Financial Performance of State bank of India and Dubai Islamic Bank: A comparative Study

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Abstract: This study is executed to compare the financial performance of selected banks namely State Bank of India and Dubai Islamic Bank of United Arab Emirates. SBI is operating as conventional banking system while DIB is operating under Islamic banking system which is fast growing concept in the world. Financial data is collected for last five years of selected banks. Profitability and Solvency is tested by using different financial ratio and Bankometer model for Solvency. It is revealed in the study that DIB successive in all parameters compared to SBI except Assets Utilisation. SBI caught critical in term of Non-performing Assets as it is constantly increasing.

Keywords: Financial performance, SBI, Dubai Islamic Bank, Bankometer

I. Introduction

An economy of any country is divided in many sectors like, service sector, manufacturing sector where financial sector is also included in service sector. Financial sector of economy plays a vital role to enhance the performance of all other sectors. Performance of all sectors is affected with the growth of financial sectors of the country. Banking industry is the core of financial sectors as it holds most of the financial assets of the public. Bank is the crucial role player in the country as it works as intermediary between fund savers and fund seekers. The common functioning of banks in India is to take deposits from the customer and pay them interest as a return on deposits and from these deposits banks provide fund to the needy people for their use and charge the interest from them. Banks get the benefit of difference in interest rate of deposit and advances for their respective services.

Services rendered by the banks in India are increasing day by day. With this increment the working of bank becomes so complicated and on the other hand majority of the banks pass through the sickness of Non-Performing Asset (NPA) which breaks the smooth working of banks. The problem of NPA is increasing day by day as number of defaulters goes on rising. Hence, the risk of insolvency increases with this problem.

Over last decade, banks suffered with NPA problem. As per provisional data on global operation of RBI, on 31/03/2019 the accumulated amount of gross NPAs of Public Sectors Banks and Scheduled Commercial Banks (SCBs) were Rs. 8,06,412 crore and Rs. 9,49,279 crore respectively[1]. Basic reason for this situation pointed out towards excessive loan allotment, loan defaulter, corruption, and problem of economic slowdown. Government tries to search out the solution for this problem and has done many reforms in banking sector but still much is to be done to solve the problem.

In India, around 14% of the total population are Muslims and as per Islamic shariah Interest is prohibited whether it is taken or given and banking industry in India is purely based on Interest hence, many of the Muslim population are excluded from the banking beneficiary. In one survey it is found that 21% of the total unbanked population of the word are Indians and among them more than 50% are Muslims (SANA BEG, 2016). Muslims which are not connected with the banks due to prohibition of interest can be included by introducing Islamic bank in India which is already working in many countries of the word like, Malaysia, Singapore, United Kingdom, UAE, etc. Islamic bank works on its personal rules and regulation as per Islamic shariah and it is purely based on Profit and Loss.

This study is conducted to do a comparative analysis of Indian based State Bank India and UAE based Dubai Islamic Bank. Uniqueness of this study is that SBI is conventional bank in India and DIB is Islamic bank in UAE. Both the banks are the oldest and the largest banks in their respective countries. Comparative analysis is done on financial reports which are published by the banks for the last five years. Accounting ratios and statistical tool are used to measure and compare the profitability and solvency of two banks.

Concept and operation of Islamic Banking

In Islam, interest is not permitted and all the transactions which involve interest are called as Haram (prohibited). Interest is prohibited as it is mentioned in many verses of the Holy Quran and Hadiths of Prophet (PBUH) and his 12 companions called as Imam. Islamic shariah is all for welfare of the society. It is the duty of the rich peoples to help the needy people in their society without exploiting them. Therefore, Islam prohibits the interest so that needy people get the helps from the empowered one and a balanced society can be formed by this way.

Islamic bank does its all operation without charging or paying the interest and at this point it is dissimilar to the conventional banking system. The working pattern of Islamic bank is similar to conventional bank up to a certain level. As like conventional

[1] http://pib.nic.in/newsite/PrintRelease.aspx?relid=190704

banks Islamic bank also accepts the deposits and provides loan to the fund seekers by avoiding interest. All the operations of Islamic bank are accomplished under the agreement of Profit and Loss sharing basis. Operation of Islamic banks is mainly divided into two parts as follow:

A) Deposits
B) Investment Activities

Deposits:

Deposits from the customers are accepted by the bank through two different accounts namely:

1) Saving Account
2) Investment Account

Saving Account:

In this type of account customers deposit their saving with the bank and give permission to the bank to use their money and the customers get the money back from the bank whenever they want. Bank is obliged to return full amount to the customer but reward or return on that is not guaranteed although banks pay them certain rate of profit.

