EVALUATING THE PERFORMANCE OF GCC BANKS USING CAMEL FRAMEWORK

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ABSTRACT

The economic importance of banks to developing countries may be viewed as promoting capital formation, monetization, influencing economic activity, encouraging innovation and facilitator of monetary policy. Banking sector performance evaluation is an effective measure and indicator to check the soundness of economic activities of an economy. This study attempts to evaluate bank's performance of the GCC region using CAMEL framework. The study examines 12 conventional banks in six GCC countries where year-end financial data from the years 2008 until 2012 were gathered from the banks' annual reports and Thomson Reuters, Data stream in the library of Universiti Utara Malaysia. The study finds that capital adequacy parameters of GCC banks are above the minimum requirement, while asset quality in the GCC countries affected the bank's performance except in Saudi Arabian banks. Management quality affects banks performance in all GCC countries except in Saudi Arabian banks. Earning ability is efficient with the banks performing well during the five years under investigation. Liquidity stood in the top position for all the 12 banks in GCC countries. The GCC countries could further improve the performance of their asset quality and management quality, using CAMEL framework as it is the best model and useful in evaluating banks performance.

Keywords: bank performance, capital adequacy, asset quality, management quality, earning ability and liquidity.

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Mohammed Ali Ahmed Al-Musai

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LIST OF ABBREVIATIONS

Abbreviation	Description of Abbreviation
UUM	Universiti Utara Malaysia
GCC	Gulf Cooperation Council
CAMEL	Model of Rating System Analysis
CAR	Capital Adequacy
AQ	Asset Quality
MQ	Management Quality
ROE	Return On Equity
ROA	Return on Assets
LR	Liquidity Risk
NPLs	Non-performing loans
GDP	Gross Domestic Product
UAE	United Arab Emiratis
KSA	Kingdom Saudi Arabia
UFIRS	Uniform Financial Institution Rating System
AIA	American International Assurance
IMF	International Monetary Fund
NBK	National Bank of Abu Dhabi
CAD	Commercial Bank of Dubai
RD	Riyadh Bank
ARB	Arab National Bank
GBK	Gulf Bank of Kuwait
NBK	National Bank of Kuwait
BM	Bank Muscat
NBO	National Bank of Oman
CBQ	Commercial Bank of Qatar
DB	Doha Bank
NBB	National Bank of Bahrain
BBK	Bahrain Bank and Kuwait

CHAPTER ONE

INTRODUCTION

1.0 Background of Study

Currently banks play an important role in our society and it is difficult to imagine the growth of the economy without banks. The banking sectors acts as the life blood of modern trade in our economy. The working of the banking system assist governments to stimulate the economy of any specific country, also through the banks all of business and finance transactions are being involved (Faizulayev, 2011).

Banks are a significant part of the financial system which plays an important role in a country's economic development. A country's economy will be affected if the banking industry is not performing well. The economy will experience slow growth or if the performance is not efficient, that may also slow affect the growth of the global economy as banks profitability is a predictor for any financial crises in the future. Banks performance becomes an important parameter which could help banks and give them an idea about the current condition of the banking industry (Barros, Ferreira and Williams, 2007).

Ratios such as capital adequacy, asset quality, management, earnings and liquidity risk, are used as parameters to measure bank's performance. In the beginning of 1970, federal regulators in USA developed the CAMEL rating system to evaluate the structure of bank examination process. A CAMEL framework is useful in investigating and evaluating the soundness of the banking safety and reduces the possible risks which may cause bank

failures. In the U.S, it is also useful as supervisory instrument and this way is helpful as it is a universally standard rating which supplies elasticity between both sides. Finally it is the main framework in evaluating bank performance (Dang, 2011).

Since 1979, the Uniform Financial Institutions Rating System (UFIRS) was adopted to provide federal bank regulatory agencies with a framework for rating financial conditions and to evaluate the performance of individual banks (Barr, Seiford, and Siems, 1993).

1.1 Development of Banking in Gulf Corporation Council (GCC) Countries

The operations of the banking business in GCC countries had existed since 1918. Bahrain was the first bank to be established in June 1900 and July 3, 1920the bank's premises were opened officially although banking services started only on July 20 of the same year (Standard Chartered Bank, 2013) its performance has been rated high in the banking sectors. There are banks that have large capital bases in GCC countries.

In the previous twenty years, the Gulf Corporation Council (GCC) region had experienced fast economic and social demographic changes. Most of the world's countries' attention has been focused on the Gulf countries' economies not only as the exporters of oil and gas but as a place of investment destinations with strong infrastructure projects, financial services, banking sectors and booming tourism.

On May 25, 1981, six countries of the Arab Gulf region (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates) ratified the charter that established the Cooperation Council for the Arab States of the Gulf (Laabas and Limam, 2002).

Gulf region financial system is primarily bank-based and their capital markets are still undergoing various development structures. Since 1990, there are a lot of reforms policies have been applied to liberalize the financial markets, by the rearrangement and deregulate the banking industry in GCC region will promote efficiency and achieve regional economic integration in the GCC. The policy making structures have been working together to reach the goal of establishing a single currency and a single market and towards agreement to implementing monetary union for all GCC states (Laabas and Limam, 2002).

The reforms of financial sectors in the GCC were intended to promote competitive stable and excellent performing in making environment of commercial banks to control the financial system. With regard to the global financial markets, commercial banks and institutions in the GCC countries have been applying strategies of their western banks counterparties by adopting new technology and using advanced risk management system to recognize and diversify their product mix, and adhering to international risk-based capital standards such as (Basel I,II and III). Overall, the objectives of financial sectors in GCC countries is to upgrade and enhances the economic integration on all gulf countries and promote efficient banking system to improve the banking industry to be more efficient in GCC countries (Laabas and Limam, 2002).

In addition, there have been done researches on banking performance and efficiency in GCC countries, in particular. As stated earlier, GCC has established strong reforms since the early of 1990, reflecting a dramatic change in the operating environment and competitive structure of the banking industry in the Gulf countries.

The banking sector in GCC region is owned by locals because the entry barriers and licensing boundaries for the foreign ownership. For example in Qatar foreigners are not allowed to own more than 49% while in Oman only 35% (Alkassim, 2005).

There are several features of banking industry in GCC region. All lending activities are focused in real estate, construction and consumer loans. All GCC countries are dependent on oil sector activities. Lastly, the industry is highly protected from foreign competition and dominated by the governments of the GCC. There are more banks stocks traded in market of GCC than stock of another industry (Sturm, Strasky, Adolf and Peschel, 2008).

The GCC region has been long standing and active traditionally in commerce and financing. Banking has contribution an important portion in the growth for the region for long time. Currently the sectors have experienced growth in both size and sophistication of the banking industry. There are 45 listed banks across the six GCC countries which has an aggregate asset size of USD 345.3 billion at the end of 2004, with a growth of 14.8% over 2003. These banks have net profit of USD 8.9 billion in 2004, having a grown by 38.6 % over 2003.

GCC banks shown high financial performances, achieving an average return about 1.5%-2% during the past decades. The most profitable banks are Kuwait, Saudi Arabia and UAE (Sturm et al, 2008).

Asset quality has improved in these recent year while non-performing loans for banks have traded down more than having from 7.9% of gross loans and NPL as a proportion of gross loans remain the highest in Oman, while during same period also it was the

lowest in Saudi Arabian banks, however in UAE the NPL gross loans was the steepest fall as stated in the report. The GCC banks have traditionally seen a healthy level of liquidity because of the result of the boom in oil prices 1970, as well as a low level of leverage. These conditions have never had to compute fiercely to attract customer deposits also with a high stability of these deposits. (GCC Banking Sector, 2005).

While GCC countries already achieved significant economic strategy, and development also integration during the thirty years, there still little substantial differences across individual economies. The macro-economic environment is operating efficiently over the past decades in all GCC countries (Berger and DeYoung, 2001).

Banking performance evaluation must be existing to ensure importance of the conditions for estimating cost and profit efficiencies. The evaluation of banking sectors provides a unique opportunity for measurement of the individual banks operating in GCC countries.

1.2 Problem Statement

In Gulf countries, the financial sector is influenced by the bank sector institutions. The GCC region has the largest banking sector with assets close to 260% of GDP. The financial crises on 2008 had affected the wholesale banking sector in Bahrain and UAE (Al-Hassan, Oulidi and Khamis, 2010). Therefore, banks' performance is very important to the consumers and individuals of the bank's deposits and loan services, government regulators, employees, stockholders, management and entire economy. In general bank

performance is important to individual consumers of the bank deposit and loan services as well as to the performance of the entire economy (Rahman, 2012).

According to Khamis and Senhadji (2010) and IMF (2010), the nonperforming loans increased in most GCC countries in 2009 to 4.6 percent in UAE, 3.9 percent in Bahrain, 2.8 percent in Oman, 3.3 percent in Saudi Arabia, 9.7 percent in Kuwait, 1.7 percent in Qatar (Appendices). These numbers reveal that the non-performing loans have been increased dramatically which may affect the performance of bank in the GCC countries. However, in GGC banks, there is higher capital, large size lead to higher profitability, and better asset quality, but there is higher cost-to-income ratio that leads to lower profitability (Smaoui and Salah, 2011). Therefore, there is a need for more evaluating system to measure financial problems of banks. For this purpose, Bahrain banks and institutions have been recommended to use financial ratios analysis to investigate the risks that may lead to financial problems (Najjar, 2013).

For the purpose of solving the issues and problems that face banks in GCC regarding the financial risks, a measurement tool is needed to evaluate the banks' performance. However, there are many measurement frameworks, CAMEL is considered by many writers (Prasad and Reddy 2012), (Mishra, 2012) and (Dang, 2011) as the best framework to evaluate the performance of banks and other institutions. It involves the process of evaluating capital adequacy, asset quality, management quality, earning ability, and liquidity risk. The components of CAMEL address the main issues that can face banks and lead to financial problems and sometimes to bankruptcy. Moreover, the CAMEL has not been used in evaluating the performance at banks in GCC counties, and therefore, this study is the first attempt to cover the whole six countries. Therefore, this

study is an attempt to fill the gap by using CAMEL framework to evaluate performance in GCC countries.

