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STUDY OF LIQUIDITY RATIOS OF BANKS OPERATING IN INDIA

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ABSTRACT:

The major role of banks is to collect money from the public in the form of deposits and then along with its own funds to serve the demands of the customers quickly, paying interest for the deposits and to meet out the expenses to carry out its activities. For this purpose, banks maintain adequate liquidity and earn profits from its activities. Profit is the main reason for the continued existence of every commercial organization and profitability depicts the relationship of the absolute amount of profit with various other factors. In any case, compared to other business concerns, banks in general have to pay much more attention for balancing liquidity. Liquidity is required to meet out the prompt demands of customers. In the present study an attempt has been made to evaluate the liquidity of different categories of banks lie public, private bank groups in India.



INTRODUCTION:

When analysis of banks performance is done they only concerned about various types of the ratios or the NPA levels of the banks. Also the approach to the asset liability management is not clear. One of the methods to analyze the financial strength of a bank is financial ratio analysis. Liquidity ratios are calculated and analyzed to determine the liquidity strength of a bank. Every financial institute irrespective of its size is generally exposed to market liquidity and interest rate risks. Failure to identify the risk may affect the financial position of the financial institute.

Effect on asset values:

The market liquidity of assets affects their prices and expected returns. Theory and empirical evidence suggests that investors require higher return on assets with lower market liquidity to compensate them for the higher cost of trading these assets. That is, for an asset with given cash flow, the higher its market liquidity, the higher its price and the lower is its expected return. In addition, risk averse investors require higher expected return if the asset's market liquidity risk is greater. This risk involves the exposure of the asset return to shocks in overall market liquidity, the exposure of the asset own liquidity to shocks in market liquidity and the effect of market return on the asset's own liquidity. Here too, the higher the liquidity risk, the higher the expected return on the asset or the lower is its price.

There are certain ways by which bank achieve adequate liquidity. They are as under.

Shorten asset maturities

Improve the average liquidity of assets

Lengthen liability maturities

Issue more equity

Reduce contingent commitments

Obtain liquidity protection

LITERATURE REVIEW:

Loutskina E. (2010) This paper studies the role of securitization in bank management. The author propose a new index of "bank loan portfolio liquidity," which can be thought of as a weighted average of the potential to securitize loans of a given type, where the weights reflect the composition of a bank loan portfolio. The use of this new index is to show by allowing banks to convert illiquid loans into liquid funds, securitization reduces banks' holdings of liquid securities and increases their lending ability. Thus, market trends generate time variation in the index, whereas differences in bank loan portfolio structures generate variation across institutions. Furthermore, securitization provides banks with an additional source of funding and makes bank lending less sensitive to cost of funds shocks. By extension, the securitization weakens the ability of the monetary authority to affect banks' lending activity, but makes banks more susceptible to liquidity and funding crisis when the securitization market is shut down. The results suggest that as banks' ability to securitize loans has increased, their holding of liquid assets on balance sheets has decreased.

Kress J. C. (2011) Credit default swaps were widely blamed as a primary cause of the recent financial crisis credit default



swaps fomented panic as the price of credit protection spiked and contributed to the Federal Reserve’s decision to bail out American International Group. To reduce the likelihood that credit derivatives will lead to future financial distress, the Dodd-Frank Wall Street Reform and Consumer Protection Act mandates that many crisis credit default swaps be traded through a centralized counterparty, a clearinghouse that acts as a seller to every buyer and a buyer to every seller. Proponents of central clearing argue that this reform minimizes risks to the financial system by reducing interconnections and dispersing losses.

Wuryandani G. (2012), study investigates the determinants of banks liquidity. There are two category of bank liquidity in this study that is precautionary and involuntary. The definition of precautionary liquidity is the ratio of total cash, demand deposit at central bank, and demand deposit at other banks to total asset. Whilst the definition of involuntary liquidity is the ratio of total traded securities of central bank, government, and others, to total asset. The study indicates that credit, saving and deposit affect precautionary liquidity.

Kumar A. (2014) This paper is focused on the analysis and comparison of liquidity ratios and asset liability management practices in top three banks from public, private and foreign sector in India. The analysis is based upon the liquidity ratios calculation and the determination of maturity gap profiles for the banks under

study. The paper also compares these banks maturity gap profiles with their corresponding group’s maturity gap profiles. This paper identifies the interest rate sensitivity of the balance sheet items of these banks to determine the gap between rate sensitive assets and rate sensitive liabilities. The results of this study suggest that overall banks in India have very good short term liquidity position and all banks are financing their short term liabilities by their long term assets.

OBJECTIVES:

The following broad objectives are laid down for the purpose of the study:

To study Liquidity trend in last 5 years of private and public sector banks.

To make a comparative study of Liquidity of public sector and private sector banks.

To offer suggestions to improve its profitability.

RESEARCH METHODOLOGY:

“Research design is the arrangement of activities for the collection and analysis of the data in a manner that aims to combine relevance to the purpose with economy in procedure. The study carried out here is an Analytical Research. The data has been collected from secondary sources. This study was conducted for a period of five years from 2010-2011 to 2014-2015.

