Chapter X

SUMMARY OF FINDINGS AND SUGGESTIONS

In this chapter, an attempt is made to make a summary of the major findings of the study and also to suggest suitable suggestions for further improving the operational efficiency and risk management of Old Private sector Banks (OPBs) in India, particularly the Kerala-based OPBs (KOPBs, in short). Part – I of the chapter gives a summary of the major findings. Part – II gives the suggestions for improvement of the performance of (i) OPBs in general, (ie. General Suggestions); (ii) KOPBs in general, and (iii) each of the four KOPBs in particular (ie. Specific Suggestions).

Part – I

SUMMARY OF THE MAJOR FINDINGS

10.1. Financial Position of Old Private Sector Banks: Overall Position

Among the OPBs in India, Tamilnadu Mercantile Bank (TMB) is the best bank in respect of financial condition as evidenced by the highest CAMEL ranking. Secondly comes another Tamilnadu based OPB viz. Karur Vysya Bank (KVB), while the third position goes to City Union Bank (CUB). Fourthly comes Jammu & Kashmir Bank (JKB). It may be noted that none of the four Kerala-based OPBs (KOPBs) figure in the first four OPBs as above which represent the ‘Excellent’ category banks falling in the top 25 percent as per the CAMEL rankings (First quartile, with CAMEL ranking upto 6.57).

Among the OPBs, the worst performance is that of Bank of Rajasthan (BOR) as is evidenced by the least CAMEL ranking. The second worst performer is a KOPB, viz. Catholic Syrian Bank (CSB), while the third worst performer is ING Vysya Bank (IVB). The fourth from the last is another KOPB viz. Dhanalakshmi Bank (DB). All these four banks fall under the ‘Poor’ category (Fourth quartile, last 25 % with CAMEL ranking over 9.45). It may be noted that two out of the four KOPBs viz. CSB and DB fall under this ‘Poor’ category banks.
Three banks including one KOPB viz. Federal Bank (FB) fall under the ‘Good’ category banks (Second Quartile, between 25% to 50%, with CAMEL rankings between 6.57 to 8.01). The other two banks in this ‘Good’ category are Nainital Bank (NB) and Karnataka Bank (KKB), in that order. It may further be noted that the KOPB named FB is the first (top most) in this group of three ‘Good’ category banks.

Four banks fall under the ‘Fair’ category (50% to 75% group, with CAMEL rankings between 8.01 to 9.45). These four are Lakshmi Vilas Bank (LVB), Ratnakar Bank (RKB), SBI Commercial and International Bank (SBC) and South Indian Bank (SIB), in that order. One KOPB viz. SIB is falling in this group of ‘Fair’ banks. But, it may be noted that SIB is the last bank (bottom most) in this group of four OPBs.

10.2. Financial Position of Kerala based Old Private Sector Banks (KOPBs)

It is worth noting that none of the four KOPBs are in the ‘Excellent’ category banks. But among the four KOPBs, Federal Bank (FB) is quite significantly superior to others. FB is the first in the ‘Good’ category banks. The second best KOPB is South Indian Bank (SIB); and is falling in the ‘Fair’ category of banks, as the last member (bottom most) in that group. Thus, SIB is distantly following FB among the KOPBs. The remaining two KOPBs viz. Dhanalakshmi Bank (DB) and Catholic Syrian Bank (CSB), are both falling in the ‘Poor’ category banks – the group of the least performing banks. Among these two banks, DB is relatively superior as it is the first member out of the four banks in ‘Poor’ category whereas CSB is only in the third position (or, second from the last).

In short, the overall position of KOPBs is not very encouraging among the OPBs in India. Yet, the position of FB is relatively good and that of SIB is somewhat satisfactory. Position of both DB and CSB are unsatisfactory, and that of CSB in particular is rather miserable. As such, there is significant difference between KOPBs in their financial position.
10.3. Profitability of Kerala based Old Private Sector Banks (KOPBs)

Profitability of all OPBs (and also NPBs, the New generation Private sector Banks) measured in terms of Operating Profit to Total Assets (OPR), is significantly and positively influenced by non-interest income. Thus, higher non-interest income leads to higher OPR and vice-versa. Or, in other words non-interest income is a significant driver of the overall profitability of OPBs. But, in respect of Catholic Syrian Bank, the evidence in this regard is less prominent, though it is obvious.