1.3 Research Questions

This research intends to answer the following questions:

1) Does capital adequacy affect the performance of banks in GCC countries?
2) Does asset management affect the performance of banks in GCC countries?
3) Does management quality affect the performance of banks in GCC countries?
4) Does earning ability affect the performance of banks in GCC countries?
5) Does liquidity affect the performance of banks in GCC countries?

1.4 Research Objectives

The main objective of this study is to evaluate the banks' performance in GCC area by using CAMEL rating system. The specific objectives are:

1) To determine if capital adequacy affects bank performance.
2) To determine if asset quality affects bank performance.
3) To determine if management quality affects bank performance.
4) To determine if earning ability affects bank performance.
5) To determine if liquidity risk affects bank performance.

1.5 Significance of the Study

Conducting such a research related to bank performance in GCC countries is important because the banking sector is one of the fastest growing sectors in the GCC region. Most of the empirical and theoretical studies in the GCC countries have concentrated on the comparison between the Islamic and conventional banks. Generally, non-Islamic banks have more funds to enhance the needs of most of the financial projects and to perform better in the current market.

Nevertheless, the conventional banks have various studies in aspects that affect efficiency and other performance indicators. However, studies on the level of performance that fully use the CAMEL rating system are still lacking.

This study is based on Middle-eastern banks because the GCC banking industry is protected from foreign competition and dominated by the governments of the GCC.

This study hopes to enhance the understanding on banking performance and the benefits that can be obtained from evaluating bank performance using CAMEL rating system.

To the knowledge of the author, none of the previous studies have done an evaluation of GCC bank performance using CAMEL rating system. This study aims to cover banking industry in six GCC countries and it will evaluate their bank performance.

This study examines the financial soundness of banks using financial ratios, which forms a different component of CAMEL. Evaluation is required to measure the performance of banks, which is important to many shareholders and investors.

Furthermore, mangers, suppliers and government can benefit from the bank performance evaluation because both mangers and investors are able to make better decision. For example, if the bank performance is weak, then many investors may not want to invest in that bank. Managers therefore have to find new strategies to improve the bank performance and its profitability.

1.6 Scope of the Study

This study examines only 12 conventional banks in the six GCC countries, during the period of 2008-2012, using financial ratios to evaluate banking performance under CAMEL rating system, which includes capital adequacy, asset quality, and management quality, earning ability and liquidity.

Previous studies have used financial ratios as their proxy for evaluating the bank performance in different countries. The financial ratios have been popularly used in evaluating bank performance. There are few studies on performance of GCC countries conventional banks, and not much literature on using CAMEL framework to examine bank performance in the GCC region. This study will analyze the performance of 12 conventional banks in each of the GCC countries.

1.7 Organization of the Study

This study is divided into five chapters. Chapter one discusses the background of the study and provides an overview of the GCC countries as well as the problem statement and the research objectives and questions. Chapter two explains the relevant literature on bank performance in GCC region and the empirical studies in other countries. Chapter three describes the research methodology, while chapter four discusses the results. Chapter five provides the summary and the main conclusion of the study.

CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction

This chapter focuses on the review of literature related to bank performance of GCC countries using the CAMEL framework. The chapter is broadly divided into two sections. The first section examines the theoretical literature with the basic definitions under the CAMEL framework. The second section of this chapter reviews empirical literature with related evidences and findings.

2.1 Banking Sector in GCC Countries

The GCC region has the largest banking sector with assets close to 260% of GDP. UAE and Bahrain have the least number of banks among the GCC countries. In Bahrain, banks such as Ahli united bank, National Bank of Bahrain and Bank of Bahrain and Kuwait own 40% of the total asset while the biggest bank is Arab Bank Corporation that provides off-shore and project finance services through the investment banks. The financial sector contributes 3 percent of the workforce related to the total assets at 1200 percent of GDP. The financial crises had affected the wholesale banking sector in Bahrain. In terms of which country owns the most banks in GCC countries, the first is Bahrain and this is followed by the UAE. The biggest banks in UAE are Abu Dhabi Commercial Bank, Emirates Bank International and National Bank of Abu Dhabi; these banks have 32 % of the total assets, while the UAE total percent of GDP is 140% compared to other countries in the GCC. In Kuwait, the largest banks are Kuwait

Finance House and National Bank of Kuwait, where they own half of the total assets or 42 % of both on- and off-balance sheet. Global liquidity conditions and some assets prices had strongly affected the Kuwait banking sector. Oman has the smallest banking system with a share of 66% of the GDP while its biggest banks are National Bank and Bank Muscat. These two banks own 55% of the total assets of the banking sector. The third biggest banking sector in GCC region is Qatar with assets of 94% of the GDP and the three largest banks are Doha Bank, Commercial Bank of Qatar and Qatar National Bank. Doha Bank and Commercial Bank of Qatar have close to 70% of the total assets. Foreign banks are also engaged in starting business by financing some infrastructure projects and investment. Specialized and government banks are engaged in the housing projects and development. The largest banks in Saudi Arabia are Al Rajhi Bank, Samba and National Commercial Bank. The banking sector is small compared to the other GCC countries and it accounts 45% of the total assets. There are five specialized credit financial institutions with half of the total assets compared to banking sector (Al-Hassan et al, 2010)

2.2 Overview of CAMEL Rating System

The efficiency of the financial system of any country is the key to the success of its economy. Evaluating bank performance is very important for shareholders to make better decision, and for banks to mark and re-value their performance on routine basis. There are many tools to measure bank performance and one of the methods is the CAMEL framework. Many regulators have recommended bank's management to use the CAMEL model of rating to evaluate and estimate the bank's performance. Banks use the CAMEL model to measure their competitive performance analysis which is basically the

application of some ratios namely capital adequacy, asset quality, management efficiency, earning ability, and liquidity (Rozzani and Rahman, 2013).

The CAMEL rating system was developed by federal regulators in USA in the early 1970s, for the purpose of structuring process of bank examination. The Uniform Financial Institution Rating System was assumed in 1979 to support federal bank regulatory agencies with a framework for the purpose of banks' performance and rating financial condition (Barr et al., 1993).

Barr, Killgo, Siems and Zimmel, (2002) emphasized that CAMEL rating is considered an indispensable and concise instrument for regulators and examiners. This type of rating explains and guarantees healthy situations of a bank by revising different parts of a bank based on various information, for example financial statement, cash flow, and funding resource. Furthermore, Hirtle and Lopez (1999) argued that the CAMEL rating of banks is highly trusted. Therefore, the evaluation of bank performance using this tool is useful for bank's top management for the purpose of projecting the business strategies in order to improve the bank's performance. In sum, CAMEL model consists of five components as shown in the Table 1.1.

Table 1.1
Ratios Formula

Ratios	**Formula of Ratio**
Capital adequacy	Tier1 Capital + Tier2 Capital/ Risk weighted assets
Asset quality	Non-performing Loans/ Total Loans
Management quality	Total Loans / Total Deposits
Earning ability	
ROE	Net profit After Tax/Equity Capital
ROA	Net profit After Tax/Total Assets
Liquidity	Cash & Due From Banks +Treasury Securities/ Total Assets

2.2.1 Capital Adequacy

Capital adequacy is the first component of CAMEL model. It is the capital required to maintain balance with the risks exposure of bank or any financial institution such as credit risk, operational risk and market risk in order to absorb the potential losses, and for protecting the bank debt holder, and for the purpose of meeting the requirement of statutory minimum capital which is considered as the key factor in the process of capital adequacy decision. The critical element is maintaining an adequacy level of capital according to Uniform Financial Institution Rating System 1997 (Bank and Manual, 1997).

Capital adequacy has been defined by Mithcell (1984) in terms of the ratio of capital deposit for the reason that the primary risk is a risk of depository that derived from the unexpected and considerable large level of withdrawals of deposit.

2.2.2 Asset Quality

Asset quality management has currently received much consideration in the banking industry. Asset quality is the key factor for a bank success and therefore the major cause of failure of most banks is due to the poor asset quality. Loan portfolio is the most important asset category because the greatest risk facing the bank is the risk of loan losses derived from the delinquent loans. Financial analyst and credit analyst ought to focus on the assessment of asset quality by implementing the credit risk management and evaluate the portfolio of quality of loan by using peer composition and trend analysis. The asset quality measurement is not easy because it is generally derived from the subjectivity of analyst (Grier, 2007).

Asset quality highlights the non- performing loans ratios (NPLs) that can be considered as the proxy for assets quality, credit risk, and provision to loan losses reserve.

According to UFIRS, every component in the CAMEL rating system scores from 1 to 5. In other words, the context of asset quality, a score of 1 indicates a strong asset quality with low risks of portfolio. On the other hand, a score of 5 reflects unfavorably and poor asset quality that shows bad condition for the institution.

2.2.3 Management Quality

Management quality reflects the capacity of the management and board of directors, to recognize, identify, measure, and control the risks of organizational activities to guarantee the stable, safe, sound and effective operation in compliance with appropriate regulations and laws as stated by Uniform Financial Institutions Rating System (UFIRS) 1997.

According to Grier (2007), the management quality is treated to be the most of the significant element in the CAMEL rating system due to its significant role in the success of banks. In spite of that, it is subject to measure as the examination of asset quality.

The rating of management quality as recorded by UFIRS is rated from 1 to 5. In the management quality context, rating of 1 reflects a fully effective board of directors and management and that indicates highly the management quality and the institution is in safe, stable, sound, and good financial condition. A 5 rating refers to a critically poor and deficient bank management.

2.2.4 Earning Ability (ROE and ROA)

Earning ability can be measured by the return on asset (ROA) and return on equity (ROE) as a useful indicator of bank profitability. ROA is calculated by dividing net income and total assets giving a ratio of earning that is generated from invested capital. It indicates management effectiveness in generating each dollar of investment (Hassoune, 2002). The measures of assets performance include ROA as a performance indictor and as dependent variable (Hassan and Bashir, 2003). ROE also indicates how much profit the bank has generated on money invested by shareholders and it is calculated by dividing net income by shareholders equity. ROE indicates how efficient bank management uses shareholders investments (Hassoune, 2002).