Current Ratio					
Banks	2011	2012	2013	2014	2015

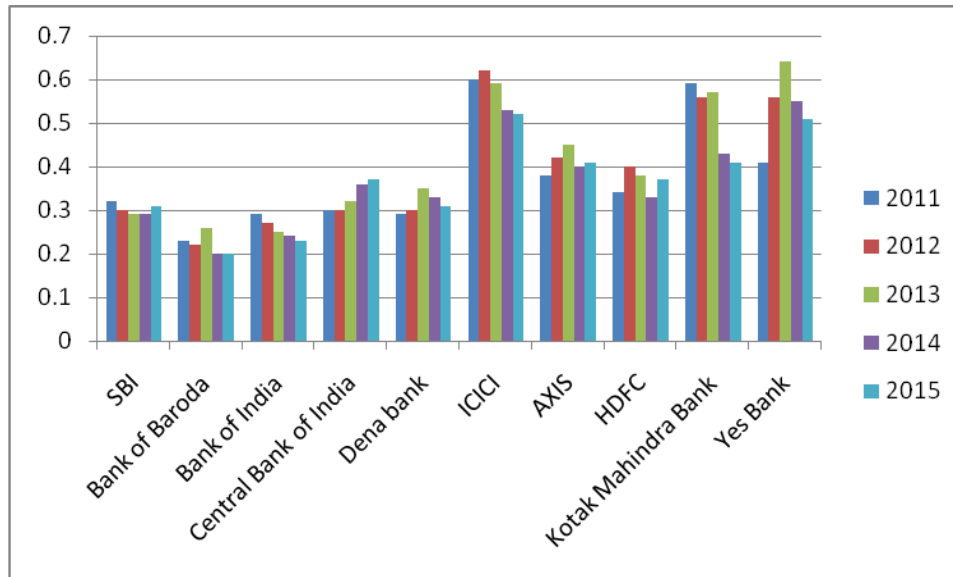


SBI	0.32	0.3	0.29	0.29	0.31
Bank of Baroda	0.23	0.22	0.26	0.2	0.2
Bank of India	0.29	0.27	0.25	0.24	0.23
Central Bank of India	0.3	0.3	0.32	0.36	0.37
Dena bank	0.29	0.3	0.35	0.33	0.31
ICICI	0.6	0.62	0.59	0.53	0.52
AXIS	0.38	0.42	0.45	0.4	0.41
HDFC	0.34	0.4	0.38	0.33	0.37
Kotak Mahindra Bank	0.59	0.56	0.57	0.43	0.41
Yes Bank	0.41	0.56	0.64	0.55	0.51
Source: www. moneycontrol.com					

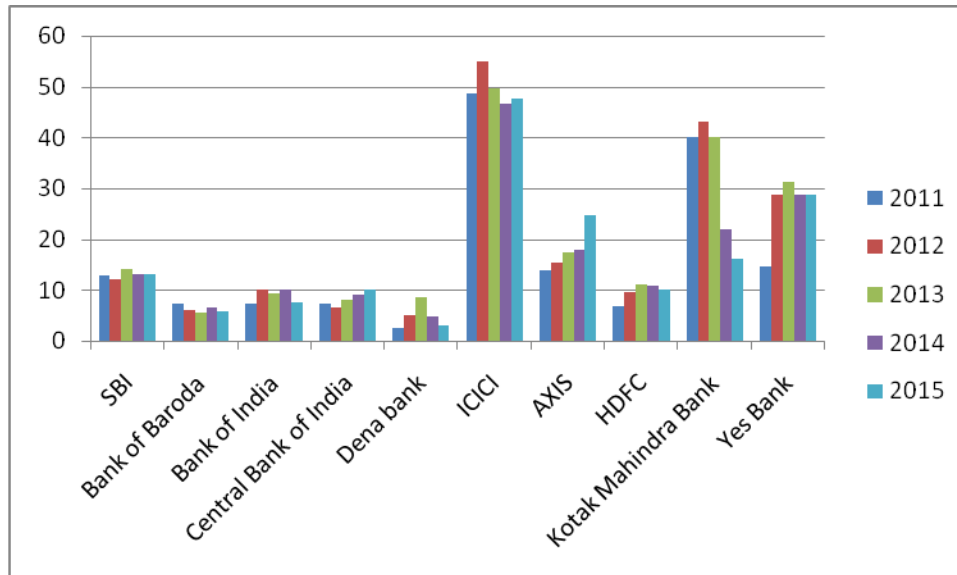
Quick Ratio					
Banks	2011	2012	2013	2014	2015
SBI	12.8	12.17	14.07	13.13	13.01
Bank of Baroda	7.3	6.12	5.61	6.47	5.71
Bank of India	7.37	10.09	9.26	10.15	7.53
Central Bank of India	7.19	6.59	8.1	9.2	10.16
Dena bank	2.63	5.03	8.66	4.69	2.96
ICICI	48.56	54.86	49.67	46.63	47.69
AXIS	13.88	15.48	17.4	17.9	24.74
HDFC	6.9	9.67	11.14	10.74	10.03
Kotak Mahindra Bank	40.07	43.06	40	21.83	16.2
Yes Bank	14.56	28.8	31.25	28.73	28.76
Source: www. moneycontrol.com					



Current Ratio:



Quick Ratio:



From the above diagram we can see that private banks current ratios is more compare to the public sector banks. Which means that private sectors performance is better in comparison to the public sector



banks. In quick ratio also private banks is higher than the public sector banks. In quick ratio there is a major difference in both the types of banks. Private banks performance is higher than the public banks. Public banks have to improve the ratio so that they can maintain proper liquidity in banks and they can work properly. If this ratios are improved in public banks than they can perform better like public banks.

SCOPE OF THE STUDY:

The present study is restricted to the analysis and interpretation of the published financial data through the use of commonly used techniques.

CONCLUSION:

This study examines the relationship among the liquidity of Indian public banks and private sector banks. The bank management should speed up the recovery process to reduce the liquidity problem. The problem of recovery is not with small borrowers but with large borrowers and a strict policy should be followed for solving this problem. With the increasing competition in the banking sector, liquidity has become a greatest challenge to Indian commercial banks. Banks should explore every possibility for improvement in liquidity. The problem of liquidity needs lots of serious efforts otherwise liquidity will keep killing the profitability of banks which is not good for the growing Indian economy at all.

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