Investment Account:

Investment account can be of two types, one is account with authorisation in which customer authorises bank to use his money in any specific project of the bank and after completion of that project account holder get the profit at pre agreed rate. While another type of account is account without authorisation in which customer may or may not specify any project and time for the use of his money. Investments accounts are opened for fix period of time.

Investment Activities:

Different kinds of financing modes are used by the Islamic bank to make an investment of deposits received from the customers. Modes are as follow:

Musharakah

Musharakah is the investment activity of equity participation in which bank invests money in any project on the offer of its client. Both the parties contribute the capital and share Profit and loss on pre agreed rate.

Mudarabah

In this type of activity banks provide all the financing for the business and client manage the business and both the parties get the profit earned in agreed proportion. Here client does not provide any capital.

Murabaha

According to the requirement of the client bank purchases the goods and sell it to the client by charging the profit on its price. Client pays the full amount of goods in equal instalments.

Ijara

In this event bank owns a fixed assets as per requirement of the customers and give it to the client on a rental basis. Customer has to pay the rent for the use of that asset. Ijara contract is similar to the leasing agreement.

Defining Important terms

In this study the researcher makes the comparative analysis of two banks on the basis of profitability performance and Solvency and for this analysis different types of ratios are used as follow:

Profitability performance:

Ratio	Formula	Significance
Return on Assets	$\frac{\text{Net profit}}{\text{Total Assets}} \times 100$	It is used to measure the profitability in the context of total Assets of the bank.
Return on Deposits	$\frac{\text{Net profit}}{\text{Total Deposits}} \times 100$	It is used to measure the profit with regards to the total deposits of the bank.
Profit Margin	$\frac{\text{Net profit}}{\text{Operating Income}} \times 100$	It is used to calculate profit margin percentage of bank.
Asset utilisation	$\frac{\text{Operating income}}{\text{Total Assets}} \times 100$	This ratio is used to measure the utilisation of assets to earn total operating income.
Operating efficiency ratio	$\frac{\text{Operating expense}}{\text{Operating income}} \times 100$	It is used to measure banks efficiency to cut operating expense to earn maximum revenue.

Solvency:

To measure and compare the solvency of two selected banks, the researcher used a model named Bankometer which is developed by Amir Hussain Shar and others in 2010. This model is easy to use and apply as it require minimum variable as compare to others. This model is developed by considering IMF (2000) Recommendations. (Onyema JI, 2018)

S = 1.5* CA+1.2* EA +3.5 * CAR+0.6*NPL+0.3*CI+0.4*LA

Where,

S = Solvency
CA = Capital Assets Ratio
EA = Equity to Assets Ratio
CAR= Capital Adequacy Ratio
NPL= Non-performing loan to total loan
CI= Cost to Income Ratio
LA= Loan to Assets Ratio

With the benchmark that,

- When value of S<50, Bank is facing financial crisis and difficulty.
- When value of 50<S>70, Bank is in the gray area due to susceptibility to error classification.
- When S>70, Bank is financially sound.

II. Literature Review

Study has been carried out to do a comparative analysis of conventional banks and Islamic banks in Bahrain for the period of 1991 to 2001. Different types of financial ratios are used to examine the profitability, liquidity and credit risk of the banks. It is revealed in the study that there is no major difference among the conventional banks and Islamic banks in terms of profitability and liquidity. While in term of Credit risk parameter Islamic bank found superior to conventional banks as it has less credit risk. (Samad, 2004)

Research is conducted to check the Liquidity risk management of Conventional bank and Islamic bank in Pakistan for the period of 2006 to 2009. Liquidity of the selected banks has been checked with the context of size of the bank, net working capital, return on equity, capital adequacy and return on assets. Results show that size of the bank and net working capital does not affect to Liquidity risk much in both the format of banks. Further, Capital Adequacy ratio in Conventional banks and return of assets in Islamic bank has major effect on Liquidity of banks. (Muhammad Farhan Akhtar, 2011)

Study accompanied to measure the financial performance for comparison of selected banks of Indonesia which follow under Islamic banking and Conventional banking. Performance of banks are measured with the parameters namely profitability, liquidity, risk and solvency and efficiency from 2000-2007. In the concluding part of the study the researcher discussed that no major dissimilarities found between Islamic banks and Conventional banks on their financial data except liquidity, as Islamic banks are more liquid than Conventional banks. (Siti Rochmah Ika, 2011)

