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Website

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A STUDY ON MEASURING THE PERFORMANCE OF INDIAN BANKING SECTOR IN THE EVENT OF RECENT GLOBAL ECONOMIC CRISIS- AN EMPIRICAL VIEW

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ABSTRACT
When banks in almost all the countries have witnessed a severe thunder bold due to global financial turmoil, the Indian banking system has shown remarkable resilience in withstanding the impact of global financial crisis. The performance of banking sectors in the recent years have vindicated that the sector has no direct impact of global crisis and it has the capability of handling the crisis relatively better than other countries. It is still argued that the banking sector in India is well insulated and it is immune to the crisis because of well regulated banking system. In the light of the above fact this paper has made an attempt to highlight certain key parameters to evaluate the performance of the Indian banking sector amidst in the global financial turmoil. The parameters used in evaluating the performance of the banking sector of our sub- continent are Current Growth of bank credit to the private sector, Capital to risk weighted asset ratio (CRAR), Asset quality management, Classification of loan asset, Cost of funds , Return on fund and Spread, Return on asset (ROA) and Return on Equity & Procurement of capital through domestic and foreign sources,

KEYWORDS
Capital Adequacy Ratio, NPA, Spread, ROE, ROA, GDR, ADR

INTRODUCTION
When banks in almost all the countries have witnessed a severe thunder bold due to global financial turmoil, the Indian banking system has shown remarkable resilience in withstanding the impact of global financial crisis. The performance of banking sectors in the recent years have vindicated that the sector has no direct impact of global crisis and it has the capability of handling the crisis relatively better than other countries. It is still argued that the banking sector in India is well insulated and it is immune to the crisis because of well regulated banking system. In the light of the above fact this paper has made an attempt to highlight certain key parameters to evaluate the performance of the Indian banking sector amidst in the global financial turmoil.
The following selected parameters are considered to be worthwhile in evaluating the performance of the banking sector of our sub- continent.

- Current Growth of bank credit to the private sector.
- Capital to risk weighted asset ratio (CRAR).
- Asset quality management.
- Classification of loan asset
- Cost of funds , Return on fund and Spread
- Return on asset (ROA) and Return on Equity
- Procurement of capital through domestic and foreign sources

GROWTH OF BANK CREDIT TO THE PRIVATE SECTOR
Growth in bank credit to private sector plays an important role in nourishing the industries. According to RBI, the advances of all scheduled commercial banks grew at 24% till the end of 2008. The major contributor to the credit growth was corporate credit just as time deposit. The primary reason for the growth in bank credit is attributed to the non-availability of credit from other sources and so that bank credit is one of the few sources which is available at the door step of the industries.
When we compare the year 2007 to 2010 towards the disbursement of bank credit to the private sectors by taking selected countries, the following facts are revealed:

- US contribution declined from 12% to -2.7%
- France, Germany, Japan, Italy, Greece, Spain, Russia, Brazil and Mexico have struggled to maintain the growth in bank credit to the private sector.
- Almost all the countries except India and china have shown negative growth in bank credit to the private sector
- India has managed to the large extent to maintain the percentage in growth in bank credit throughout the quarters. Finally it has marginally sacrificed to the extent of 35% towards the growth in bank credit to first quarter, 25.7% of growth in bank credit to private sector has been declined to 17% in the II quarter of 2010. Though the decrement in the growth took place, Indian banking sector is no longer inferior to any other country in distributing the credit to the private sector.

CAPITAL TO RISK WEIGHTED ASSET RATIO (CRAR)
CRAR is one of the soundness indicators of banking sector; higher ratio of CRAR indicates that the bank maintains the capital adequacy position in order to meet any emergency position. The CRAR of Indian banks under Basel I framework, has shown a consistent increment since 2007, and even in the financial crisis, the

sector has witnessed a marginal increment from the year 2008 to 2009. According to Basel II norm, RBI has stipulated minimum ratio of 9% and the stipulated ratio has been met by all the banks and to say almost all the banks have been maintaining more than 9% of capital adequacy ratio in the end of year 2008 and 2009.

