Performance Analysis of UAE Banks-An Exploratory Study

K. Ravichandran[1] & H. I. Ahmad[1]

[1] School of Management, New York Institute of Technology, Abu Dhabi Campus, UAE

Correspondence: K. Ravichandran, School of Management, New York Institute of Technology, Abu Dhabi Campus, UAE. Tel: 97-124-048-760. E-mail: kravicha@nyit.edu

Abstract

In this research study, we propose an alternative empirical technique for the performance of UAE top 5 banks (initially) in comparison with global banks. The comparative ratio analysis has been performed and the UAE based banks are ranked as per their performance. The findings of this appraoch are important in the context recent banking and financial crisis, the methodology can be used as a pedagogical benchmarking exercise in or outside the class room at undergraduate and graduate level and can also serve as an important input for performance analysis research studies.

Keywords: financial performance, financial ratios, commercial banks, performance evaluation, UAE

1. Introduction

Financial ratios are tools to analyze the performance of a company and are mostly drawn from two key financial statements; statement of financial position and income statement, Gitman (2009). The analysis helps identify the weak and strong performance areas of a firm, James (2013). And, this assist management to determine the direction of the company, Payne (2011). The results are useful for decision making purposes Madura (2009). With the help of ratios a comparison can be made of the pre- and post-action results. Hence, they are helpful in identifying success or otherwise of a particular choice of action.

When it comes to financial institution performance analysis, Elizabith and Greg (2004) showed that all financial performance measures such as interest margins, return on assets, and capital adequacy are positively correlated with customer service quality scores. And, Arzu and Gokhan (2005) discussed the asset and liability management in financial crisis. They argued that an efficient asset-liability management requires maximizing bank's profit as well as controlling and lowering various risk, and their study showed how shifts in market perceptions can create trouble during crisis. Bayraktar and Wang (2004), investigated firstly the impact of foreign bank entry on the performance of domestic banks, and secondly how this relationship is affected by the sequence of financial liberalization. The authors indicated that the sequence of financial liberalization matters for the performance of domestic banking sector. After controlling for macroeconomic variables and grouping countries by their sequence of liberalization, foreign bank entry has significantly improved domestic bank competitiveness in countries which liberalized their stock potentially low profits, compared to other banks. A high ATD ratio presents the risk that some loans may have to be sold at a loss to meet depositors' claims. Misir (1998) have used this ratio for measuring liquidity of a bank.

From the merging market standpoint, Mohammad Omar Faruk (2014) made a comparative study on the Bangladeshi banks performance using Profitability Ratio, Liquidity Ratio, Risk Measurement Ratio and DuPont Analysis and reported the results based on the these ratios. A comparative analysis of commercial banking performance in Bangladesh was conducted by Malek (2005). The author studied Nationalized Commercial Bank, Local Private Commercial Banks and Foreign Commercial Banks operating during 1999 to 2002 and noted that the foreign banks outperformed the local banks.

The macroeconomic changes in the UAE has led to a strong growth in the banking sector. According UAE central bank, the assets grew at the rate 36% since 2008. In the year 2013 the deposits grew at 8.8%, loan and advances to 7.2% and the non-resident deposits grow at 10% depicting this growth phenomenon. And, making UAE based banks performance in comparison with global banks an interesting area of study.

From the perspective of Basel III, the capital requirements present an opportunity for Middle East banks and regulators to embrace new rules and improve the sector's asset quality and risk-return profiles. The Basel III

