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Portfolio Analysis Of Banking Sectors – Investment Scenario

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Abstract

Portfolio analysis is an evaluation of an investment portfolio to determine if it is meeting an investor's needs, whether the investor is a multinational corporation or a teacher planning for retirement. The analysis provides a breakdown of current assets in the portfolio, along with a discussion of their current and historic performance to see if the investor is making smart decisions about resource allocation. The analysis can offer recommendations for improving the mixture of the portfolio, taking the unique needs of the investor into account. The success of a product line is often measured in terms of its profitability. However, profits should not be the only basis for mapping product success. Organizations also need to take the risk-factor for a product into account so that they can make an accurate assessment of their product-line portfolios. Ideally, products with low margins and high volatility should be divested as they clearly overexpose the company to a high level of risk without sufficient returns. Similarly, low margin, low-volatility product lines do not expose the company to excessive risks and can be considered if the profitability can be improved. So, on what basis should companies assess the risk vis-à-vis return profile of their product portfolio? Econometric modeling can be used to estimate the risk/return profile of products. Besides performing the usual commercial banking functions, banks in developing countries play an effective role in their economic development. The portfolio analysis of banking sector at present is playing very vital role in the development of economy. Hence, the present study focuses on portfolio analysis of some selected banks in India. Study based on both Primary and Secondary sources.

Key words: *Investor's Needs, Resource Allocation, Profitability, Risk-Factor, Low Margins & High Volatility, Econometric Modeling and Development of Economy.*

INTRODUCTION

In finance, a portfolio is a collection of investments held by an investment company, hedge fund, financial institution or individual. The term portfolio refers to any collection of financial assets such as cash. Portfolios may be held by individual investors and/or managed by financial professionals, hedge funds, banks and other financial institutions. It is a generally accepted principle that a portfolio is designed according to the investor's risk tolerance, time frame and investment objectives. The monetary value of each asset may influence the risk/reward ratio of the portfolio and is referred to as the asset allocation of the portfolio. When determining a proper asset allocation one aims at maximizing the expected return and minimizing the risk. This is an example of a multi-objective optimization problem: more "efficient solutions" are available and the preferred solution must be selected by considering a tradeoff between risk and return. In particular, a portfolio A is dominated by another portfolio A' if A' has a greater expected gain and a lesser risk than A. If no portfolio dominates A, A is a Pareto-optimal portfolio. The set of Pareto-optimal returns and risks is called the Pareto Efficient Frontier for the Markowitz Portfolio selection problem.

OBJECTIVES OF THE STUDY

The present study has been conducted with the following objectives:

1. To know about Banking sector in India
2. To analyze the contribution of each category of banking in deposits
3. To analyze the portfolio analysis of selected banks in India
4. To give suggestions for future successful analysis of portfolio

OPERATIONAL DEFINITIONS

"The banking industry consists of financial institutions that receive demand deposits and term deposits from customers and channelize this money into lending activities. The banking industry can be broadly divided into retail banking, corporate banking, treasury services, wealth management and agricultural banking"

Portfolio analysis is "a process used to assess the suitability of a portfolio of securities or business relative to its expected investment return and its correlation to the risk tolerance of an investor seeking the optimal trade-off between risk and return".

BANKING SECTOR IN INDIA

The banking industry in India has witnessed a constant growth in the last decade. The most common form of measuring the size of the banking industry is measuring the total assets of the banks. According to BMI India Commercial Banking Report, in 2011, the assets of the banking sector of India were valued at $1,267.7 billion. The banking industry in India grew at a rate of 13.92% between 2008 and 2011 and is expected to grow at 27.59% between2012 and 2016As on 31st March 2011, the banking sector in India comprised of 170 commercial banks. The growth in this sector has primarily been driven by increasing globalization and liberalization of Indian economy. Realizing the potential of the Indian banking sector, many foreign banks are entering the industry which in turn is further driving the growth and opportunities of the industry.

