RESEARCH PAPER

Commerce

Volume : 5 | Issue : 7 | July 2015 | ISSN - 2249-555X

A Study of Earning Quality of Selected Public & Private Sector Banks in India

KEYWORDS

Earning Quality, Net Interest Margin (NIM), Interest Income, Total Income

Nayan M. Gadhia

Associate Professor Lt. M. J. Kundalia English Medium Mahila Commerce College Opp. Jain Derasar, Rajkot

ABSTRACT *The quality of earnings is an important criterion that determines the ability of a bank to earn consistently, going in to the future. It basically determines the quality of bank's profitability and its ability to maintain quality, sustainability and growth in earnings in the future. The parameter gains importance in the light of the argument that a large part of a bank's income is earned through non core activities like interest & dividend on investments, treasury operations, and corporate advisory services and so on.*

. If the Government monetary policies fail to curb inflation, then it weakens the economic growth and development in any country. Banking sector is directly associated with economic growth of the nation. The recent fall in rupee, volatility in oil prices, instability in bullion and security markets in India, instability of euro and the European Market, probable hike in interest rate by USA are some examples of failure of governments to manage the monetary and Fiscal policies. In this paper, an attempt has been made to discuss Earning Quality of selected banks.

INTRODUCTION:

Every business entity is judged by its earning. Earning is one of the good parameter to measure the financial performance of financial organizations. But, in the context of banks, quality of earning is also very important. The quality of earnings is an important criterion that determines the ability of a bank to earn consistently, going in to the future. It basically determines the quality of bank's profitability and its ability to maintain quality, sustainability and growth in earnings in the future. The parameter gains importance in the light of the argument that a large part of a bank's income is earned through non core activities like interest & dividend on investments, treasury operations, and corporate advisory services and so on.

So, not only earning, but the quality of earning is also to be seen in the context of sustainability, competitiveness, healthy growth, income from core activities etc. for the banking sector. For the purpose of present study, following earning quality criteria or ratio is considered for this parameter:

- Net interest margin (NIM) to total assets
- Interest income to total income

RESEARCH METHODOLOGY:

The present study is concerned with the Indian banking system. For this study, five public sector nationalized banks and five private sector banks have been selected. The study is based on secondary data for a period of five years, 2007-08 to 2011-12. The required data have been collected from the various issues of Banking Statistics, published by the Reserve Bank of India.

To compare the performance of selected sector banks, ratio analysis as an accounting tool while F-Test ONE WAY ANOVA as statistical tools is used.

The following ratios are analysed to examine the earning quality of the study.

- Net interest margin (NIM) to total assets
- Interest income to total income

Net Interest Margin (NIM) to Total Assets

NIM, being the difference between the interest income and the interest expended as a percentage of total assets, shows the ability of the bank to keep the interest on deposits low and interest on advance high. It is an important measure of a bank's core income (income from lending operations). A higher spread indicates the better earnings given the total assets. The interest income includes dividend income and interest expended includes interest paid on deposits, loan from the RBI, and other short term and long-term loans. Here total assets means an average of total assets, which has been arrived by making an average of opening balance of assets & closing balance of assets. For example, for 2007-08= op. Balance of assets of 2007-08+ closing balance of assets of 2007-08/2.

Formula:

Net Interest Margin to Total Assets= Net Interest Margin/ Total (Av.) Assets*100

Table 1

NET INTEREST MARGIN TO TOTAL ASSETS

NAME OF BANK	2007-08	2008-09	2009-10	2010-11	2011-12	TOTAL	AVG.	RANK
SBI	2.64	2.48	2.35	2.86	3.38	13.71	2.74	5
PNB	3.06	3.06	3.12	3.5	3.21	15.95	3.19	3
BOB	2.42	2.52	2.35	2.76	2.56	12.61	2.52	9