Guidelines maintains the amount of minimum capital required at 8% of risk weighted assets. he total amount of Tier 1 capital now required under Basel III Guidelines is 6% out of which Core Tier 1 is required to be 4.5% (against the Basel II requirement of 2%). The Core Tier 1 can consist of ordinary share capital and retained earnings. The Additional 1.5% Tier 1 capital may consist of ordinary shares/retained earnings (if the bank so chooses), but other instruments are permitted to make up the difference. The criteria for inclusion in Core Tier 1, Additional Tier 1 and Tier II are detailed in the Basel III Guidelines. At present the minimum capital requirement in the UAE is 12% and Tier 2 capital under the UAE Central Bank rules can only be a maximum of 67% of Tier 1 capital. Considering that many of the UAE local banks already have high level of capital adequacy, the Basel III changes may not substantially impact the requirements of capital profile of the local banks. The Basel III Guidelines now proposes two liquidity constraints on a bank's portfolio: (a) the Liquidity Coverage Ratio (LCR); and (b) the Net Stable Funding Ratio (NSFR). The former is designed to promote banks' short-term resilience to liquidity shocks, whilst the latter is designed to address liquidity mismatches and aims to give banks an incentive to fund themselves on an on-going basis with more stable sources of funding. Banks in the UAE have sizeable capital buffers by international standards. UAE Banks are holding high levels of high-quality capital. UAE capital adequacy frameworks are broadly in line with the Basel II accord and are moving toward Basel III regulations. The current high capitalization of UAE banks will make it easier for them to move to and comply with Basel III standards. UAE banks' gross exposures are concentrated in claims on corporates, sovereigns, and public sector entities. Net exposures after credit risk mitigation (CRM) represented about 90 percent of gross exposures at end-2013. Total provisions in UAE banks generally fully cover nonperforming loans (Gurauv Jain & Sakshi Puri, 2014; IMF, 2014).

Predicting the profitability and efficiency of banks, searching for some key banking characteristics is an important area research. For this purpose, Bashir (2001), examined the determinants of Islamic banks' performance across eight Middle Eastern countries between 1993 and 1998. The results indicate that high leverage and large loans to asset ratios lead to higher profitability. The results also indicate that foreign-owned banks are more profitable than their domestic counterparts. Everything remaining equal, there is an evidence that implicit and explicit taxes affect the bank performance measures negatively. Moreover, favorable macroeconomic conditions impact performance measures positively. Even stock markets are complementary to bank financing. Advance to deposit (ATD) ratio is the most commonly used liquidity ratio of a bank. Misir (1998) and Hossain and Bhuiyan (1990), have used this ratio for measuring liquidity of a bank. Federal Reserve Bank of Dallas also uses this ratio. A low ratio of ATD indicates excess liquidity.

This research study is different   from all the previous comparative performance analysis studies, here, we first discuss the performance of UAE based banks in comparison with top global banks calculated through profitability, credit, liquidity, CAPEX ratios and benchmarking ratio like Price to Earnings and Price to Book. Finally, we present the final ranking of the UAE based banks. The rest of the paper is organized as follows. In the second section of this paper the data and methodology are discussed. Empirical results are presented in the third section. And, fourth section concludes this paper.

2. Data and Methodology

This paper tries to compare the UAE banks with the top five global banks. The top ten global banks were identified based on their total assets (http://www.relbanks.com/worlds-top-banks/assets) and out of that five banks namely Agricultural Bank of China Ltd (ABCL), BNP Paribas SA (BNP FP), Bank of China Ltd (BOC), China Construction Bank Corp. (CCBC), Industrial & Commercial Bank of China Ltd. (ICBC) were chosen based on the data availability. And, the top five UAE banks namely Abu Dhabi Commercial Bank PJSC (ADCB), Dubai Islamic Bank PJSC (DIB), Emirates NBD PJSC(ENBD), First Gulf Bank PJSC(FGB), National Bank of Abu Dhabi PJSC (NBAD) were also identified and five years financial (2010- 2014) and key ratios were collected from Bloomberg and the analysis were conducted based on these. Based on the various ratio averages of top global banks UAE banks were ranked and the best banked is identified through this exercise.

3. Empirical Analysis

In this section we present the and discuss the analysis obtain through different performance ratios like profitability, Credit, liquidity, CAPEX ratios and Du Pont analysis.

3.1 Profitability

Table 1. Profitability ratios

	Global Banks					UAE Banks				
Financial ratio's	ABCL	BNP	BOC	CCBC	ICBCL	ADCB	DIB	ENBD	FGB	NBAD
Return on Common Equity	20.81	9.85	16.7	21.08	20.88	10.5	14.2	9.35	17.3	18.06
Return on Assets	0.99	0.32	1.08	1.35	1.29	1.14	1.59	1.02	2.8	1.74
Return on Capital	7.53	0.56	5.37	8.81	7.78	3.45	7.82	3.31	10.2	5.31
Operating Margin	38.7	20.4	46.7	51.76	53.04	27.52	35.7	28.84	59.2	53.07
Net Income Margin	30.09	14.1	34.7	39.38	41	31.15	37.8	31.4	60.1	51.55
Net Income to Common Margin	30.09	13.7	34.7	39.38	41	31.15	37.8	31.4	60.1	51.55
Dvd. Payout Ratio	26.15	32.9	40.6	43.51	41.62	0.78	0.62	0.94	0.29	2.89
Sustainable growth	14.24	6.56	10	12.04	12.36	32.48	53.5	43.52	33.8	22.3