2.2.5 Liquidity Risk

Liquidity risk is measured by dividing cash and treasury securities to total assets and it is used to help assess whether the bank has sufficient amount of cash to withstand rising NPA levels while the bank manages to keep the cash and reserves above 4% (Ariffin, 2012)

2.3 Bank Performance

Olweny and Shipho, (2011) examined 38 Kenyan commercial banks during the period of 2002-2009 by using panel data to evaluate the effects of bank specific factors, such as capital adequacy, asset quality, liquidity, and operational cost efficiency. The study found that the specific factors had significant relationship on the bank's profitability while the market factors had no significant relationship on the bank's profitability. In

addition the study recommends banks to change their policies to encourage revenue diversification, also on the other side to minimize credit risk, to reduce the operational costs and to reduce their liquidity holdings.

Kumar, Harsha, Anand and Dhruva, (2012) analyzed the performance of top 12 public and private banks in India for the period from 2000 to 2011 using CAMEL approach. It was applied to evaluate the performance of banking sector in India. The study found that private banks were at the top of the list with a high performance in terms of soundness and being the best. On the other hand, public banks took a backseat and presented a low financial soundness in comparison.

Rozzani and Rahman (2013) examined the performance of both Islamic and conventional banks that were operating in Malaysia by using CAMEL rating system. The study period was from 2008 to 2011 and the results showed that both Islamic and conventional banks in Malaysia were similar in performance during that period. The study contributed to stakeholder to make better investment decisions and to enhance both Islamic and conventional banks to re-evaluate their performance.

Prasad and Reddy (2012) carried out a research for evaluating the Indian banking sector's nationalized banks and SBI group. The study used CAMEL model to measure the performance of banks. The study found that there was no significant difference between performance of nationalized banks and SBI group.

In a case study, Dang (2011) conducted a research about American International Assurance Vietnam (AIA). The study aimed to determine if the framework of CAMEL played a critical role in evaluating banking performance and supervision and to identify the benefits from using CAMEL model to evaluate other institutions as well. The study revealed that CAMEL framework was useful as a supervisory tool in the U.S. Furthermore, the study found that the approach of CAMEL analysis was useful and beneficial because it is a globally standardized rating system and provides flexibility between off-site and on-site examination.

Kumar et al. (2012) examined state bank group using CAMEL model and the study found that some banks got high rank with capital adequacy, SBP in top position while SBI was in lowest rank. The assets quality found SBBJ in the top position, SBI in lowest rank.. The study concludes SBI should improve its positions with asset quality and capital adequacy and SBBJ have to enhance its management efficiency and SBP must improve its earning quality.

Kabir and Dey (2012) examined the competitive performance of commercial banks in the private sector namely, IFIC and EXIM bank, by using CAMEL model and the findings of the study indicated that in the capital adequacy and leverage, IFIC banks performed better than EXIM. EXIM in terms of return on equity and net worth protection showed better performance than IFIC. Furthermore, asset quality of IFIC bank revealed a much stronger performance than EXIM bank. Finally, management capacity of EXIM bank was better than IFIC bank.

Aspal and Malhotra (2012) examined the banks in Indian public sector except state bank group for the period of 2007 to 2011. The study revealed that Bank of Baroda was found to be on the first position with overall composite ranking average of 6.05 because of its high performance in the asset quality and liquidity areas. Bank Andhra achieved the second position with an average of 6.15 due to its strength in management efficiency, and assets quality and capital adequacy. United Bank of India was at the bottom position with an average of 14.60 because of poor asset and earning quality. Additionally, the study remarked that United Bank of India should improve its management efficiency, asset quality, and earning quality.

Sangmi and Nazir (2010) carried a study to evaluate the financial performance of two banks operating in northern India and the researcher applied CAMEL model which was the latest model of financial analysis. The study revealed that the banks used sound and satisfactory conditions to their capital adequacy, asset quality, management capability and liquidity. It means there is a positive relationship between CAMEL framework and bank performance.

Soltani, Esmaili, Poor and Karami (2013) conducted a study by applying CAMEL model to evaluate the performance and compare the financial performance of public and private banks in Iran. The results of the study revealed that there was a significant difference between private and public banks in terms of liquidity, earning performance, and management quality. Private Banks had better performance in terms of liquidity and earning performance, and public banks had better performance in term of management quality.

Valahzaghard and Jabbari (2013) examined the performance of bank in Iran during the period of 2006 to 2011. The study used CAMEL framework which was one of the most effective models to evaluate financial performance of banks. The study revealed that asset quality had a meaningful effect on bank performance. Furthermore, the study supported the direct and meaningful effects of capital adequacy. However, the management quality and liquidity quality were rejected.

Ongore and Kusa (2013) carried out a research to evaluate the financial performance of commercial banks of Kenya. The findings of the study showed that bank specific factors were significantly influencing the performance of commercial banks in Kenya. The study concluded that the financial performance of banks in Kenya was driven mainly by board and management decisions. On other hand, macroeconomic factors did not affect banks of Kenya and had insignificant contribution.

Chowdhury and Ahmed (2009) analyzed the development and performance of private commercial banks in Bangladesh which was one of the developing countries and the banking system played a vital role in the economic development. The result of the study revealed that private commercial banks were more stable and able to achieve a stable growth of deposit, employees, branches, loan and advance, net income, and earnings per share for the period of 2002-2006.

Pinyani, Saluja, Daga and Rao (2013) studied three diverse banking models namely Islamic, American and Canadian. The objective of the study was to provide insights into how these banks performed for the period 2007–2010. The researchers had used

CAMEL model to assess the performance of three major banks under each banking model. The study suggested that despite good profit figures, the banking system may collapse if the fundamentals are not followed and risks are not properly evaluated. The study found that Canadian banking system outperformed the Islamic and American banking system in terms of liquidity, asset quality, expenses, security. Furthermore, Islamic banks performed better than the others in terms of capital adequacy and management quality.

Kouser, Aamir, Mehvish and Azeem (2011) investigated and compared the financial performance of interest-based banks and interest-free based banks operating in Pakistan. The measurement of financial performance of these two categories was assessed using CAMEL framework. The duration of the study was five years, which was from 2006-2010. The study indicated that Islamic banks in Pakistan did not have a good financial condition during the study period as compared to the conventional banks. The study suggested government should formulate Islamic economic policies to support the Islamic banking in Pakistan.

Matkar (2013) attempted to evaluate the improvement in financial performance of MSC bank in India through CAMEL framework from 2006 to 2010. The study found that MSC bank had a good performance. Fader (2001) evaluated the performance of commercial banks in Malaysia for the period from 1985 to 1997. The study examined six performance dimensions namely earning, liquidity, risk solvency, profitability and efficiency. The study used t-test to find out the significance of bank performance during the period. The study found that earning efficiency and productivity performance were

significant. The study also revealed that non-interest income, loan loss provision net interest margin and efficiency ratios, contributed to the bank's earnings performance.

Ilhomovich (2009) carried out a research to analyze and compare the performance of domestic and foreign banks operating in Malaysia for the period from 2001 to 2008. The study used CAMEL model to evaluate bank performance. The study found out that foreign banks had a strong capital but domestic banks were more profitable. Furthermore, the study showed that the existing foreign banks are affecting financial services quality in Malaysia because all banks offered better and low cost banking for customers during the competition.

2.4 Bank Performance in GCC Region

From the survey of literature, some of the studies conducted to assess bank performance in the GCC countries are reviewed in the following paragraph.

Najjar (2013) conducted a study on Bahrain banks which covered profitability management, interest rate risk management and liquidity management by using accounting ratios to investigate the performance of the banks. The study found that there was a corporate excellence in asset management and value equity shares while this analysis also can be used as a basis for identifying the bank's future bankruptcy and analyzed the market risk. The study recommended Bahraini banks and institutions to use financial ratios analysis to investigate the risk issues which will cause financial problems to the banks.

Zeitun (2012) did a study on Islamic and conventional banks' performance in GCC countries during the period of 2002 - 2009. The study used a cross sectional times series (panel data) containing 38 conventional banks and 13 Islamic banks to determine the bank performance by equity, cost to income and ownership. The study found that the banks' equity to be one of the most important ratios to enhance the profitability of conventional banks. Furthermore, the study found that cost to income had a negative and significant effect on the both types of banks. On the other hand, there was a significant relationship between the ROE of Islamic banks in terms of size, and there was no significant effect on conventional banks. Finally, the study concluded that ownership had no effect on the Islamic or conventional banks' performance.

Al-Hares, Abu Ghazaleh and El-Galfy (2012) carried out a study about the quality capital and financial performance of the Islamic and conventional banks in the GCC region. The study comprised of 55 conventional and 20 Islamic banks. The study found that the Islamic banks were affected more than the conventional banks during the financial crisis in terms of leverage and return on average equity of capital ratio. On the other hand, Islamic banks suffered more than conventional banks in terms of return on average assets and liquidity. The Islamic banks proved that it was better than the conventional banks by showing higher liquidity reserves and also maintained stronger credit and assets growth. Finally, financial ratios were used to measure and compare Islamic and conventional banks' performances.

Johnes, Izzeldin and Pappas (2009) examined the conventional and Islamic banks of the GCC countries in the period between 2004-2007. They conducted the study using both financial ratios and data envelopment analysis (DEA). Their study found that Islamic banks by financial ratios were less cost efficient and highly profitable. Islamic and conventional banks had a good and significant relationship in four of the ratios. DEA showed the gross efficiency was significantly higher in each conventional bank compared to Islamic banks. On the comparison of the two types of banks based on financial ratios and DEA efficiencies, they found a positive and significant relationship in the case of cost ratios and gross DEA efficiency. In conclusion, productivity increased slightly over the four-year period.

Islam (2003) examined the internal performance by financial ratios of domestic and foreign banks of Oman, UAE and Bahrain. The study found that the financial ratios showed an improved performance during the observed years. Also the commercial banks developed their economic parameters by adopted modern banking services. Their operations assessed by satisfactory assets quality showed high capital assets and high level of profitability. Market share measured the external performance of the bank's confidence and many banks were assessed with better progress.