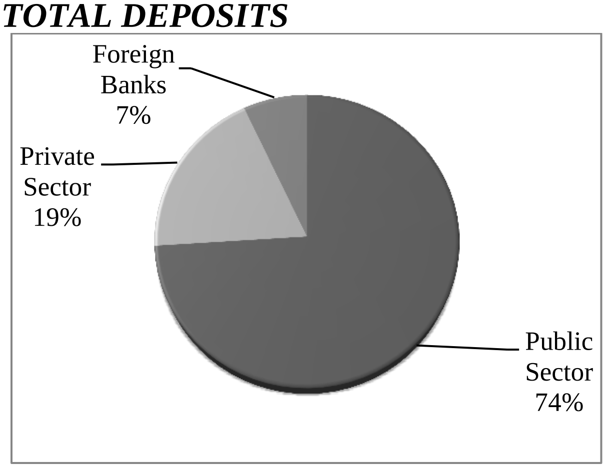
Public Sector Banking

Public sector banking refers to the banking activities of a certain class of commercial bank. The specific use of this term depends on the country or region of the world where it is used, but generally speaking, public sector banks are those that are owned or operated by national governments. Some countries use this kind of banking more than others, but in large regions of the world, where state control is traditional, it's not uncommon to talk about public sector banking. A study of public sector banking can be related to an overall analysis of a national economy. The way that governments interact with commercial banks or undertake banking activities has a lot to say about how that form of government administrates their control over a country or federation. Many finance pros and economists view banking as an inherently political sector. One example of using public sector banking in a national context is in India. India is a country that many investors are now looking at, since it is known as an "emerging market," where future economic growth is likely. India uses a great number of public sector banks, where the government may have a majority stake in publicly traded commercial banks.

Private Sector Banking

Private sector banking is a type of banking process that involves financial institutions which are primarily owned and operated by private individuals and business organizations rather than by a government entity. This is in contrast with public sector banking, in which the banking enterprise is owned and operated by the state in some manner. In many nations that are supportive of free enterprise, private sector banking is the most common form of banking available. While a government may not actually control banks and other financial institutions that engage in this form of banking, private sector institutions do typically have to comply with governmental regulations that apply to banking in general. It is not unusual for private sector banking to play a major role in the economy of a given nation. Since this form of banking along with other private sector business enterprises tends to account for a large portion of the money that moves through an economy, financial analysts will pay close attention to what is happening in the private sector. In some nations, a government bank may sometimes set the standard for issues such as interest rates, with banks in the private sector following the example. Since so much of the economy depends on the activities occurring within the private sector, the current policies and procedures that govern private sector banking within a given nation can often help to slow and eventually reverse an unfavorable economic trend, such as a recession.

CONTRIBUTION IN TOTAL DEPOSITS



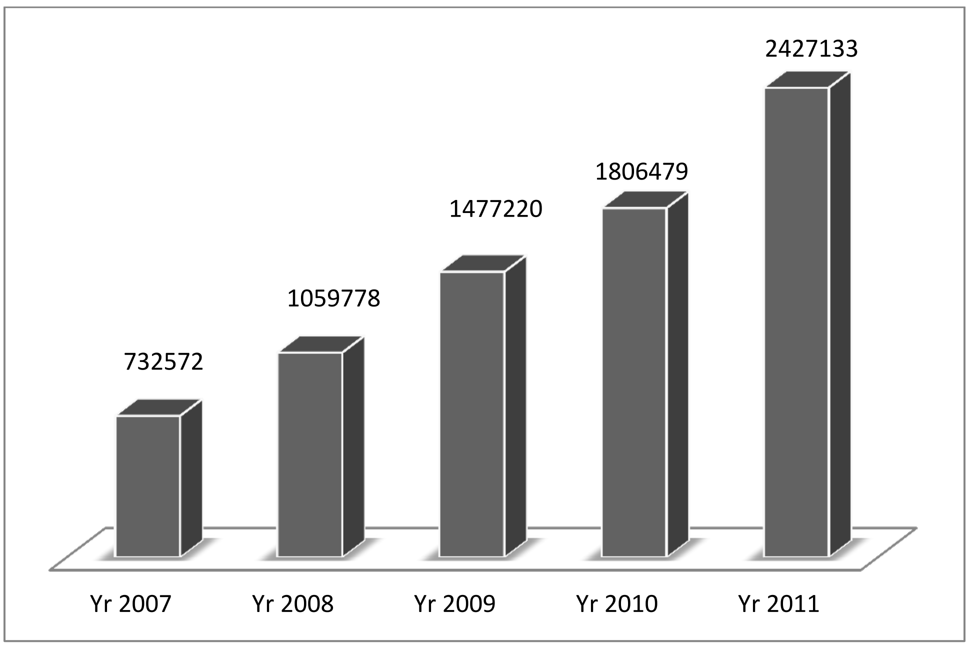
The public sector, private sector and foreign banks are collectively known as scheduled commercial banks (SCBs).