Comparative analysis has been done between First Islamic bank and 5 Conventional banks of Pakistan on the ground of Different financial ratios like Return of Assets, Return on Equity, and Loan to Deposit ration etc. It is observed in the study that Islamic bank MBL (Meezan Bank Limited) which was introduced in 1977-78 in Pakistan is less profitable and less risky as compared to 5 average Conventional banks and also less in efficiency. Both the groups of banks have similarity in terms of Liquidity management. These differences can be argued on the ground that Conventional banks in Pakistan have longer history and experience therefore; it has dominant influence over financial sector and holding major portion of Financial Assets of Pakistan. It is concluded that Islamic banking system is growing considerably. (Moin, 2008)

This study was undertaken to identify the difference and similarities among Islamic banks and Conventional banks. Some arguments suggest that Islamic banking system is working as like conventional banks in addition to certain restrictions according to Shariah compliances. In this study the researcher found that the above statement is not perfectly true. Difference noted among the working of conventional banks and Islamic banks but on the other hand similarities also exist between these two types of banks. Study concludes that the present financial and economic environment and existing accounting system is not proper for application of Islamic banking products like Musharakah and Mudarabah. (Hanif, 2014)

III. Objective of the Study

Research is directed to examine the financial performance of SBI and DIB. By comparison of financial ratios of selected banks, an attempt is made to find that either of the banks have similarities in their financial results or difference is spotted in the results. Study is also trying to search out which bank is superior to others in terms of Profitability ratio, and solvency. Study is also conducted for the purpose of indicating the scope of Islamic banking in India.

IV. Data and Methodology

For the purpose of study two cross countries banks are selected namely SBI from India and DIB from UAE (United Arab Emirates). SBI is working under conventional system of banking. The oldest bank still in existence in India is SBI which was established in 1806 as Bank of Calcutta.[2] DIB is also the oldest and the largest Islamic bank of UAE which is working under Islamic banking system. It is also a first full service Islamic bank in the world established in 1975.[3]

Financial data of both the banks are collected for the last five year and it is mentioned in study as year1, year2, year3, year4, year5 in ascending order because SBI follow Accounting year (1st April to 31st March) while DIB follow Calendar year (1st January to 31st December). Hence, data of SBI is from 2014-15 to 2018-19 and that of DIB is from 2014 to 2018.

Major focused area of the study is Profitability and Solvency for comparison of financial position of banks. Return on Assets (ROA), Return on Deposit (ROD), Profit Margin (PM), Assets Utilisation (AU), Operating Efficiency Ratio (OER) are used to check the Profitability of banks. To check the solvency of banks, Bankometer model is used which consisted of different parameters namely: Capital Adequacy Ratio (CAR), Capital Assets Ratio (CA), Equity to Assets Ratio (EA), Non-performing Loan to Total Loan Ratio (NPL), Cost to Income Ratio (CI), and Loan to Assets Ratio (LA).

V. Analysis and Interpretation

Profitability Criteria

Table1: Return on Assets (ROA) of SBI and DIB

Bank	Year1	Year2	Year3	Year4	Year5	Mean
SBI	0.64	0.44	0.39	-0.19	0.02	0.26
DIB	2.26	2.56	2.31	2.17	2.24	2.31

In the above table1 Return on Assets is compared to both the banks for selected years. It is calculated by dividing net profit by total Assets. It is disclosed the earning capacity by using available assets to the bank. There is a vast difference marked among the return on assets of SBI and DIB for all the years and DIB leads SBI in all periods. In year4 SBI has ratio in negative value as it

[2] https://www.gkduniya.com/bank-india

[3] https://en.wikipedia.org/wiki/Dubai_Islamic_Bank

incurred a loss in that year. Two main reasons found for the loss from the annual report and other sources are that in year4 BMB (Bharatiya Mahila Bank) is merged with SBI on 1st April 2017[4] and due to that procedure heavy operating expense is incurred.

Table2: Return on Deposit (ROD) of SBI and DIB

Bank	Year1	Year2	Year3	Year4	Year5	Mean
SBI	0.83	0.57	0.51	-0.24	0.03	1.71
DIB	3.04	3.49	3.31	3.06	3.21	3.22

In comparison to SBI, DIB is also leading in terms of Return on Deposit. On average of selected range of periods DIB earns 3.22% return on total deposits received from the customers while that of SBI earns 1.71%. Islamic banks work on profit and loss basis rather than interest even though earnings of Islamic bank are much better than the conventional bank.