According to Smaoui and Salah (2011) who investigated the characteristics and macroeconomic factors affecting the profitability of 44 Islamic banks in GCC countries during the period of 1995-2009, large size caused higher profitability and better assets quality while higher cost to income ratio caused lower profitability.

Ahmed (2008) conducted a study on the performance of the commercial and Islamic banks in Kuwait. The study found that all banks had a good and respective strength with the CAMEL factors, while Islamic banks performed better than commercial banks in term of rating on asset quality, earnings and liquidity.

Espinoza and Prasad (2010) used a dynamic panel estimated during 1995-2008 in 80 banks of GCC countries. The study found that economic development or growth was very bad because of the worsening non-performing loans. This study also investigated the impact on the NPL growth by a value at risk model. The result showed that there could be strong relationships albeit short lived feedback effect from losses in banks, economic activity and balance sheet with half elasticity of 0.4.

Khamis and Senhadji (2010) and IFM (2010) found that non-performing loans increased in most of the GCC countries in 2009 to 4.6 % and the growth percentage differ between the countries and these numbers revealed that the non-performing loans had increased dramatically which affected the banks' performance in the GCC countries.

A study conducted by Ravichandran and Sharma (2009) covered commercial banks of Saudi Arabia using CAMEL model. The study found that all Saudi Arabian banks were highly performing and there was only one area the banks should focus on which was asset quality. The study also found the banks did not concentrate on the public deposits and was very low when compared to loans. The bank that was rated high was Al Jazira bank compared to other banks in Saudi Arabia based on the CAMEL framework.

Siraj and Sudarsanan (2012) investigated the performance of Islamic and conventional banks during the period of 2005-2010 in GCC countries. The study used performance indicators such as ROA, ROE, OER, NPR and EOA. Their study found that Islamic banks used more equity finance than conventional banks. They also found there was a significant relationship between the six financial indicators, while conventional banks could not achieve the level of profitability in account towards credit losses and other impairment losses. The study found that the financial indicators were affected by financial crises.

2.5 Summary of the Chapter

The review of literature in various countries and the GCC region showed that CAMEL rating system was widely used in evaluating the bank's performance. However, the use of CAMEL framework varies among countries in the region. CAMEL rating works equally well with other kind of financial institutions.

CHAPTER THREE

METHODOLOGY

3.0 Introduction

In a contemporary banking environment, competitive banking has experienced innovations for methods to evaluate the risks and returns involved in the sector by analyzing their bank's performance. There are many statistical techniques and measurements that have been used as proxies of the bank's performance. Recently, bank regulators use financial ratios for accounting data to analyze bank performance. Adesina (2005) argued that the Nigerian banks found that financial capital adequacy, asset quality, management quality, earning ability and liquidity were useful in evaluating the bank's performance in Nigeria.

In this chapter, the data collection, sampling, variable measurement are discussed. In this study also, the financial statements of all banks in GCC countries are analyzed using descriptive and ratio analysis. The CAMEL framework is used to evaluate the GCC banks performance. The variables of CAMEL framework are capital adequacy, asset quality, management quality, earning ability and liquidity. This study, however, excludes sensitivity to market risk, which is the "S" factor under the CAMELS framework because there is no data available for this ratio. Furthermore, it is quite difficult to assess for the GCC banks at the moment. Thus, this study only adopts the CAMEL framework and the variables used within the framework are described in the subsequent section.

3.1 Data Collection and Sampling of the Study

3.1.1 Sampling

The population of this study is all the conventional banks of GCC countries. There are more than 100 conventional banks in the GCC region but this study uses data from 12 conventional banks (commercial, national, investment and government owned banks) only. They are selected based on the largest total assets in each GCC country, which comprises UAE, Saudi Arabia, Kuwait, Oman, Qatar and Bahrain. Conventional banks are different from the Islamic banks. This study also excludes Islamic banks and the other financial institutions.

Table 3.1 List of Banks in the Sample

No	Country	Names of Conventional Banks
1	UAE	National Bank of Abu Dhabi
2		Commercial Bank of Dubai
3	KSA	Riyadh Bank
4		Arab National Bank
5	KUWAIT	Gulf Bank of Kuwait
6		National Bank of Kuwait
7	OMAN	Bank Muscat
8		National Bank of Oman
9	QATAR	Commercial Bank of Qatar
10		Doha Bank
11	BAHRAIN	National Bank of Bahrain
12		Bank Bahrain and Kuwait

3.1.2 Data Collection

Whenever possible, this study used data downloaded from annual reports from websites of each conventional bank of the GCC countries. In addition, data were obtained from Thomson Reuters, Data stream in the library of Universiti Utara Malaysia (UUM). The data was for five years, which was collected from the year 2008 to 2012. The annual reports contained the income statement, statement of change in stockholders' equity, balance sheet, statement of cash flows, and also the notes to the financial statements. The data from a sample of 12 banks are collected for the period mentioned above. This provides the current study with 60 observations (N= 60).

3.2 Variable Definition

This section describes the variables used in this study. The variables used are based on the CAMEL framework, which will be explained individually. Each variable is based on a financial ratio, which is used to measure the performance of the GCC banks.

3.2.1 Capital Adequacy

Capital adequacy is a measure of overall financial strength of banks. It is vital for maintaining soundness of banking system since it acts as a cushion against bank run uncertainties (Keovongvichith, 2012).

$$\text{Capital Adequacy} = \frac{\text{Tier 1 Capital + Tier 11 Capital}}{\text{Risk Weighted Assets}}$$

Capital adequacy is important for a bank to maintain depositor's confidence and protect the bank from going bankrupt. Also it is one of the major indicators of the financial health of a bank. It is used to measure the financial solvency of banks by determining whether the risks it has incurred are adequately offset with capital and reserves to absorb potential losses. Capital adequacy is seen as cushion to save depositors and promote the efficiency and stability of financial system around the world. It also represents the overall financial condition of banks and the ability of bank management to meet the need of any additional capital. Capital adequacy identifies whether the bank has enough capital to take up unexpected losses and it acts as an indicator to bank leverage

There are two types of capital: Tier 1 Capital and Tier 2 Capital. capital tier 1 is capital which is permanently and freely available to absorb losses without the bank being obliged to cease trading also its important because it safeguarded both the survival of the bank and the stability of financial system. Tier 2 capital is used to absorb loses only in the event of a winding-up of a bank and it provides a lower level of protection for depositors and other creditors. Tier 2 comes into play in absorbing losses after Tier 1 has been lost by bank. (Ilhomovich, 2009).

Capital adequacy is very important in the banking sector because it is relevant to the equity capital and securities, which bank has as reserves against risky assets and hedge against possibility of bank failures. Basel Capital Accord established a framework to measure the bank capital adequacy standards. It also provides 8% of capital adequacy ratio which is the minimum (Ezike, 2013).

3.2.2 Assets Quality

$$\text{Asset Quality} = \frac{\text{Non-Performing Loans (NPLs)}}{\text{Total Loans}}$$

Asset quality management has currently received much consideration in the banking industry. Asset quality is the key factor for a bank success and poor asset quality is the major cause of most bank failures. Loan portfolio is the most important asset category because the greatest risk facing the bank is the risk of loan losses derived from the delinquent loans. Financial analyst and credit analyst ought to focus on asset quality of loan portfolio by using trend analysis and peer composition. The measurement of asset quality is not easy because it is mostly derived from the analyst subjectivity (Grier, 2007).

Based on UFIRS, each of the components in the CAMEL rating system is scored from 1 to 5. In the context of asset quality, a rating of 1 indicates a strong asset quality and low portfolio risks and a rating of 5 reflects unfavorably and poor quality that presents bad condition for the institution.

Non-performing loans ratio is calculated by dividing non-performing loans to total loans. NPL represents the past due loan accounts whose interest or principle is unpaid for 30 days or more after the due date.

3.2.3 Management Quality

$$\text{Management Quality} = \frac{\text{Total loans}}{\text{Total deposits}}$$

Management quality is determining the future of the banks.. Management quality can be measured by emulating its operating efficiency which involves cost of management and productivity of employees. The management determines profitability objective and also determines the risk level undertaken by the bank.

Management quality reflects the capability of the management and board of directors to recognize, identify, measure and control the risks of an organization's activities and to guarantee the safe, sound, stable and efficient operation in compliance with appropriate laws and regulations as stated by Uniform Financial Institutions Rating System, 1997.

According to Grier (2007), management quality is considered to be the most single important element in the CAMEL rating system because it plays a significant role in the bank's success.

Commercial banks have to make 1 percent for pass loan/performing loan, 25 percent for substandard loan, 50 percent for doubtful loan and 100 percent for bad loan (NRB, 2005).

The rating of management quality as recorded by UFIRS (1997) is scored from 1 to 5. In the context of management quality, rating of 1 reflects a fully effective board of directors and management that indicates the highly management quality efficiency and

the initiation in the safe, stable, sound and good financial condition. On the other hand, the rating of 5 indicates critically poor and deficient bank management.

3.2.4 Earnings Ability

Return on Equity =	**Net Profit After Tax**	
	Equity Capital	
Return on Assets =	**Net Profit After Tax**	
	Total Assets	

Earnings ability uses a number of indicators to evaluate the bank performance but this study uses return on equity and return on assets to evaluate how earnings are related to the performance of the banking industry. The performance of banks in terms of its earnings and profitability indicates its ability to support current and future operations. This determines the capacity to absorb losses by building an adequate capital base, finance its expansion and pay adequate dividends to its shareholders.

The earning quality is very important criterion that examines the ability of a bank to earn consistently, going into the future. It determines the profitability of a bank and also it explains the sustainability and growth of the bank future earrings. This ratio gains importance in the light of the discussion that much of bank's income is earned by non-core activities like investment, operation treasury, and corporate advisory service.

As mentioned previously, this study uses two ratios to measure the earnings ability of banks as follows:

3.2.4.1 Return on Equity (ROE)

ROE is useful for comparing the bank's profitability and other financial institutions. The formula is net profit after tax divided by the equity capital. It measures the return rate on the ownership interest of the common stock owners, and measures banks efficiency for every unit of shareholders equity.