ANALYSIS ON PORTFOLIO OF SELECTED BANKS

AXIS BANK

Axis Bank Limited, formerly UTI Bank, is an Indian financial services firm that had begun operations in 1994, after the Government of India allowed new private banks to be established. The bank changed its name to Axis Bank in April 2007 to avoid confusion with other unrelated entities with similar name. After the Retirement of Mr. P. J. Nayak, Shikha Sharma was named as the bank's managing director and CEO on 20 April 2009. Axis Bank is the third largest private sector bank in India. The bank operates through treasury, retail banking, corporate/wholesale banking and other businesses divisions. The Bank's Registered Office is at Ahmadabad and its Central Office is located at Mumbai. At the end of December 2011, the Bank has a very wide network of more than had a network of 1,493 domestic branches and extension counters and 8,324 ATMs situated in 971 cities and town. Interest margins of Axis bank, while they have declined from the 3.15 per cent seen in 2003-04, are still hovering close to the 3 per cent mark.

Chart 2: Total Assets (INR million)

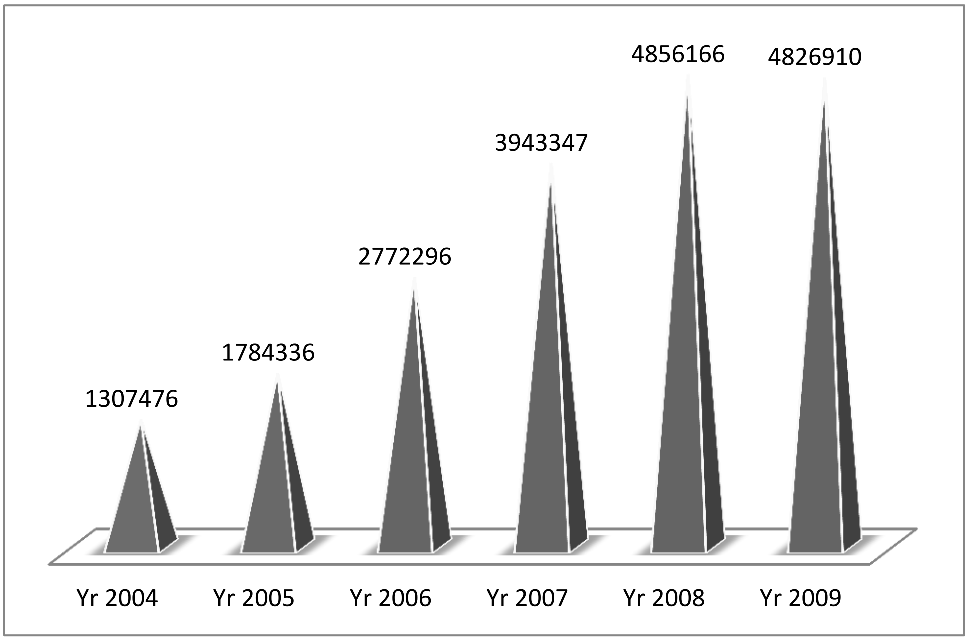


This bank has the least amount of spending on advertising as a percentage of net profit. It is only 1.2% as against 1.73%and 3.12% by ICICI and SBI respectively. The bank does not have an as extensive distribution channel as ICICI bank and State Bank of India do. The market share of this bank is lowest in comparison with other two banks. Overall, the reputation of the company is lesser as compared to SBI and ICICI. The bank was previously named UTI Bank and has changed its name a couple of years back. However, the awareness about the bank is on a rise and is expected to match other major banks because of its high growth.