Table3: Profit Margin (PM) of SBI and DIB

Bank	Year1	Year2	Year3	Year4	Year5	Mean
SBI	7.49	5.19	5.97	-2.47	0.31	3.30
DIB	44.03	50.88	46.90	44.16	42.66	45.72

Profit margin ratio of DIB is too higher than SBI. Average Profit margin ratio of SBI and DIB is 3.30% and 45.72% respectively. Higher profit margin ratio indicates that bank earns maximum profit by cutting its expenditures at optimum level and making profitable investment. Based on the analysis this difference it is also assumed that Islamic bank makes an investment on Profit and loss basis which increases the possibilities of high profit at the risk of high loss while Conventional bank advances money on fixed rate of interest due to this it can't get an advantage of higher return.

Table4: Assets Utilisation (AU) of SBI and DIB

Bank	Year1	Year2	Year3	Year4	Year5	Mean
SBI	8.54	8.49	6.49	7.67	7.60	7.76
DIB	5.14	5.03	4.94	4.92	5.24	5.05

Here, SBI is leading in term of Assets Utilisation to DIB. Average ratio of Assets Utilisation of SBI and DIB is 7.66 and 5.05 respectively. This ratio indicates that how much the banks utilise their assets to earn maximum revenue and profit.

Table5: Operating Efficiency Ratio (OER) of SBI and DIB

Bank	Year1	Year2	Year3	Year4	Year5	Mean
SBI	22.10	21.78	26.48	22.61	24.92	23.58
DIB	32.10	29.46	26.60	22.90	19.80	26.17

From the above table we can see that in early previous year there was a difference between the two said banks on the ground of operation efficiency but now a days it is not more we may assume that with the emergence of online banking system now days there is not much significance difference between the two banks. This shows the operation performances of activities are more or less similar to each other.

Solvency Criterion

Table6: S-score of SBI and DIB

Bank	Year	1.5*CA	1.2*EA	3.5*CAR	0.6*NPL	0.3*CI	0.4*LA	S-score (Total)	Mean S-score
SBI	1	9.41	0.044	44.77	1.27	6.63	25.39	87.514	89.12
	2	9.58	0.041	48.79	2.29	6.53	25.92	93.151	
	3	10.44	0.035	47.46	2.06	7.94	23.22	91.155	
	4	9.51	0.031	44.59	3.44	6.78	22.4	86.751	
	5	9	0.029	44.98	1.81	7.48	23.75	87.049	
DIB	1	18.07	17.15	52.15	0.95	9.63	25.46	123.41	131.22
	2	19.46	18.25	54.95	0.58	8.84	27.26	129.34	
	3	21.96	18.7	63.35	0.16	7.98	27.86	140.01	
	4	19.68	16.72	59.5	0.11	6.87	27.25	130.13	
	5	20.67	18.31	61.25	0.09	5.94	26.95	133.21	

In table6, S-score of the SBI and DIB is calculated for the selected range of periods by Bankometer model. S-score is the indicator of solvency of the banks by disclosing financial position. S-score consisted of 6 different parameters like Capital to Assets ratio, Equity to Assets Ratio, Capital Adequacy Ratio, Non-performing to Loan Ratio, Cost to Income Ratio, and Loan to Assets Ratio. Any bank has not S-score below 50 which means that they are not facing any financial crisis. Higher S-score indicates healthy financial position. DIB in all years have more than 100 and it shows that bank is more financially sound than SBI as it has S-score less than 100 in all years.

[4]https://economictimes.indiatimes.com/industry/banking/finance/banking/bharatiya-mahila-bank-to-be-merged-with-sbi-from-april-1/articleshow/57758599.cms?from=mdr

VI. Conclusion and Results

- Performance of DIB is found appreciable in comparison of SBI on the ground of profitability criteria
- DIB leads SBI in term of Return on Deposits, Return on Assets and Profit Margin ratio. Major differences found in the results of two banks.
- SBI overtakes to DIB with regards to Assets Utilisation and it is the only criterion where SBI is leading.
- No significance difference is found in the results of Operating Efficiency Ratio of two banks.
- Solvency of DIB is sounder than SBI as DIB has average S-score 131.22 while SBI has average S-score 89.12 which is also in safe area.
- It is also revealed from the analysis that NPA problem is increasing year by year in SBI while DIB has better recovery system of Advances as its NPA decreased year by year.

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