3.2.4.2 Return on Assets (ROA)

ROA is useful to indicate the profitability of the banks to total assets and it shows the efficient management that uses its assets to generate earnings. Higher ROA leads to higher profit and this ratio gains importance in the light of the discussion that much of a bank's income is earned by non-core activities like investment, operation treasury, and corporate advisory service.

3.2.5 Liquidity Risk

$$\text{Liquidity Risk} = \frac{\text{Cash \& Due From Banks + Treasury Securities}}{\text{Total Assets}}$$

Liquidity is important for any financial organization that deals with money. Bank liquidity is a significant aspect which represents its ability to meet its financial obligations. Banks should take care in hedging liquidity risk and ensure that a good

percentage of funds are invested in higher return generating investments. The bank can gain a profit while at the same time provides liquidity to the depositors. Most bank assets and cash investments are the most liquid. High liquidity shows that bank is more affluent. Liquidity for a bank is the ability to meet financial obligations due to illiquid assets and this ratio helps to evaluate whether the bank has enough amount of cash and short-term funds to withstand rising of NPA levels.

Cash and due from banks represent cash on hand while due from banks indicate receivables from, or short term loans to other banks and financial institutions which usually bear minor interest earnings.

Treasury securities can be divided into three instruments, namely government bond bills, T-bonds and T-notes.

CHAPTER FOUR

RESULTS AND DISCUSSION

4.0 Introduction

This chapter presents the empirical results based on the descriptive statistics and trend analysis of the 12 conventional banks of the GCC countries during the period of 2008 until 2012. Descriptive statistics and trend analysis had been applied in this study using SPSS Version 19 and Excel to indentify how the five components of CAMEL framework such as capital adequacy, asset quality, management quality, earning ability and liquidity risk affect the performance of banks in the GCC countries.

This chapter provides the answers to the study questions and objectives mentioned in chapter one. This chapter is divided into two sections. Section one describes the descriptive statistics and section two provides a discussion of the ratio analysis.

4.1 Descriptive Statistics

Table 4.1 provides the descriptive statistics of this study. The table includes the mean and standard deviation.

Table 4.1 Descriptive Analysis

Ratio/Year		2008	2009	2010	2011	2012
CAR	Mean	14.2039	17.0322	17.8123	17.8982	17.8263
	Std. deviation	4.9797	2.3605	3.0328	3.4521	4.2209
AQ	Mean	2.6225	5.1967	4.9842	6.0300	5.4400
	Std. deviation	2.7826	7.6246	4.5408	5.6235	4.1495
MQ	Mean	127.2758	121.4483	110.9892	111.4275	110.5467
	Std. deviation	21.1387	21.1995	19.9772	22.8630	20.2894
ROE	Mean	4.8408	12.9250	13.7675	13.7625	13.8842
	Std. deviation	44.5204	8.6305	3.9697	2.9974	2.8468
ROA	Mean	1.4538	1.7414	1.8877	1.8759	1.8782
	Std. deviation	2.6927	0.8495	0.6912	0.7035	0.6422
LR	Mean	8.7044	12.8587	14.5254	12.4387	12.6748
	Std. deviation	4.0130	7.6297	7.1517	6.2915	6.1936

Notes:
N= 12 banks
Figures are in percentages

Table 4.1 indicates that capital adequacy mean is 14.2039 in 2008 and increases in 2009 to 17.0322. Capital adequacy is slightly higher in 2010 and reaches 17.8123 and then remains constant until 2012. The table also shows that capital adequacy is able to meet the capital needs and implies that the banks do not need external funds.

As shown in Table 4.1, asset quality, which is measured by non-performing loans to total loans, has a mean of 2.6225 in 2008, which indicates that the asset quality of a bank is stable. The table also shows the mean in 2009 is 5.1967, which indicates that there is high non-performing loan in GCC countries during the period of study. In addition, the table shows that the mean is 5.1967 in 2009, which reveals that non-performing loan is

still high, while in 2010 the mean slightly decreases to 4.9842. In 2011, however, it increases to 6.0300 and drops slightly to 5.4400 in 2012. GCC conventional banks were facing losses as indicated by a high percentage of non-performing loans and the asset quality of the conventional banks were very poor.

According to Table 4.1, management quality which is measured as total loan divided by total deposits, has a mean of 127.2758 in 2008, which is according to CAMEL model indicates that the bank is in a stable situation because of the increasing in loans compared to deposits. In 2009, the mean for asset management slightly decreases to 121.4483 and in 2010 the mean is 110.9892. It continues to be constant for the next two years. Overall, it can be concluded that asset management in the GCC conventional banks is very high which reflects poor performance.

Table 4.1 shows ROE has a mean of 4.8408 in 2008 and it increases in 2009 to 12.9250. In 2010 it increases further to 13.7675 and remains constant until 2012. Overall, ROE for conventional banks in GCC seems to be stable and keep on improving.

Table 4.1 shows that mean for ROA is 1.4538 in 2008 and it increases to 1.7414 in 2009. ROA mean increases further in 2010 to 1.8877 and remains slightly constant until 2012. Overall, ROE for GCC banks seems to be stable and keep on improving.

Table 4.1 shows the mean for liquidity is 8.7044 in 2008 and it increases to 12.8587 in 2009. In 2010, it increases to 14.5254 to register the highest position during the period of study. The mean for liquidity is 12.4387 in 2011, while in 2012, it slightly increases to 12.6748.

4.2 Trend Analysis

In this section, the study describes the trend analysis for each of the country in the GCC. It depicts the graphical representation of each element of the CAMEL framework used in this analysis.

4.2.1 Trend Analysis in UAE Banks

4.2.1.1 Capital Adequacy

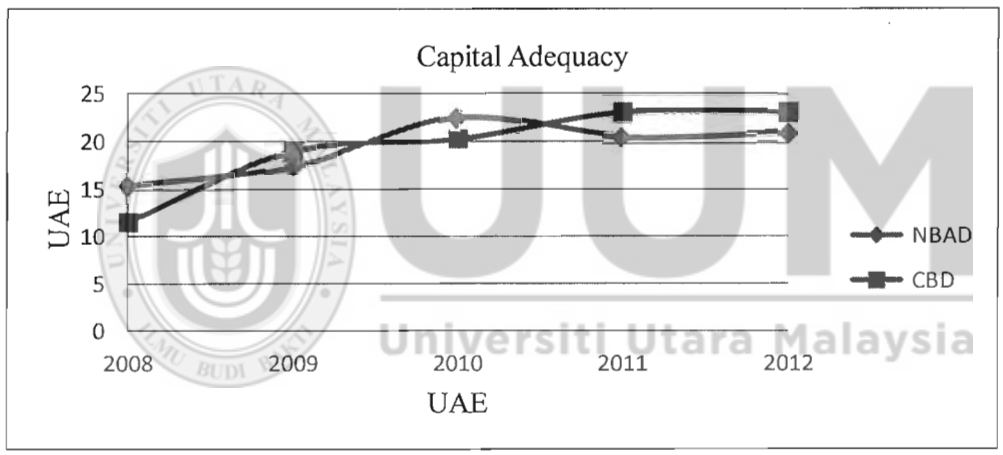

Figure 4.1 Capital Adequacy of Banks in UAE

Capital adequacy ratio (CAR) is a ratio of bank's capital to its risk. The CAR ensures that it can absorb a reasonable amount of losses complying with their legal capital requirements. Figure 4.1 shows that, the CAR for NBAD is about 15.39 in 2008 and it increases to 21.05 in 2012. The CAR for CBD is 11.49 in 2008 and rises steadily to 23.18 in 2012. The trend shows that the CAR is more than 8% and this means the banks are able to meet the liabilities and other risks. .

4.2.1.2 Asset Quality

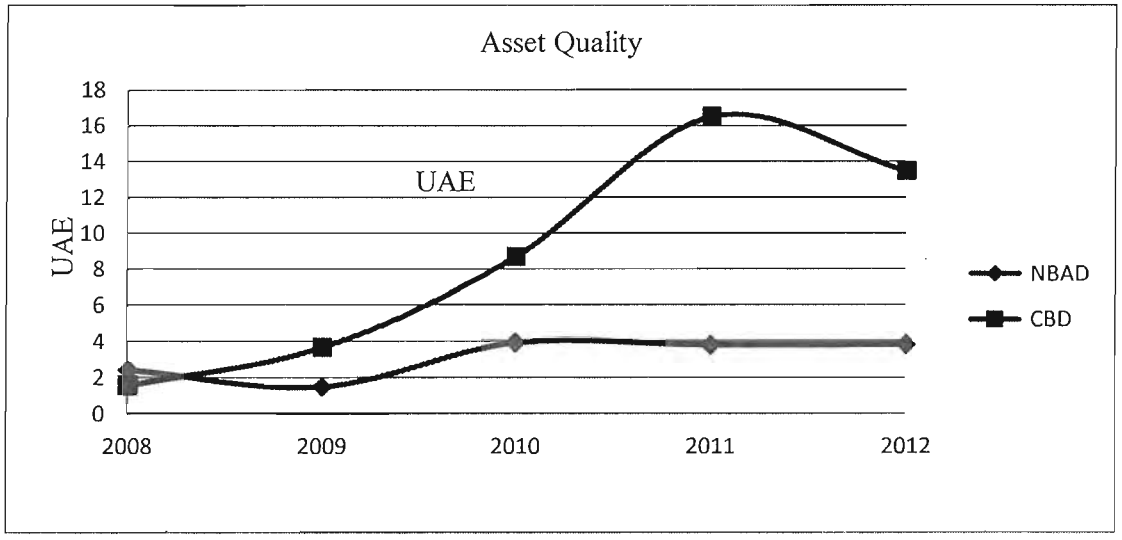

Figure 4.2 Asset Quality of Banks in UAE

Asset quality is the key factor of the bank success and a poor asset quality may cause bank failure. From the above chart, it indicates that the asset quality of NBAD is strong in the first two years and then it drops in 2010 to about 3.89, with some categories to be watched such as financial, operation or compliance weaknesses that would give reasons for supervisory concern. Then it declines slightly to 3.79 in the 2012. CBD asset quality is strong in 2008 amounting to 1.57 and it increases in 2010 to about 8.67. It continues to increase and it reflects the bank's serious financial weakness that may cause failure to be extremely high in the near future. The result indicates that the CBD has a critical issue in terms on non-performing loans and this may cause failure.