In respect of Federal Bank (FB), investments in government securities is also contributing positively towards profitability. For FB, priority sector advances may adversely affect its profitability, though the evidence is not very strong.

In general, factors like (i) relative share of priority sector advances, or (ii) relative intensity of the rural (and semi-urban) branches, or (iii) investments in government securities, or (iv) size of the total assets is not significantly affecting the profitability of any of the OPBs or even NPBs. The case of KOPBs is also similar, except the slight evidences to the contrary as noticed in the case of FB, as already noted above.

10.4. Efficiency of Kerala based Old Private Sector Banks (KOPBs)

In general, investments in government securities is having an adverse (negative) impact on the efficiency of OPBs as measured in terms of NIM (Net Interest Margin). As against the popular perception, the intensity of rural (and semi-urban) branches in the total branch network is positively contributing to NIM. That is, higher the rural presence, higher the NIM and vice versa. Though this general trend is evident for all OPBs and also NPBs, Federal Bank (FB) is an exception in this regard as it does not show any such correlation.

In respect of FB, non-interest income is positively influencing NIM whereas in respect of Dhanalakshmi Bank (DB) it is the size of Assets that is influencing NIM. Share of priority sector advances is not at all a determinant of NIM, in respect of all OPBs and also NPBs. There is no exception in this regard.
10.5. **Impact of Technology on Efficiency and Risk Management of KOPBs**

Technological change is having a strong and positive influence on non-interest income of OPBs. That is, higher investments in technology may improve the non-interest income of OPBs. There is no exception to this general observation. On the other hand, technological change is associated with an adverse (negative) impact on net-interest income of OPBs, in general. This may be because of the higher interest burden associated with huge investments in technology affecting the net interest income of banks. However, the second observation as above is not supported by FB and SIB.

Higher net-interest income may result in higher share of non-performing assets also. That is, it may reduce the quality of assets. This may be because of the fact, that aggressive lending may bring in higher interest income, but dilution of due diligence that is often associated with aggressive lending may result in higher NPAs, thus adversely affecting the asset quality. This finding is, however, not supported by SIB.

Higher variability on earnings (risk taken by banks) may positively result in higher net interest income in general, as per the economic theory and also as per the evidence from the figures relating to all OPBs. This finding, however, is supported by only one KOPB, viz. Dhanalakshmi Bank, and to a some extent by SIB also.

**Part – II**

**SUGGESTIONS FOR IMPROVEMENT OF PERFORMANCE OF OPBs**

10.6. **General Suggestions: Applicable to All OPBs in India**

(i) For improving their profitability, OPBs in India need to concentrate on increasing the non-interest income. For augmenting non-interest income, OPBs may focus on various fee-based activities. In the current deregulated environment the above suggestion makes sense as margin from fund-based business is growingly under the competitive pressures. Moreover, for augmenting their non-interest income OPBs may invest more on advanced technology as there is a strong and positive correlation between the two. [See, suggestion (iv) below.]
(ii) Investments in government securities may adversely affect the operational efficiency and credit risk management (measured in terms of NIM). Accordingly, higher exposure to government securities may result in lower operational efficiency and also riskier credit management. Thus, OPBs need to curtail excessive investment in government securities and limit the same to the minimum level, like to maintain SLR requirements.

(iii) Rural branches, in general, are good for maintaining higher efficiency in operations and hence better management of credit risk. This may be because of the fact that such branches ensure higher proportion of core deposits and advances which in turn are less vulnerable to market forces. Thus, OPBs may focus more on rural branches and open more such branches, if otherwise feasible.

(iv) As technological change has got a strong and positive association with higher non-interest income, OPBs have to invest more in modern technology to augment their non-interest income. This in turn has got a direct and positive impact on their operating profits as well. [See, Suggestion (i) above].

(v) Technological change may sometimes result in a drag in the net interest income of OPBs, in spite of the higher non-interest income as noted in suggestion (iv) above. This may be because of the high interest burden arising from the huge investments in advanced technology. However, considering the relatively short-term nature of the adverse impact on net-interest income as against the long term benefits accruing from it in the form of higher non-interest income and also higher operating profits, investments in technology is always appreciable.