Generally CAR is measured through the tools Tier I & Tier II capital and risk – weighted assets. Tier I capital refers core capital i.e. paid up capital and Tier II capital refers non-core capital. In addition to that, the assets are classified according to the risk and the weightage will be given in tandem with risk. In order to measure CAR, capital funds via Tier I & Tier II capital are reflected as percentage of risk weighted assets. In case of Indian banks, core capital made up of 70% of total capital at the end march 2010. Core CRAR itself is being represented as 9.4% and 10.1% under Basel I and Basel II norms.

TABLE 1.1 SHOWING COMPONENT WISE CAPITAL ADEQUACY OF SCBS (AS AT END-MARCH) (RS IN CRORES)

Item	Basel I		Basel II	
	2009	2010	2009	2010
A. Capital funds (i+ii)	488563	572582	487826	567381
i) Tier I capital	331422	397665	333810	395100
ii) Tier I capital	157141	174916	154016	172281
B. Risk-weighted assets	3704372	4216565	3488303	3901396
C. CRAR (A as % of B)	13.2	13.6	14.0	14.5
Of which tier I	9.0	9.4	9.6	10.1
tier II	4.2	4.1	4.4	4.4

Source: RBI report on banks 2010

The above table shows that CRAR has been improved from 13.2% to 13.6% during the year 2009 and 2010 under Basel I norms and under Basel II norms, the scheduled commercial banks have shown an increment from 14% to 14.5% in the year 2009 and 2010. The contribution of Tier I capital is much significant rather than Tier II capital in measuring capital adequacy ratio indicates that the banking sector in India has shown robust fool proof in withstanding the pressures of the global financial crisis.

TABLE 1.2 SHOWING CAPITAL TO RISK WEIGHTED ASSETS RATIO – BANK GROUP – WISE (AS AT END -MARCH)

Bank Group	Basel I		Basel II	
	2009 (%)	2010 (%)	2009 (%)	2010 (%)
Public Sector Banks	**12.3**	**12.1**	**13.5**	**13.3**
Nationalised banks	12.1	12.1	13.2	13.2
SBI Group	12.7	12.1	14.0	13.5
Private Sector Banks	**15.0**	**16.7**	**15.2**	**17.4**
Old Private Sector Banks	14.3	13.8	14.8	14.9
New Private Sector Banks	15.1	17.3	15.3	18.0
Foreign banks	**15.0**	**18.1**	**14.3**	**17.3**
Scheduled commercial banks	**13.2**	**13.6**	**14.0**	**14.5**

Source: RBI report on banks 2010

The above table indicates the following facts with respect to CRAR maintained by bank group.

- In 2009, the private sector banks have maintained 15% and 15.2% of CAR under Basel I and Basel II norms. The above figure is far more than the minimum stipulation of RBI
- The public sector banks have witnessed a thin decline in terms of capital adequacy ratio in the year 2009 and 2010 under Basel I and Basel II norms. The decline is very much negligible in the event of global financial crisis

ASSET QUALITY MANAGEMENT

While the capital adequacy of Indian banks remained robust, there were some emerging concerns with regard to the second important soundness indicators of banks' Non-Performing Assets (NPA).

TABLE 1.3 SHOWING TRENDS IN NON PERFORMING ASSETS – BANK GROUPWISE

Gross NPAs as per cent of gross advances	Public sector banks	Nationalised banks	SBI Group	Private Sector Banks	Old Private Sector Banks	New Private Sector Banks	Foreign banks	Scheduled commercial banks
2008-09	**1.97**	1.73	2.46	**2.89**	2.36	3.05	**3.80**	**2.25**
2009-10	**2.19**	1.95	2.70	**2.74**	2.32	2.87	**4.29**	**2.39**

Source: RBI report on banks 2010

Asset quality of Indian banks had gradually seen a steady improvement since 1999. The gross NPA ratio of SCBs placed at 14.6% at the end march 1999 had declined steadily to 2.25% at the end march 2008. During the crisis year 2008-09, the gross NPA ratio remained unchanged for Indian banks.

At the bank group level, the gross NPA ratio was the highest for foreign banks followed by private sector banks in the year 2010. On the other hand, it was the lowest for public sector banks.