4.2.1.3 Management Quality

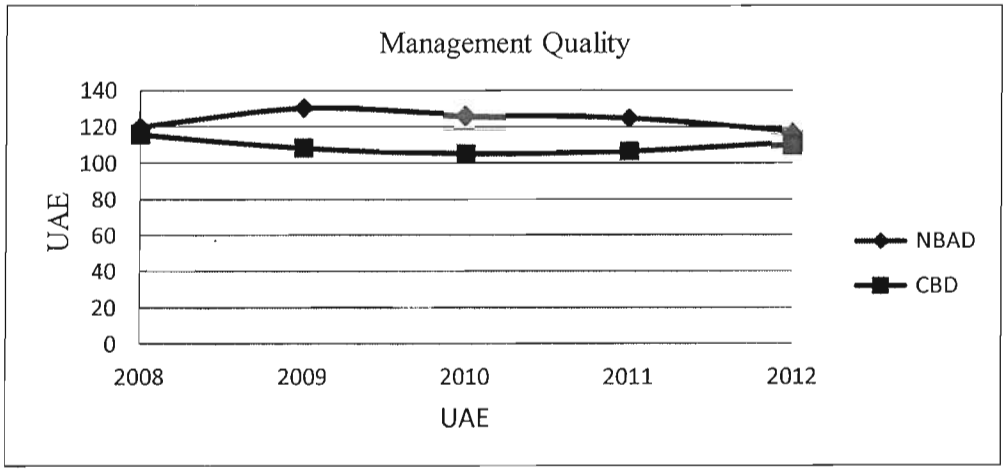

Figure 4.3 Management Quality of Banks in UAE

Management quality of the National Bank of Abu Dhabi and Commercial Bank of Dubai is not that efficient because the total loan to total deposits ratio is more than 120 and that infers a bad management. From the above figure, it shows that the management quality ratio is very high in 2008 and then it decreases steadily. The management is not able to control and manage the bank losses of the deficit amount that should be paid by depositors to the banks.

NRB (2005) supported that the rating of the asset quality by CAMEL rating system is 1 percent for pass loan/performing loan, 25 percent for substandard loan, 50 percent for doubtful loan and 100 percent for bad loan.

4.2.1.4 Earning Ability

i) Return on Equity

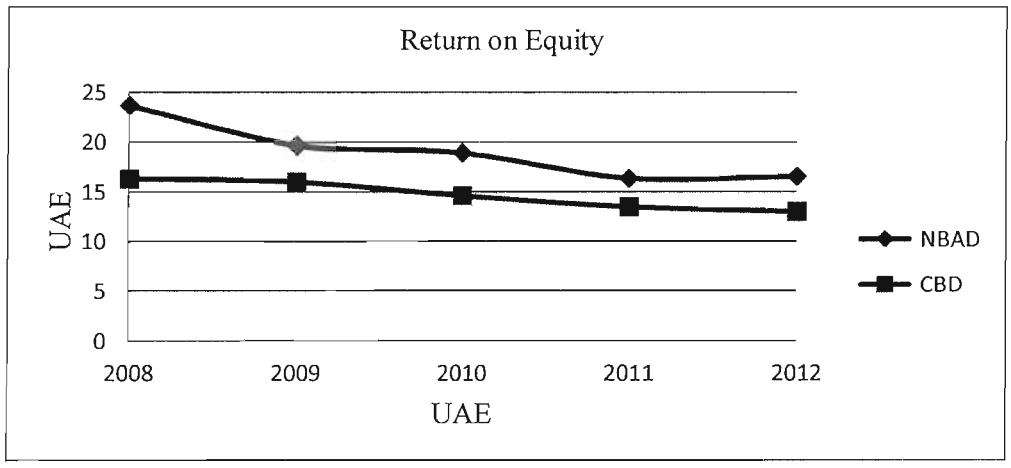

Figure 4.4 ROE of Banks in UAE

Figure 4.4, shows the movement of ROE level in the two conventional banks of UAE across five years period beginning from 2008 to 2012. The ROE has been fluctuated during the period and the highest ROE of NBAD in 2008 about 23.69 and it decreased constantly in the 4 years while the CBD have the same criteria and it recorded the highest and best ROE in 2008 and then it decreased down. The lowest ROE was in 2012 in the CBD. ROE shows that the two banks are profitable banks and the current situation is good also it observed the high efficient for every unit of shareholder equity.

ii) Return on Assets

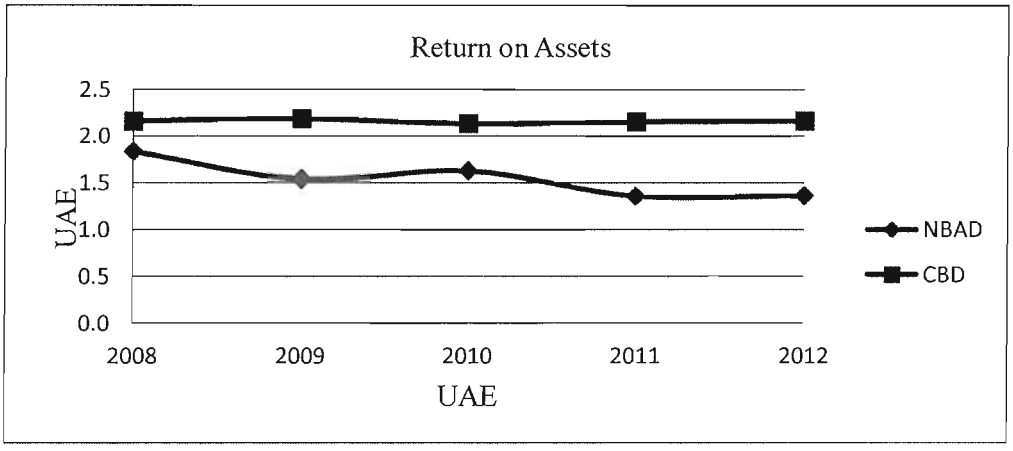

Figure 4.5 ROA of Banks in UAE

Figure 4.5 provides the movement of the ROA ratio of the two banks, for the ROE of NBAD, fluctuated along in the five years and the best ROE was in 2008 about 1.83 and that infer this bank is a profitable bank. In addition the CBD was better than the NBAD and it gain a profit during the five years. ROE was constant during the five years in CBD bank. CAMEL framework is a good model to indicate the effect of the financial ratios to bank's performance.

4.2.1.5 Liquidity Risk

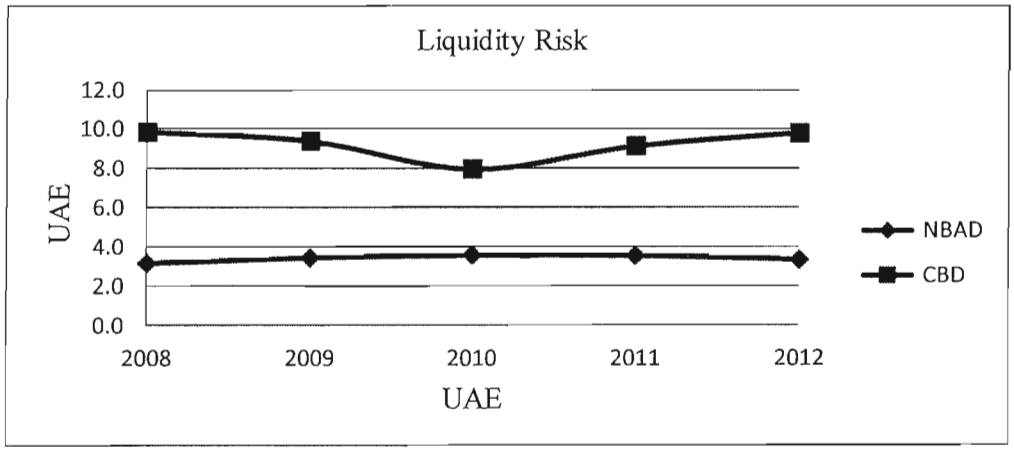

Figure 4.6 Liquidity Risk of Banks in UAE

For the financial organization, liquidity is very important because it deal with the money. Bank liquidity is a significant aspect which represents its ability to meet its financial obligations. From figure 4.6 it infers that the bank of NBAD was not that qualified to meet the financial obligation while the CBD was very good in term of liquidity. These two banks not in a critical position but it seem from the chart there is a chance for not getting losses. Banks should take care of the liquidity risk because it will affect the entire cycle of the bank's operations if it become not efficient and the bank will suffer in term of the financial flow.

4.2.2 Trend Analysis in KSA Banks

4.2.2.1 Capital Adequacy

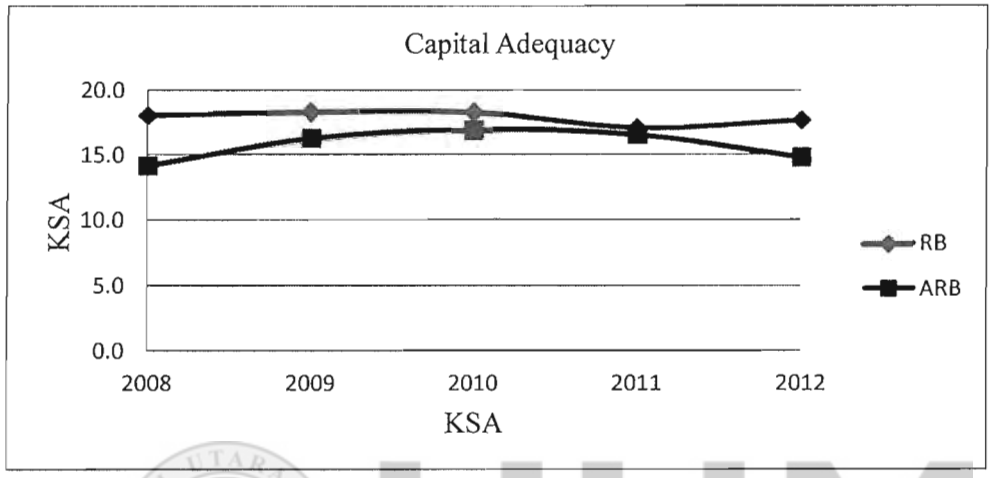

Figure 4.7 Capital Adequacy of Banks in KSA

According to figure 4.7, the capital adequacy in Riyadh Bank and Arab National Bank were fluctuated during the five years. It indicated that the capital adequacy of RB was 18.3 and it's the highest rate while CAR was 14.1 in ANB and that recorded the lowest rate. Generally the CAR in these two banks was very good.