(vi) As higher net-interest income is also associated with higher level of NPAs (ie. lower asset quality), it is essential to have adequate due diligence even when adopting an aggressive policy towards lending. Accordingly, higher NPAs accompanied with higher net-interest income needs to be controlled. A risk taking attitude (higher variability in returns) may improve net-interest income.
10.7. **Specific Suggestions for KOPBs: Applicable to All KOPBs**

(i) Financial position of all KOPBs need further strengthening. For FB, a reasonable improvement in financial position would enable it to become one of the ‘Excellent’ category OPBs in India, as it is already the best among the ‘Good’ category. For SIB, concerted attempt is required to catch up, at least to the level of ‘Good’ category banks, if not ‘Excellent’ category. This is because, it is at present the worst among the ‘Fair’ category OPBs. For DB and CSB, both of which are in ‘Poor’ category at present, very stringent financial controls for boosting profitability, and measures for augmenting capital for attaining higher capital adequacy may be required to tide over the current miserable situation.

(ii) Boosting non-interest income primarily through investment in modern technology is good for all KOPBs. This in turn would improve their profitability through bringing in higher operating profits.

(iii) Investments in government securities be maintained at the minimum level by the KOPBs, because their net interest income may be adversely affected otherwise.

(iv) More focus on rural branches including opening of more such branches if otherwise feasible, and also launching specialised products for the rural masses etc. would improve their net-interest margin further. Thus, rural focus may help higher efficiency and also better management of credit risk.

(v) An aggressive and risk-taking approach to lending is good as it may improve both net-interest income and non-interest income. But, this may also lead to higher level of NPAs (ie. lower asset quality), and as such due emphasis on due diligence is essential for ensuring quality of assets and controlling NPAs.

(vi) None of the KOPBs have financial soundness comparable with the ‘Best in the Class’ viz. Tamilnadu Mercantile Bank (TMB). Moreover, none of them except Federal Bank (FB) is comparable with even the average financial position of the OPBs in India. Thus, the financial soundness of KOPBs is quite poor, in general.
10.8. **Specific Suggestions: Federal Bank (FB)**

(i) FB is already the best among the ‘Good’ category banks. As such, a little more focus on its financial condition (like, added capital, higher operating profits etc.) may enable it to become an ‘Excellent’ category bank.

(ii) Boosting non-interest income primarily through investment in modern technology is good for FB also, as is the case with all OPBs. This in turn would improve its profitability through bringing in higher operating profits. Moreover, in the specific case of FB, technology is observed not to have any negative impact on net interest income. Thus, technology is more desirable for FB.

(iii) It is noted that its investments in government securities reduce the net-interest income of FB, though it may increase non-interest income to some extent. As such, just like other KOPBs, for FB also it is advisable to limit its investments in government securities, for enhanced efficiency and credit risk management.

(iv) For FB, it is noted that rural branches and priority sector advances are not contributing towards either net interest income or non-interest income. Rather, its priority advances has got a negative association with operating profits also. Thus, it is advisable for FB to limit both, rural branches and priority advances.

(v) The net-interest income of FB is positively associated with its NPA level. As such, even while following an aggressive approach towards advances, a tighter control over asset quality (like, more thrust on due diligence) is quite essential.

(vi) In the specific case of FB, higher regulatory cost is positively associated with its earnings. As such, efforts to augment its regulatory capital (ie. increasing the capital base) is quite desirable for FB. This would boost its capital adequacy position, financial stability and would further improve its CAMEL ranking.

(vii) FB is the only bank among the KPOBs that has got financial soundness that is comparable with the average of OPBs in India. However, just like other KPOBs, FB is nowhere when compared with the ‘Best in the Class’ bank viz. TMB.
10.9. **Specific Suggestions: South Indian Bank (SIB)**

(i) SIB is the least performer among the ‘Fair’ category banks at present. As such, concerted efforts are required to enhance its financial condition (like, enhanced capital base, higher operating profits etc.) to enable it to become a ‘Good’ category bank, if not an ‘Excellent’ category bank.

(ii) Boosting non-interest income primarily through investment in modern technology is good for SIB also, as is the case with all OPBs. This in turn would improve its profitability through bringing in higher operating profits. Moreover, in the specific case of SIB, technology is observed not to have any negative impact on net interest income. Thus, high-end technology is more desirable here.