From the profitability ratio perspective, it is evident the UAE banks are performing better than that of the global banks in terms of returns, net income and sustainability. But the UAE banks are far behind when it comes to the dividend payout ratio. Keeping the shareholders happy is the important objective of financial management, but in UAE the story is different, most of the banks are partly government owned or the major shareholders are the rulers of the state, so offering less dividend will not affect the company in a big way. Another perspective on this can be the growth opportunities (Expo: 2020 etc.) that are present in the UAE perhaps influence management decision on dividend.

3.2 Credit

Table 2. Credit ratios

	Global Banks					UAE Banks				
Financial ratio's	ABCL	BNP	BOC	CCBC	ICBCL	ADCB	DIB	ENBD	FGB	NBAD
Total Debt/EBIT	7.7	161.1	10.9	5.6	-6.9	16.3	8.4	22.3	4.6	13.9
Net Debt/EBIT	-10.9	144.3	-6.6	-5.9	6.6	10.5	10.8	11.2	16.2	10
Net Debt/Equity	252.8	1350	131.2	150.5	166.5	42.7	52.9	76.4	49.7	60.5
Net Debt/Capital	-95.3	82.6	-42.8	-63.2	62.8	16.7	26.9	26.4	29.2	18.3
Tot loan/tot deposits	2	2.9	1.8	1.9	2	1.2	0.9	1.1	0.9	0.9

UAE banks net debt to capital was surprisingly high. Overall, debt levels in UAE banks are considerably high when compared to the global banks. And the good news to the UAE banks is that their total loan to deposits ratio is at par with the global banks.

3.3 Liquidity

Table 3. Liquidity ratios

	Global Banks					UAE Banks				
Financial ratio's	ABCL	BNP	BOC	CCBC	ICBCL	ADCB	DIB	ENBD	FGB	NBAD
Long-Term Debt/Equity	54.9	768.2	49.6	23.1	17.2	43	53	76	50	60.5
Long-Term Debt/Capital	19.9	48.42	15	9.66	6.13	17	27	26	29	18.3
Long-Term Debt/Total Assets	2.86	30.06	3.32	1.48	1.08	5.5	6.1	8.3	8.2	6.02
Total Debt/Equity	174	151.9	221	142	173	195	86	187	71	236
Growth (YoY)	18.3	-5.77	14.8	11.3	-3.7	-6	5.6	-14	15	2.31
Total Debt/Capital	62.8	93.31	68.1	58.4	62.9	65	44	62	41	69.5
Total Debt/Total Assets	8.93	59.04	14.9	9.16	10.9	23	9.9	20	12	23
CFO/Total Liabilities	-1.96	1.45	-0.74	-0.59	-1.2	2.2	0.2	1.4	3.4	2.17
CFO/Capex	-8.97	17.18	-2.94	-2.53	-9	24	-2	4.8	33	6.52
Common Equity/Total Assets	2.36	3.32	6.43	6.44	6.22	11	11	11	16	9.99

Form the liquidity point of view the debt level is the issue with the UAE banks and the growth rate of the UAE banks is also at par with that of the global banks.

3.4 Dupont

Table 4. Dupont ratios

	Global Banks					UAE Banks				
Financial ratio's	ABCL	BNP	BOC	CCBC	ICBCL	ADCB	DIB	ENBD	FGB	NBAD
EBIT/Revenue %	38.7	20.4	46.7	51.8	53	27.5	35.7	28.8	59.2	53.1
Revenue/Avg Assets	0.1	0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0
Avg Assets/Avg Equity	20.1	32.4	15.5	15.7	16.2	9.6	9.3	9	6.1	10.3
Adjusted Return on Equity	20.7	10.1	16.7	21.1	20.7	10.5	14.3	9.4	17.3	18.1
5 Year Average Adj ROE	20.7	12.5	15.6	20.3	20.4	12.6	18	8.9	18.5	22.2
Payout Ratio	26.2	32.9	40.6	43.5	41.6	32.5	53.5	43.5	33.8	22.3
Sustainable Growth Rate	14.2	6.6	10	12	12.4	7.5	6.8	5.7	11.8	14.2

The Du Pont analysis is a method of financial performance measurement that was started by the DuPont Corporation (Investopedia) in the 1920s. With this method assets are measured at their gross book value rather than at net book value in order to produce a higher return on equity (ROE). It is also known as "DuPont identity". From the above analysis, it is inferred that the ROE of ADCB and ENBD banks were less than the industry average. Also we can find that all the banks were performing well and their growth also seems to be good except ENBD, where the performance is not high when considered the industry.