4.2.2.2 Asset Quality

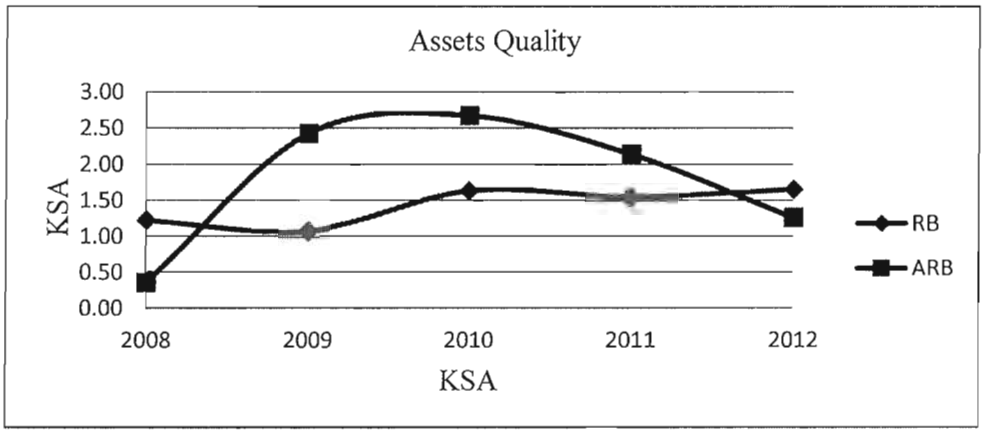

Figure 4.8 Asset Quality of Banks in KSA

From the trend analysis figure, the asset quality of Riyadh bank was a strong in the year of 2009 and then it fluctuated during the five year. Asset quality of RB was in control over the five years period. On the other hand, Arab National Bank started with a strong rate of 0.35 in the year of 2008, suddenly increased to 2.67 in the year of 2010. There is weakness in the bank assets quality.

4.2.2.3 Management Quality

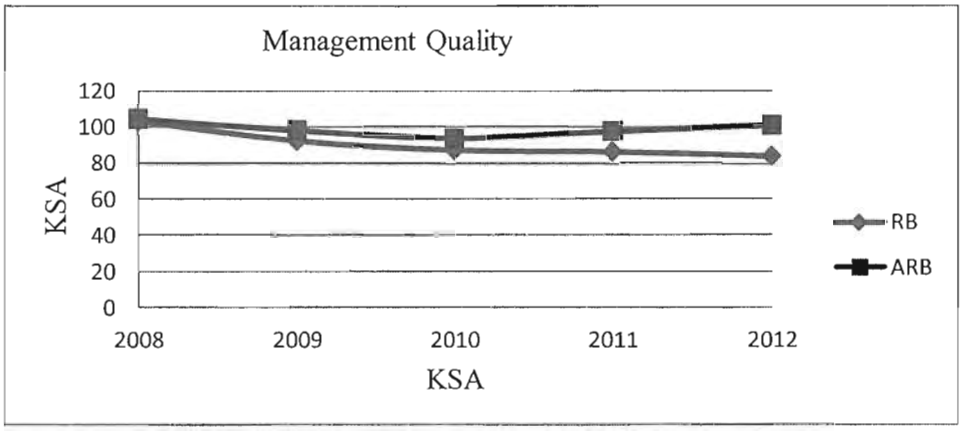

Figure 4.9 Management Quality of Banks in KSA

Management quality of the RB and ARB was in a critical situation at the year of 2008, lucky it decreased as steady decline in the rest of for years. Total loans to total deposits were in the rate of 84% to 98% and it infers the total loans are more than the total deposits in these two banks. Ravichandran and Sharma (2009) found that the commercial banks were performed better in all the CAMEL framework components except in Asset quality it was not caring about the public deposits and it became low compare to the total loans.

4.2.2.4 Earning Ability

i) Return on Equity

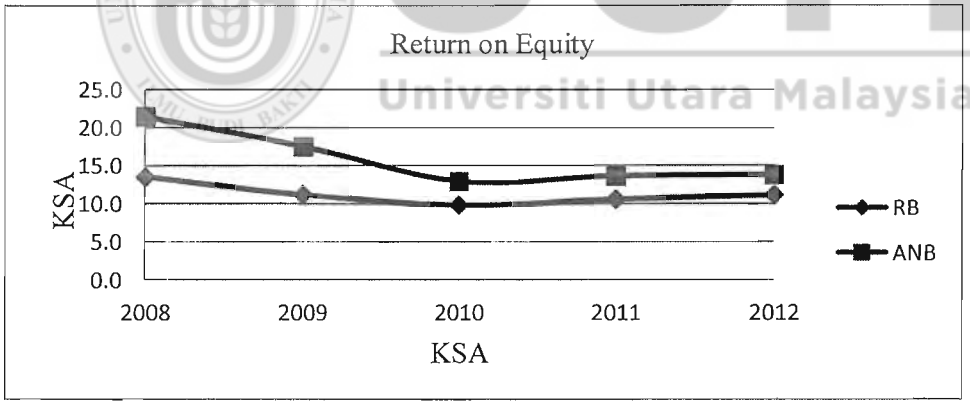

Figure 4.10 Return on Equity of Banks in KSA

Figure 4.10 infers the result of the return to equity for the RB and ANB banks for the period of five years, the return to shareholder was good enough to the investors and

shareholders. It shows the highest rate was in 2008 for both banks and then it decreased constantly at 2009 until 2012.

ii) Return on Assets

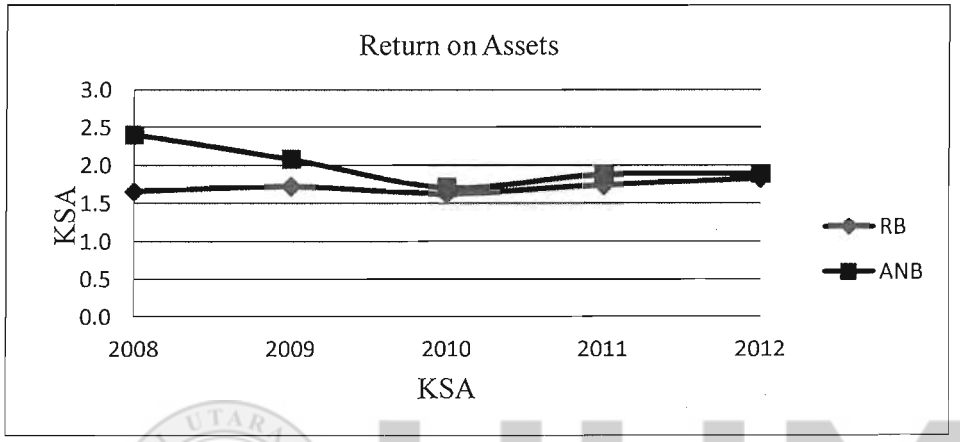

Figure 4.11 Return on Assets of Banks in KSA

Return on Assets ratio measure by dividing the net income to total assets, Riyadh Bank and Arab National Bank was in the highest growth at year 2008 also it indicated that the bank is profitable, in the next four years ROA was volatile and it increased up again in the year of 2009 for both banks.

4.2.2.5 Liquidity Risk

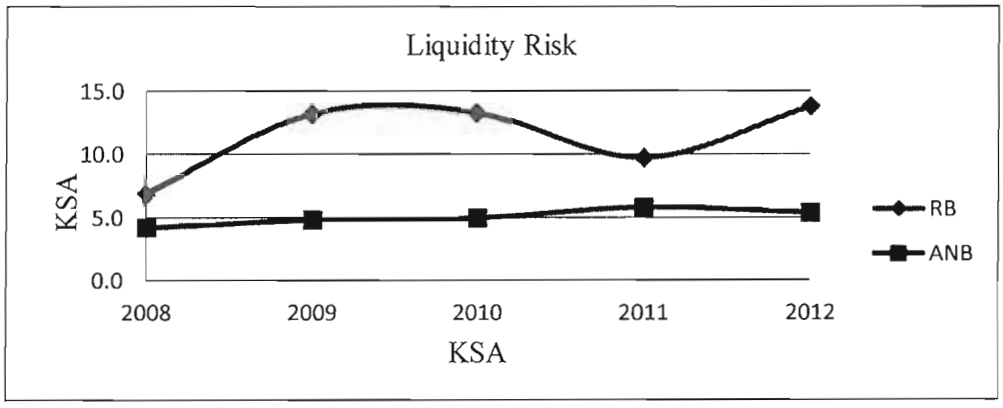

Figure 4.12 liquidity Risk of Banks in KSA

Figure 4.12, provide the results of RB and ANB were not in a crucial position but these banks should increase their liquidity because liquidity is the main hub of the financial institutions. RB seems better than the ANB in term of liquidity. The liquidity was increasing up during the five years and that reflect a good observation of the banks cash management.