CLASSIFICATION OF LOAN ASSET

In case of classification of loan assets, public sector banks maintained 98% of standard assets in the year 2010 showing drastic improvement in terms of maintaining quality assets compared to private sector banks and foreign banks.

As far as the loss asset is concerned, public sector banks, private sector banks and foreign banks had a portion of less than 1% in their asset portfolio.

COST OF FUNDS, RETURN ON FUNDS AND SPREAD

Performance parameters during the two-year period showed that banking sector exhibited a significant improvement. The cost of funds registered a significant decline. Analysis of bank group wise performance is as follows with the table

TABLE 1.4 SHOWING COST OF FUNDS, RETURN ON ADVANCES ADJUSTED TO COST OF FUNDS & RETURN ON ASSETS - BANK GROUP WISE

Bank groups	Cost of fund (%)		Return on advances adjusted to cost of funds (%)		Return on assets (%)	
	2009	2010	2009	2010	2009	2010
SBI and its subsidiaries	5.94	5.32	3.95	3.60	1.02	0.91
Nationalized banks	6.09	5.35	4.09	3.83	1.03	1.00
Old private sector banks	6.67	6.13	5.15	4.81	1.15	0.95
New private sector banks	6.06	4.43	5.23	5.13	1.12	1.38
Foreign banks	4.46	2.82	8.14	7.17	1.99	1.26
All scheduled commercial banks	5.96	5.09	4.53	4.19	1.13	1.05

Source: RBI report on banks 2010

COST OF FUNDS

The cost of funds had come down considerably during 2009-10 although it continued to be high for all bank groups except for foreign banks. The cost of funds which ranged between 4.46% and 6.67% for different bank groups in March 2009 came down considerably and worked out between 2.28 % and 6.13% in March 2010.

Foreign banks could bring down their cost of funds from 4.46 % to 2.82% during the period, whereas the State bank group and nationalized banks could bring down their cost only from 5.94% to 5.32% and 6.09% to 5.35% respectively.

While the new private sector banks could bring down their cost of funds only by 0.54% during the period.

RETURN ON ADVANCES ADJUSTED TO COST OF FUNDS

Return on advances adjusted to cost of funds in respect of various bank groups remained in the range of 3.95 % and 8.14 % as at end March 2009 and 3.60 % and 7.17% as at end march 2010. State bank group had the lowest return on advances for both the years.

Foreign banks outperformed the entire bank groups as their return on advances adjusted to cost of funds stood at 8.14% and 7.17% as at end March 2009 and 2010 respectively. The new private sector banks also did well as compared with all other bank groups with 5.23% and 5.13% during the two years. Sustenance of this sort of return will be a major task for all bank groups in a dynamic financial market

RETURN ON ASSETS

In respect of return on assets, while the foreign bank group scored well as compared with the other bank groups, state bank group stood lowest even compared with old private sector banks.

It is noteworthy to observe that while the new private sector banks increased their return on assets from 1.12% in March 2009 to 1.38% in March 2010, all other bank groups, including foreign banks, registered a decline on their return on assets.

SPREAD

TABLE 1.5 SHOWING SPREAD - BANK GROUP WISE

Bank groups	Spread (%)	
	2009	**2010**
SBI and its subsidiaries	2.95	2.81
Nationalized banks	3.14	3.13
Old private sector banks	3.34	3.12
New private sector banks	3.77	3.99
Foreign banks	6.10	5.49
All scheduled commercial banks	3.40	3.31

Source: RBI report on banks 2010

One of the major indicators of profitability of the banking sectors namely, the spread – which is the difference between return and cost of funds. The spread of the public sector banks during 2008-09 was at 3.07% and during 2009-10 it was at 3.02%. The spread of the private sector banks during 2008-09 it was at 3.67% and during 2009-10 it was at 3.77%. The spread of the foreign banks during 2008-09 was at 6.10% and during 2009-10 it was at 5.49%. The spread of the all SCBs during 2008-09 was at 3.40% and during 2009-10 it was at 3.31%. Though there are fall in the spreads of public sector banks, foreign banks and all SCBs, the fall of spreads are marginal and they are at an optimum level. The spread of private sector banks is at an increasing point.