(iii) It is noted that its investments in government securities reduce the net-interest income of SIB. As such, for SIB also it is advisable to limit its investments in government securities, for enhanced efficiency and credit risk management.

(iv) For SIB, it is noted that higher share of rural branches can contribute more towards net interest income. As such added thrust on rural branches is advisable, including opening more such branches, if otherwise feasible. This may improve its operational efficiency and credit risk management capability.

(vi) In the specific case of SIB, higher risk appetite is positively associated with its earnings. As such, an aggressive approach to lending may add up to its earnings, both net-interest income and non-interest income. This in turn may improve its operational efficiency, profitability and credit risk management capability.

(vii) In spite of its status as a ‘Fair’ category type bank among the OPBs in India, it may be noted that SIB does not even compare with the national average for OPBS, in respect of its financial soundness. Naturally, its position is nowhere compared with the ‘Best in the Class’ (Benchmark) bank viz. Tamilnadu Mercantile Bank (TMB) as is the case with any of the KOPBs. This points to the utmost need for further enhancing its financial position and profitability.
10.10. Specific Suggestions: Dhanalakshmi Bank (DB)

(i) DB is one of the worst performers among the OPBs in India, in spite of the fact that it ranks first in that category ('Poor'). Accordingly, very sincere efforts are required to upgrade its financial position (by enhancing its capital base, improving its profitability through cost control as well as augmenting fee-based and other non-interest incomes). This may help it to upgrade its position to ‘Fair’ category with relative ease, and eventually to ‘Good’ category in due course.

(ii) Boosting non-interest income primarily through investment in modern technology is good for DB also, as is the case with all OPBs. This in turn would improve its profitability through bringing in higher operating profits.

(iii) It is noted that its investments in government securities reduce the net-interest income of DB. As such, for DB also it is advisable to limit its investments in government securities, for enhanced efficiency and credit risk management.

(iv) For DB, it is noted that higher share of rural branches can contribute more towards net interest income. As such, added thrust on rural branches is advisable, including opening more such branches, if otherwise feasible. This may improve its operational efficiency and credit risk management capability.

(v) In the specific case of DB, higher risk appetite is positively associated with its net-interest income. As such, an aggressive and risk-taking approach to lending may add up to its net interest earnings. This in turn may improve its operational efficiency and credit risk management capability.

(vi) The income (both, interest and non-interest) of DB is positively associated with its NPA level. Hence, while following an aggressive approach towards advances for higher earnings, a tighter credit policy (like, thrust on due diligence) is very essential. Moreover, as size of assets of DB is having a positive bearing on net-interest income, an aggressive policy towards lending makes more sense for DB.
10.11. Specific Suggestions: Catholic Syrian Bank (CSB)

(i) CSB is one of the worst performers among the OPBs in India, its position being the second worst among all OPBs in India. Among ‘Poor’ category banks, only Bank of Rajasthan (BOR) is worse than CSB. Thus, all the other 13 OPBs under study are having a better financial condition than CSB. Naturally, very sincere and earnest efforts are essential to tide over from the current miserable situation and hence to upgrade itself at least to the level of a ‘Fair’ category bank. Urgent measures for improving its financial position (by enhancing its capital base, improving its profitability through cost control, augmenting fee-based or other non-interest incomes etc.) are very much required for CSB for its survival.

(ii) Boosting non-interest income primarily through investment in modern technology is good for CSB also, as is the case with all OPBs. This in turn would improve its profitability through bringing in higher operating profits.

(iii) It is noted that its investments in government securities reduce the net-interest income of CSB. As such, for CSB also it is advisable to limit its investments in government securities, for enhanced efficiency and credit risk management.

(iv) For CSB, it is noted that higher share of rural branches can contribute more towards net interest income. As such, added thrust on rural branches is advisable, including opening more such branches, if otherwise feasible. This may improve its operational efficiency and credit risk management capability.

(vi) The earnings (both, net-interest income and non-interest income) of CSB are positively associated with its NPA level. As such, even while following an aggressive approach towards advances for higher earnings, a tighter control over asset quality (like, more thrust on due diligence) is very essential for CSB.