Volume : 5 | Issue : 7 | July 2015 | ISSN - 2249-555X

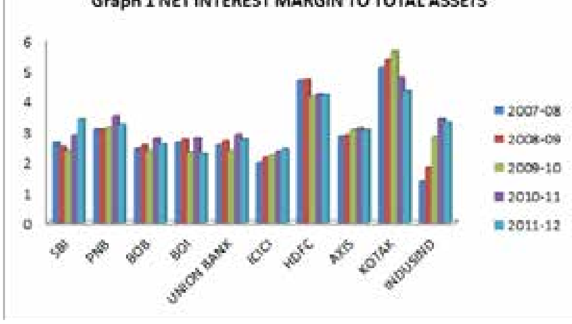
BOI	2.64	2.72	2.3	2.77	2.26	12.69	2.54	7
UNION BANK	2.52	2.68	2.35	2.88	2.73	13.16	2.63	6
ICICI	1.96	2.15	2.19	2.34	2.4	11.04	2.21	10
HDFC	4.66	4.69	4.13	4.22	4.19	21.89	4.38	2
AXIS	2.83	2.87	3.05	3.1	3.04	14.89	2.98	4
KOTAK	5.08	5.33	5.62	4.75	4.31	25.09	5.02	1
INDUSIND	1.36	1.8	2.81	3.4	3.28	12.65	2.53	8

Analysis of calculated ratios for selected banks

NIM To Total Assets is the key ratio of lending operations of the banking industry. In the present study, all the selected banks are showing NIM ratio between 2 to 5 percent. KOTAK MAHINDRA BANK is having high NIM ratio with average of 5.02 percent during research period while lowest ratio generated by ICICI BANK which is average 2.21 percent during research period. There are no specific criteria for NIM but higher the ratio shows the better earning on total assets.

Graphical Analysis

Graph 1 NET INTEREST MARGIN TO TOTAL ASSETS



By observation of the graph of selected banks it shows Average of the ratio of the research period that highest ratio is shown by KOTAK BANK (5.02) which is followed by HDFC BANK (4.38) and lowest ratio is shown by ICICI (2.21) during research period. In the present study, all the selected banks are showing NIM ratio between 2 to 5 percent.

Statistical Analysis

H_0: All the selected Banks have equal Net Interest Margin to Total Asset Ratio

H_1: All the selected Banks have unequal Net Interest Margin to Total Asset Ratio

Table 2

"F"-Test One Way ANOVA for Net Interest Margin To Total Asset Ratio

Source of Variation	Sum of Square	Degree of Freedom	Mean Sum of Square	F_c	F_t
B.S.S.	37.228512	9	4.13650133	27.1440002	2.124029
W.S.S.	6.09564	40	0.152391		
T.S.S.	43.324152	49			

From the "F" test one way ANOVA Table as calculated above it shows that Calculated value of F_c = 27.1440002 while tabular value of F_t = 2.124029 which show that calculated value F_c is larger than tabular value F_t. $F_c > F_t$. Hence Null Hypothesis is rejected and Alternative Hypothesis is accepted that Net Interest Margin to Total Assets is different for selected Banks.

Interest Income To Total Income

Interest income is a basic source of revenue for banks. The interest income to total income indicates the ability of the bank in generating income from its lending, which is a healthy sign. In other words, this ratio measures the income from lending operations as a percentage of the total income generated by the bank in a year. Interest income includes income on advances, interest on deposits with the RBI, and dividend income. While total income include interest income & other income like commission, profit (loss) on sale of investment & other assets etc.

Formula:

Interest Income to Total Income= Interest Income/Total Income***100**

Table 3

INTEREST INCOME TO TOTAL INCOME

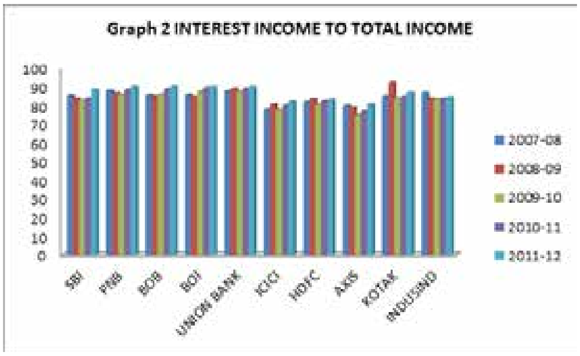
NAME OF	2007-08	2008-09	2009-10	2010-11	2011-12	TOTAL		
BANK							.AVG.	RANK
SBI	84.92	83.41	82.59	83.72	88.13	422.77	84.55	6
PNB	87.72	86.19	85.58	88.19	89.67	437.35	87.47	2
BOB	85.21	84.55	85.61	88.62	89.66	433.65	86.73	4
BOI	85.37	84.27	87.23	89.17	89.56	435.6	87.12	3
UNION BANK	87.47	88.91	87.07	88.97	89.57	441.99	88.40	1
ICICI	77.75	80.35	77.47	79.62	81.72	396.91	79.38	9
HDFC	81.58	83.23	80.24	82.13	82.81	409.99	82.00	8
AXIS	79.6	78.9	74.68	76.59	80.23	390	78	10
KOTAK	84.54	91.8	83.82	84.3	86.35	430.81	86.16	5
INDUSIND	86.34	83.5	83.02	83.41	84.11	420.38	84.08	7

Volume : 5 | Issue : 7 | July 2015 | ISSN - 2249-555X

Analysis for calculated ratio for selected banks

The interest income to total income indicates the ability of the bank in generating income from its lending, i.e. the core activity of banks. In the present study highest ratio of income from interest to total income is generated by UNION BANK with 88.40 % which is followed by PNB with 87.47 while lowest ratio is generated by AXIS BANK with 78.00 %. In the present study, all the selected banks are showing interest income between 78 to 88 percent during research period.

Graphical Analysis



By observation of the graph of selected banks it shows that most of the selected research unit shows average ratio of interest income to total income is falls between 78 percentages to 88 % during research period for selected research unit. Highest average ratio is shown by UNION BANK (88.40 %) which is followed by PNB (87.47 %) while lowest ratio is shown by AXIS BANK (78.00%).

Statistical Analysis

H_0: All the selected Banks have equal Interest Income to Total Income Ratio

H_1: All the selected Banks have unequal Interest Income to Total Income Ratio

Table 4

"F"-Test One Way ANOVA for Interest Income To Total Income Ratio

Source of Variation	Sum of Square	Degree of Freedom	Mean Sum of Square	F_c	F_t
B.S.S.	566.89129	9	62.987921	15.19202	2.124029
W.S.S.	165.84476	40	4.146119		
T.S.S.	732.73605	49			

From the "F" test one way ANOVA Table as calculated above it shows that Calculated value of F_c = 15.19202 while tabular value of F_t = 2.124029 which show that calculated value F_c is greater than tabular value F_t. $F_c > F_t$. Hence Null Hypothesis is rejected and Alternative Hypothesis is accepted that Interest Income to Total Income is different for selected Banks.

CONCLUSION:

From this study, it is concluded that net interest margin (NIM) to total assets and interest income to total income of each selected banks are not having an equal earning quality during research period. Hence, it is concluded that net interest margin is far variable to total assets while interest income is also variable factors. So, from the result, it can be said that earning quality of the selected banks is far different during research period.

REFERENCE

1. Gupta, R. (2008), a Camel Model Analysis of Private Sector Banks in India. Journal of Gyan Management. Vol. 2, (1) pp .3-8. | 2. Bhayani, S. (2006), "Performance of the New Indian Private Sector Banks: a Comparative Study". Journal of Management Research, 5(11), pp 53-70. | 3. Kapil, S. & Kapil, K, N, (2005), "CAMEL's Ratings and Its Correlation to Pricing Stocks- an Analysis of Indian Banks". University Journal of Bank Management, 4(1), pp 64-78. | 4. Sarker, A. (2005), "CAMEL Rating System in the Context of Islamic Banking: A Proposed "S" for Shariah Framework. Journal of Islamic Economics and Finance, 1 (1), pp 78-84. | 5. Satish D, Jutur Sharath and Surender V., " Indian Banking Performance And Development 2004-05", Chartered Financial Analyst Vol. 11 (10), pp 6-15. |