ICICI BANK

ICICI (Industrial Credit and Investment Corporation of India) Bank Ltd. is an Indian diversified financial services company headquartered in Mumbai, Maharashtra. It is a wholly owned subsidiary of ICICI Ltd. Established in 1994, it is the second largest bank in India by assets and third largest by market capitalization. It offers a wide range of banking products and financial services to corporate and retail customers through a variety of delivery channels and through its specialized subsidiaries in the areas of investment banking, life and non-life insurance, venture capital and asset management. The Bank has a network of 2,575 branches and 8,003 ATM's in India, and has a presence in 19 countries, including India. ICICI Bank is one of the Big Four banks of India, along with State Bank of India, Punjab National Bank and HDFC Bank. Established in 1994, ICICI Bank is India's second largest bank. It is a wholly owned subsidiary of ICICI Ltd. The bank has a network of 2533 branches and 6800 ATMS in India. Between 2004 and 2009, the total assets of the bank increased at a CAGR of 30%.

Chart 3: Total Assets (INR million)

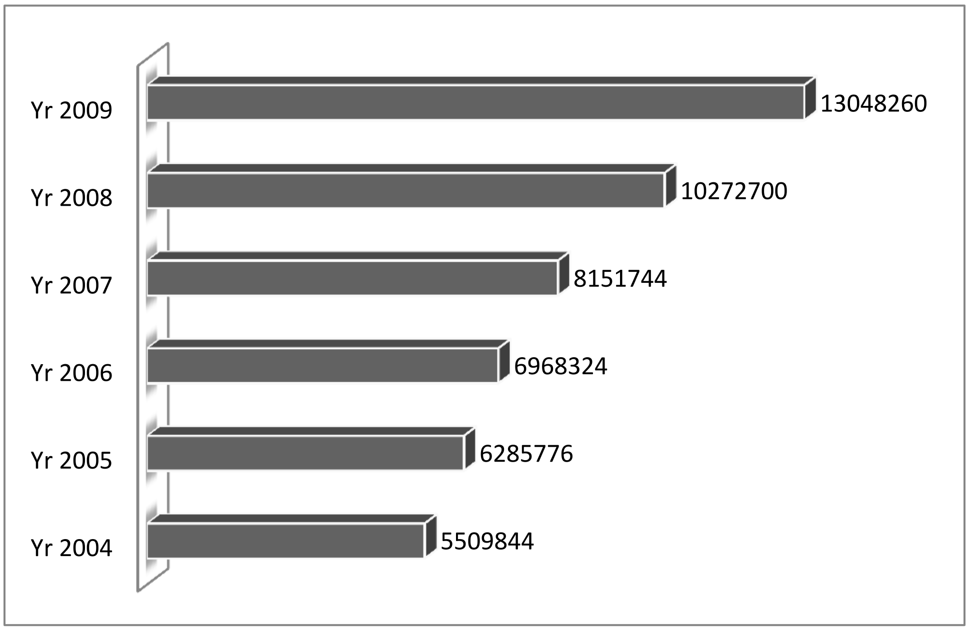


ICICI Bank is the largest private sector bank of India. It has high competitive strength in private wealth management segment because of international presence. It has highest market share in domestic private wealth management segment. The NPA levels are also satisfactory. Its performance during recent financial turmoil shows that the bank has strong fundamentals. It is accompanied by moderate expenditure in advertisement. It operates with high operating efficiency. However, it has high international exposure in risky assets which increases its risk on returns. This bank ranks second in all the business segments except private wealth management where it is ranked 1.