3.5 Capex

Table 5. Capex ratios

	Global Banks					UAE Banks				
Financial ratio's	ABCL	BNP	BOC	CCBC	ICBCL	ADCB	DIB	ENBD	FGB	NBAD
Tier 1 Risk-Based Capital Ratio	8.6	10.7	10.1	10.5	10.4	14.8	13.7	12.5	17.3	15.2
Total Risk-Based Capital Ratio	10.8	13.4	12.8	12.9	13	18	16.4	17.9	19.3	18.8
Tot loan/tot deposits	58.2	126.2	70.3	63.2	61.3	126.5	87.9	115.2	100.2	103
Non-Perf Assets/Total Assets	3.2	1.8	0.9	0.8	0.9	3.4	4.7	6.1	1.6	1.3
Non-Perf Assets/Total Loans	5.5	5.4	1.7	1.6	1.8	4.7	7.3	8.1	2.3	2.2
Loan Loss Reserves/Non-Perf Assets	178.8	70	176.6	190.5	178.2	101.2	207	76.8	135.7	117.2
Loan Loss Reserves/Total Loans	6.3	3.6	2.5	2.7	2.6	3.7	11.9	4.4	2.6	2.4
Cap & Loan Loss Res/Non-Perf Assets	630.1	328.3	1113.9	1079.4	1061.4	664.5	514.1	582.4	1606.7	1011.4
Prov for Loan Losses/Total Loans	1.1	0.7	0.3	0.6	0.5	1.7	1.3	1.7	1.4	0.8
Actual Loan Loss/Prov for Loan Loss	6.1	90.5	34.8	21.7	28.8	41.8	12.4	6.9	48.2	31.5
Loan Loss Coverage	2341	4.5	47.5	43	36.5	24.4	359.5	121.2	38.2	35.7

CAPEX ratios are basically measure the funds used by a company to acquire or upgrade physical assets such as property, industrial buildings or equipment. This type of outlay is made by companies to maintain or increase the scope of their operations, when this is applied to banks the asset performance is mainly considered. It is found that the risk based assets are considerably very high in the UAE banks and also in the risk in theTier1 ratio with UAE banks is high when compared to the global industry average.

3.6 Bench Mark Ratios

Table 6. Bench mark ratios

	Global Banks					UAE Banks				
Financial ratio's	ABCL	BNP	BOC	CCBC	ICBCL	ADCB	DIB	ENBD	FGB	NBAD
Price/EPS	43.8	21.1	49.9	52.6	54.8	33.7	33.5	25.7	58.2	50
Price/Book	6.5	9.3	5.9	8.1	8.5	11.8	10.7	8.3	10	10.5

Except ENBD all the UAE banks were performing in line with the industry standard.

Table 7. Best Banks by order of their performance compared to top global banks derived from the period (2010-2014)

Key Parameters	Ranking of UAE Banks				
	ADCB	DIB	ENBD	FGB	NBAD
Average	3.29	3.76	4.38	1.61	1.93
Ranking	**3**	**4**	**5**	**1**	**2**
	ADCB	**DIB**	**ENBD**	**FGB**	**NBAD**

The ranking on various financial ratios (see Appendix) of UAE banks infers that the top performing bank is UAE is First Gulf Bank followed by NBAD and the lease performing bank was ENBD.

4. Discussion and Conclusion

Efficient performing bank is identified through their Asset Performance (Arzu & Gokhan, 2005), from the analysis it is evident the best performing bank in UAE is First Gulf Bank. All the UAE are performing almost to the industry standards but the asset performance and total loans should be checked and kept under control. With the BASEL II norms fully implemented in UAE, it is important to check the asset performance by lowering the risk level in the Tier1 assets.   Also the growth of the UAE banks YoY was considerably underperforming, so the UAE banks has to take steps to improve their performance in order to keep their race against the global banks. The current high capitalization of UAE banks will make their transition towards Basel III compliance easier.