STEADY PROFIT GROWTH

The current economic slowdown may yet pose a challenge in sustaining this high net profit growth. However, some banks such as Punjab National Bank, HDFC Bank and axis bank, aided by a higher proportion of low- cost deposits and higher net interest margin, may be in a better position to sustain similar growth.

Higher pricing power, at a time of fund crunch, has helped banks post higher advances growth and higher yield on advances which, in turn, helped to sustain margins over the last few quarters. Further, the stimulus packages are also likely to support the credit growth. Higher margins in turn led to study profit growth.

Consider the nine months of FY 09 – net profit of 37 listed banks grew at 24%. The robust net profit growth can be attributed to a 30% growth in net interest income and 17% growth in other income.

RETURN ON EQUITY

TABLE 1.6 SHOWING RETURN ON EQUITY – BANK GROUP WISE

Bank group	Return on equity	
	2008-09 (%)	**2009-10 (%)**
Public sector banks	**17.94**	**17.47**
Nationalized banks	18.05	18.30
SBI group	17.74	15.92
Private sector banks	**11.38**	**11.94**
Old private sector banks	14.69	12.29
New private sector banks	10.69	11.87
Foreign banks	**13.75**	**7.35**
All SCBs	**15.44**	**14.31**

Source: RBI report on banks 2010

Public sector banks have shown utmost 18% of return on equity in the year 2009 which is significantly more than private sector banks and foreign banks. In general the banking sector has witnessed favourable return on equity in the year 2009 and 2010.

PROCUREMENT OF CAPITAL THROUGH DOMESTIC AND FOREIGN SOURCES

Capital market provides an important avenue to banks to raise resources for strengthening their capital base as well as to provide trading ground for banking sector stock in a liberalised and competitive environment, banks operation in the capital market have crucial implication for the growth of their banking business

TABLE 1.7 SHOWING PUBLIC ISSUES BY THE BANKING SECTOR **(RS IN CRORES)**

Year	Public sector banks		Private sector banks		Total		Grand total
	Equity	Debt	Equity	Debt	Equity	Debt	
2008-09	-	-	-	-	-	-	-
2009-10	325	-	313	-	638	-	638

Source: RBI report on banks 2010

In 2008-09 the banking sector did not tap the primary market but in 2009-10 the sector has tapped the market and mobilized the capital to the tune of Rs 638 crores, which shows that the banking sector has a scope to improve and potential to invest even in the financial crisis and as well as the public showed a strong faith on the banking system by the way of subscribing the shares in the primary market.

TABLE 1.8 SHOWING RESOURCE MOBILISATIONS THROUGH EURO ISSUES (RS IN CRORES)

Items	2008-09	2009-10
Euro issues	**4788**	**15967**
ADRs	**-**	**7763**
Of which FIs	-	-
Of which banks	-	-
a) Private	-	-
b) Public	-	-
GDRs	**4788**	**8204**
Of which FIs	-	-
Of which banks	-	843
a) Private	-	843
b) Public	-	-
Foreign Currency Convertible bonds	N.A	N.A

Source: RBI report on banks 2010

Some of the banks have gone to access the capital across the countries by the way of issuing ADRs and GDRs. As for as the above table is concerned, in 2008-09, the banking sector resorted the measure to mobilize the capital through ADR and GDR to the extent of Rs 9500 crores, where as in 2009-10 the sector attracted foreign investment of Rs 34,000 crores (approximately) through ADR and GDR and that made the Indian banking sector to be proud among other sectors

CONCLUSION

When the banks of other nations faced a terrible hit in the global financial crisis, the banking sector in India has shown and showing the positive progress in its operations and they are as follows:

- A stable growth of bank credit to the private sector
- Soundness in CRAR
- Steady improvement in asset quality of banks
- A well managed difference between cost of funds and return on funds resulted in optimum spread
- Steady profit growth
- Healthy return on equity
- Effective procurement of financial resources through domestic and foreign capital markets
- Recognition in the domestic and foreign capital markets

The above factors clearly indicate that the Indian banking sector has functioned well even at the time of crisis and it has not given up its strength during the global financial meltdown. Even after the global financial crisis the banking sector of our country is sustaining growth almost in all levels of its operations.

With the above evident this paper concludes that "Indian banking sector - a smooth sailor in the global financial tsunami".

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