STATE BANK OF INDIA

State Bank of India (SBI) is the largest banking and financial services company in India by revenue, assets and market capitalization. It is a state-owned corporation with its headquarters in Mumbai, Maharashtra. As of March 2011, it had assets of US$ 370 billion with over 13,000outlets including 150 overseas branches and agents globally. Between 2004 and 2009, the total assets of the bank increased at a CAGR of 19%.SBI provides a range of banking products through its vast network of branches in India and overseas, including products aimed at non-resident Indians (NRIs). The State Bank Group, with over 16,000branches, has the largest banking branch network in India. SBI has 14 Local Head Offices situated at Chandigarh, Delhi, Lucknow, Patna, Kolkata, Guwahati (North East Circle), Bhuwaneshwar, Hyderabad, Chennai, Trivandram, Bangalore, Mumbai, Bhopal & Ahmadabad and 57 Zonal Offices that are located at important cities throughout the country. It also has around 130 branches overseas. Established in 1806, State Bank of India (SBI) is the oldest and the largest bank of India. SBI has14 local head offices and 57 regional offices across India. The bank has 8,500 ATMs, about18, 000 SBI branches and 5,100 associate branches. Between 2004 and 2009, the total assets of the bank increased at a CAGR of 19%.

Chart 4: Total Assets (INR million)



State Bank of India is the oldest and largest bank of India. Hence it is a clear winner in terms of company reputation and image. It has a very extensive distribution network and has reach in remote areas also. This makes it possible for this bank to serve rural areas too. SBI is clear winner in retail because of its extensive distribution network and high deposits. However, this bank suffers from higher NPA percentage as compared to other banks. At the same time, the advertising budget is highest among the three banks. It is a long established bank, resulting in high level of trustworthiness. But it has a lower operating efficiency. Because of its high market share in most of the business segments, this bank has high competitive strength.

POSITION OF COST ADVANTAGE

COST PARAMETERS (IN RS. THOUSANDS)			
	AXIS Bank	SBI	ICICI Bank
Total Income	19,78,69,396	972189580	61,59,47,044

Total expenditure	16,39,84,490	889544390	55,27,65,103
Tot. expenditure as % of Total income	83%	91%	90%
Payments to and provisions for employees	1,61,39,001	144801678	43925959
% of total income	8%	15%	7%
Rent, taxes and lighting	67,98,464	17944879	97,23,158
% of total income	3.4%	1.8%	1.6%
Advertisement and publicity	7,90,153	2578761	38,74,585
% of total income	0.40%	0.27%	0.63%
Profit per employee	14.35lakhs	3.84lakhs	10lakhs

From the above table it can be inferred that SBI has the highest percentage of total expenditure as a percentage of its income. Also the profit per employee is the lowest and there is a substantial difference between in this regard between SBI and the other two banks in comparison. The total expenditure of Axis bank is the lowest and its cost per employee is the highest which puts it in the position of a cost leader amongst the three banks.

WHAT TO DO IN FUTURE….

Axis Bank and ICICI Bank lag behind SBI by a very huge margin in Retail Banking. To increase their market shares and competitive strength in this segment, it is advisable for them to look to acquire small regional banks to develop synergies. Currently, there are a large number of regional banks. This results in a lot of ATMs and branches setting up in an area. By consolidating these branches and ATMs, Axis Bank and ICICI Bank can gain economies of scale and provide competition to a large bank like SBI. Also these banks have to focus on tier II and III cities and develop a strong foothold there.

CONCLUSION

Portfolio analysis encourages management to evaluate each of the organization's businesses individually and to set objectives and allocate resources for each. It stimulates the use of externally oriented data to supplement management's intuitive judgment. Ans also it raises the issue of cash flow availability for use in expansion and growth Portfolio analysis is an important aid in the Banking sector to identify its specific competitive role. This role should be so well suited to the sector's external and internal environments that other associations are unlikely to challenge or dislodge it. The banking sector then has a distinctive competence that enables it to take advantage of specific environmental opportunities. To accomplish this, the Banks must be on the constant lookout for strategic windows or market opportunities. In today's competitive world, successful any organization will have three characteristics in common, and portfolio analysis will have an important role to play in helping associations achieve them.

- They will innovate as a way of life.
- They will compete on value in meeting member needs, not on price.
- They will achieve leadership in related niche markets.

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