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Appendix

Key Parameters	RANKING of Banks				
	ADCB	DIB	ENBD	FGB	NBAD
Market Capitalization	4	5	3	2	1
Book Value of Equity	3	4	5	1	2
Total Deposits	3	4	5	1	2
Total Loans	3	4	5	1	2
Total Assets	3	4	5	1	2
Net Revenue	4	3	5	1	2
Growth %, YoY	4	3	5	2	1
Profit bef. Provisions	3	4	5	1	2
Margin %	3	5	4	1	2
Operating Income	4	3	5	1	2
Margin %	3	4	5	1	2
Net Income Before XO	3	4	5	1	2
Margin %	3	4	5	1	2
Adjusted EPS	4	5	3	1	2
Growth %, YoY	3	4	5	1	2
Tier 1 Capital Ratio %	3	4	5	1	2
Total Capital Ratio %	3	4	5	1	2
+ Cash From Operations	4	5	2	1	3
+ Capital Expenditures	3	4	5	1	2
Free Cash Flow	3	4	5	1	2
Market Capitalization	4	5	3	2	1
Free Cash Flow Yield	3	4	5	1	2
Return on Common Equity	4	3	5	1	2
Return on Assets	4	3	5	1	2
Return on Capital	4	3	5	1	2
Operating Margin	3	4	5	1	2
Net Income Margin	5	3	4	1	2
Net Income to Common Margin	5	3	4	1	2
Dvd Payout Ratio	3	4	2	5	1
Sustainable growth	4	1	2	3	5
Return on Common Equity	3	4	5	2	1
Return on Capital	3	4	5	2	1
Operating Margin	4	2	5	1	3
Price/EPS	4	3	5	1	2
Price/Book	3	4	5	2	1
Total debt	3	4	5	2	1
Short-Term Debt	3	4	5	1	2
Long Term Debt	3	4	5	2	1
Total Debt/EBIT	3	4	5	2	1
Net Debt/EBIT	3	4	5	2	1
Common Equity/Total Assets	3	4	5	2	1
Net Debt/Equity	5	1	3	2	4
Net Debt/Capital	5	1	4	2	3
Long-Term Debt/Equity	5	1	4	2	3
Long-Term Debt/Capital	3	4	5	1	2
Long-Term Debt/Total Assets	1	3	5	2	4
Total Debt/Equity	1	4	3	5	2
Growth (YoY)	3	4	5	1	2
Total Debt/Capital	4	2	3	1	5

	ADCB	DIB	ENBD	FGB	NBAD
Total Debt/Total Assets	1	4	2	5	3
CFO/Total Liabilities	2	5	3	4	1
CFO/CapEx	4	5	2	3	1
Common Equity/Total Assets	3	4	5	1	2
Net Inc to Comn/Pre-Tax Profit %	3	4	5	1	2
Normlzd Net Inc/Net Inc to Cmn	3	4	5	1	2
EBIT/Revenue %	4	5	1	2	3
Revenue/Avg Assets	3	4	5	1	2
Avg Assets/Avg Equity	4	3	5	1	1
Adjusted Return on Equity	2	3	4	1	5
5 Year Average Adj ROE	3	4	5	2	1
Payout Ratio	3	5	4	2	1
Sustainable Growth Rate	3	5	4	2	1
Tier 1 Risk-Based Capital Ratio	3	5	4	2	1
Total Risk-Based Capital Ratio	3	4	5	1	2
Tier 1 Capital	3	4	5	2	1
Risk based cap	3	4	5	2	1
Risk-Weighted Assets	3	4	5	1	2
Tot loan/tot dep	5	1	3	2	4
Non-Perf Assets/Total Assets	3	4	5	2	1
Non-Perf Assets/Total Loans	3	5	4	2	1
Loan Loss Reserves/Non-Perf Assets	3	4	5	1	2
Loan Loss Reserves/Total Loans	3	5	4	2	1
Cap & Loan Loss Res/Non-Perf Assets	3	4	5	1	2
Prov for Loan Losses/Total Loans	4	3	5	2	1
Actual Loan Loss/Prov for Loan Loss	3	5	4	2	1
Loan Loss Coverage	3	4	5	1	2
Average	3.289474	3.763158	4.381579	1.618421	1.934211
Ranking	**3**	**4**	**5**	**1**	**2**
	ADCB	**DIB**	**ENBD**	**FGB**	**NBAD**

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