2.38 lakhs was the average of LVB. The select study units employees’ expenses were below the averages for 5 years in case of IOB and LVB and 4 years in the case of CUB. In this aspect CUB ranked first, LVB got the second and IOB the third place. The cost inflation index increased from 351 points to 551 points during the study period. Almost all the banks’ allotment on employees’ expenses doubled in terms of ratio which is justifiable one from employees point of view and acceptable from the management’s point of view.

**Earnings quality**

- From the ratio of interest earned to working funds, it is perceived that performance of all the banks increased over the respective previous years’ due to interest on loans and advances. But, during the second half of the
study period conservative approach was followed by all banks in selected factors.

- The managerial ability of all the banks were understood from the ratio of interest paid to working funds because they maintained it normally throughout the study period except during 2007-08. The payment of interest and working funds shot up exorbitantly in the entire period due to competition and enhanced quantum of deposit mobilization.

- The movements of interest paid and interest earned had its deep impact over spread and the ratio on spread to total assets. This may be proved by deducting the averages of ratios on interest paid to working funds and interest earned to working funds of all the select banks.

- The analysis of ratio of net profit to interest earned exhibited that IOB and CUB maximized their net profits during the later years and LVB lost its ability from 2004-05 due to reduction in other income and interest expended, though there was a hike in interest earned and operating expenses.

- The average ratios of net profit to total deposits were 0.99 per cent, 1.49 per cent and 0.85 per cent for IOB, CUB and LVB respectively which were more than the year-wise performances of 6 individual years of the study period. The impact of spread movement is exhibited in this ratio.

- A comparative analysis between ratio of net profits to total deposits and net profits to working funds revealed a significant relationship between
these two because the banks are depending on deposits for working funds around 87 per cent.

- On the whole, the analysis of earnings quality reveals that the profit earning capacity of LVB has been reducing when compared with the profit earning capacity of IOB and CUB.

Liquidity management

- Regarding current ratio, IOB never reached the standard ratio 2:1. Further, the current ratio analysis revealed that IOB and CUB kept a huge amount as cash whereas LVB utilised them for purchasing and discounting bills and cash credits, overdrafts and loans repayable on demand. All the study units continuously increased their commitment on cash credits, overdrafts and loans repayable on demand.

- During the first three years, maximum were attained pertaining to liquid assets' proportions to total assets. Such level exhibited the planned and careful approach towards keeping cash in their custody. Discussions with the officials of select banks suggested that around 7 per cent to 8 per cent is enough for maintaining liquidity.

- Maximum ratio of liquid assets to demand deposits revealed the strength in meeting out day-to-day commitments without much fluctuation. During competitive era risk-taking attitude of these banks can be understood by means of their hedging approach in this aspect.
• Total deposits of all the select banks progressively increased during the decade. At the same time, the cash holding kept by banks was the maximum in 1998-99 and the minimum in 2005-06.

• Cash flow movements of the three banks were to depend upon operating liabilities and operating assets’ position. The reflections of remaining factors were nominal.

**Over all ranking of CAMEL ratings**

• Analysis of ranking of CAMEL ratings reveals that gross total points of capital adequacy scored by CUB, LVB and IOB were 9 points, 13 points and 14 points respectively.

• In the case of maintaining assets quality IOB has achieved the first position by leaving LVB and CUB for second and third ranks.

• The talent and supremacy in establishing management is well understood from this analysis. In this aspect, CUB secures 11 points out of 54 points setting a difference of 9 points between it and LVB which is in the second place. IOB goes to have the third place in the above aspect.

• Earnings quality depicts that CUB’s attitude towards enhancing quality is the highest of all the select banks. Hence it has been set for first rank and LVB for the third rank.

• By maintaining effective liquidity, IOB is eligible for first rank while CUB and LVB in above aspect are drawn for second and third rank.
• On the basis of this overall ranking, CUB is ranked above the other two and placed in the first slot. The second and the third ranks go to IOB and LVB respectively.

Suggestions

On the basis of the above observations derived from the study, the following measures are suggested to improve the operations of the select banks.

Capital adequacy

• The awareness on maintaining T II capital can be created.

• RBI’s restriction on mobilising funds may be relaxed for increasing T II capital.

• New avenues for enhancing the T I as well as T II capital can be used because those instruments have similarities to equity. As they are able to avert losses on the ongoing business without triggering liquidation, they may be included in T II capital.

Assets quality

• It is better for the banks to hold optimum cash balances by trading-off between liquidity and profitability.

• Investments in government securities can be reduced because they give minimum return. Further investments have to be contained within the investible portion.
• Diversion of loanable funds can be restricted towards current assets which cater to the demand of deposit holders. Loanable funds can be utilized fully to stabilize the basement with futuristic vision.

• Precautionary measures may be taken to avoid addition of fresh NPAs. In order to ensure more standard accounts, precautionary measures may be adopted to select the borrowers so as to make the loan recovery process viable and to get disburse the loans within the given time.

Management efficiency

• To increase the total business, in addition to adequate number of employees, new products like insurance linked deposit schemes, zero balance facilities, fund transfer from one account to another without any restrictions, utilizing technological developments and providing other new service can be effectively implemented. Such steps will help to enrich the existing level of operation.

• To minimize the operating expenses and increase profitability, more branches with adequate modern facilities can be opened and the strength of the staff can be increased to keep pace with the expansion.

• By streamlining the interest expended and sources of earning interest, the spread can be increased. In this aspect, the higher interest earning avenues may be utilized instead of diverting more on investment which is a secured one but low profitable option.
- The establishment expenses which are the second largest item of total expenditure can be divided into controllable and non-controllable. By means of mutual agreement between trade unions and banks, productivity criteria can be fixed to attain higher business which may reduce the cost of establishment to improve the profitability.

**Earnings quality**

- All the funds can be utilized to enhance the existing profit earning capacity without keeping any amount as idle.
- The interest on deposits can be reduced by enhancing current accounts and savings bank accounts because the cost of these deposits is less when compared with recurring and fixed deposits.
- Increasing the sources of interest earnings and reducing the interest payment by improving operational performance would be the suggestion to increase and strengthen the spread.
- The profit may be increased by controlling the cost and enhancing the earnings through improving their operational efficiency.

**Liquidity management**

- Perfect synchronisation between cash inflows and cash outflows is necessary to avoid problems affecting liquidity.
- Efficient management of operating liabilities and operating assets will further improve the liquidity of the select banks.
Scope for further study

The following are a few areas of further research which can be pursued by the interested researchers.

2. A study on accommodating the price level adjustments to the financial aspects of banking.
4. Liquidity risk analysis of commercial banks.
5. A study on the implementation of cost control techniques and its effects on profits.
8. An analysis of the impact of development banks’ entry in commercial banking operations.