4.2.3 Trend Analysis in Kuwait Banks

4.2.3.1 Capital Adequacy

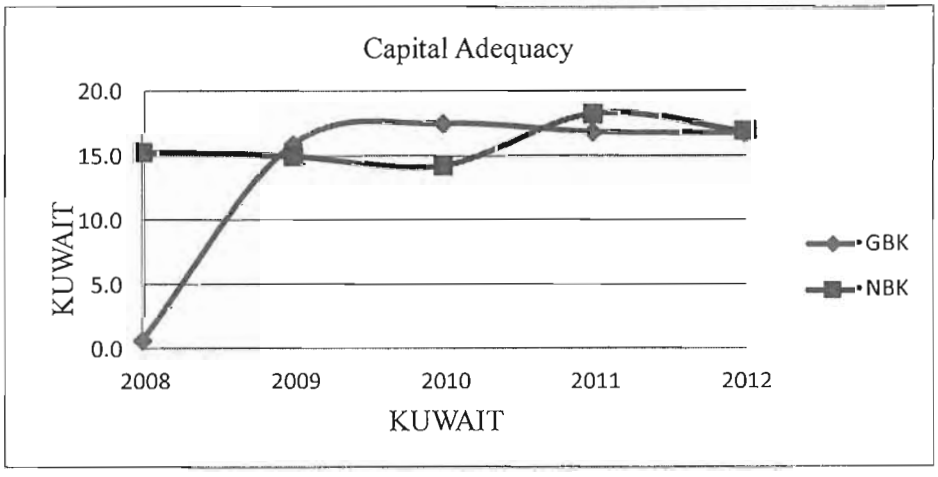

Figure 4.13 Capital Adequacy of Banks in Kuwait

Capital adequacy in the Gulf bank of Kuwait was very low in the year of 2008 and suddenly it increased in the next two years, while the heights rat of CAR was 17.5 in 2010 and then it decreased a bit in the 2011 and 2012.Capital adequacy of National Bank of Kuwait was very good and its more than 8% and there is no critical issues will meet the bank while the capital is more than 8%, its able to meet the extra capital required from the bank.

4.2.3.2 Asset Quality

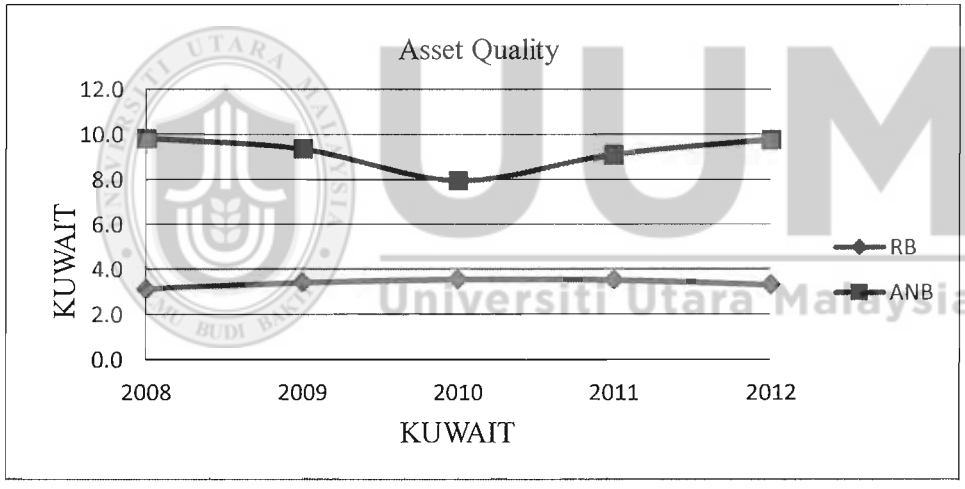

Figure 4.14 Asset Quality of Banks in Kuwait

According to Figure 4.14, asset quality of GBK was very high and this reflects weak management and there is a reasonable condition that affects the management quality of NBK. AQ show very poor and weak management, the nonperforming loan in this bank is more than the total loan and it affected the operations of the banks. For the National Bank of Kuwait the rate of Asset quality was a strong and the non-performing loan is

low compared to the total loan. The AQ was very strong and in the year of 2012 it increased to 2.4 but still under control.

4.2.3.3 Management Quality

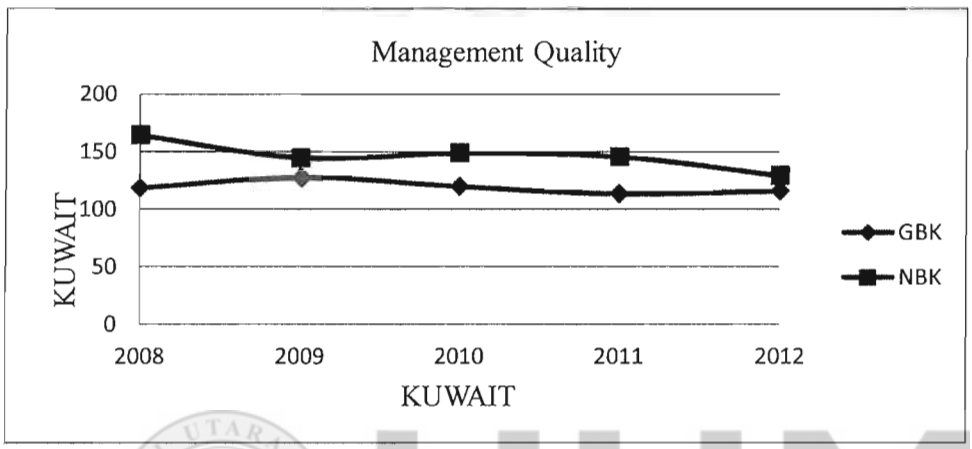

Figure 4.15 Management Quality of Banks in Kuwait

Management quality in the Gulf Bank of Kuwait and National Bank of Kuwait was very high in 2008 by 118.2 and 164.2 also it increased up in the next four years and that represent that the total loans is more that the total deposits. From this result it infers there is a bad loan and a weak management in the banks system. It observed that there is a need to measure the banks in all GCC countries and especially in Kuwait. International monetary fund found that the GCC countries have high rate of non-performing loans. It must be consider as critical issue (Espinoza and Prasad, 2010).

4.2.3.4 Earnings ability

i) Return on Equity

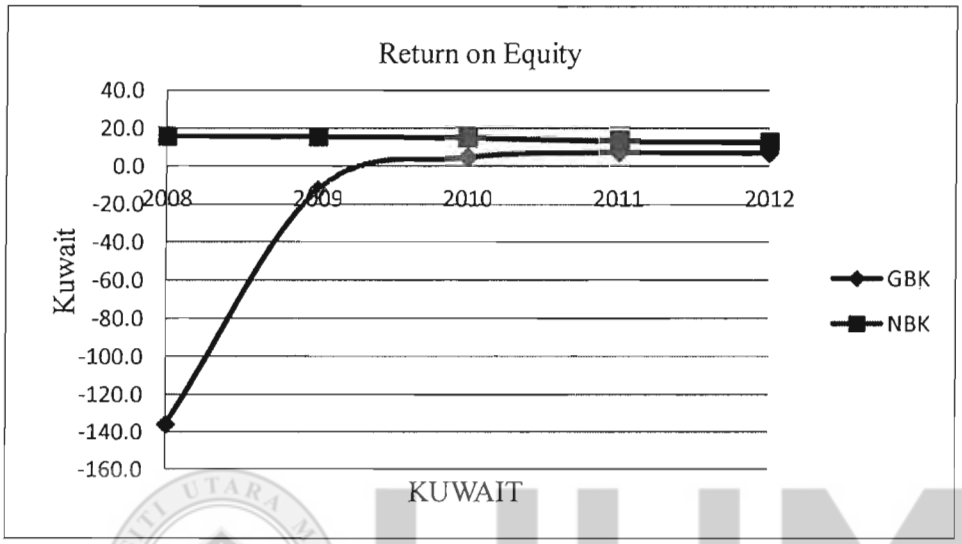

Figure 4.16 Return on Equity of Banks in Kuwait

According to the trend above the ROE of the GBK was a negative by -136 at year of 2008 and this indicated that the bank affect by the global financial Crises in 2008 and 2009 because it has many subsidiary branches in different countries around the world. ROE after the financial crises started to increase steady in the next three years. For the NBK, ROE was in a good manner and it was profitable to the shareholders, the ROE was fluctuated during the five years. The CAMEL framework is a useful model to evaluate the banks performance.

ii) Return on Assets

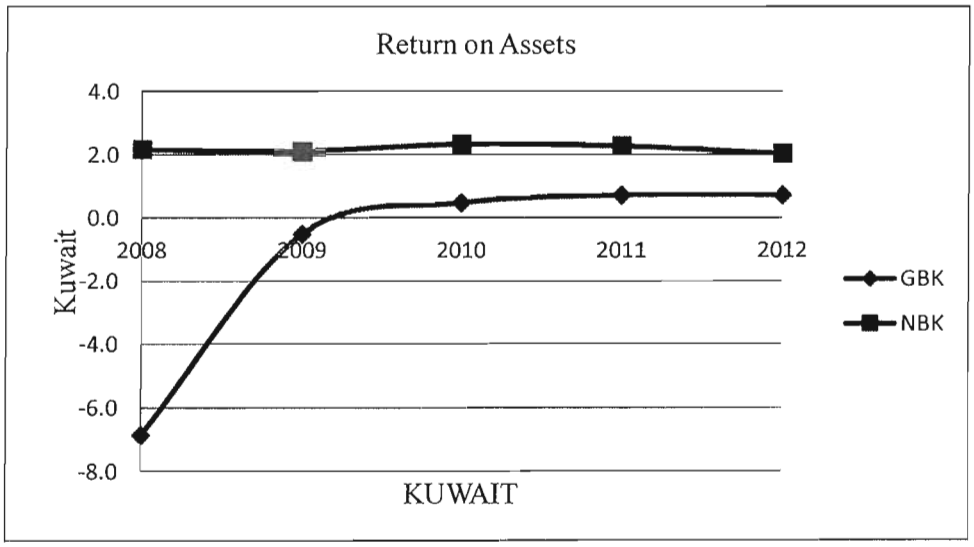

Figure 4.17 Return on Assets of Banks in Kuwait

ROA in the GBK was a negative in 2008 by -6.9 and in 2009 -0.5 and this is the worst rates in the bank during the five years. GBK was in critical position and it facing losses. It continue to increase in the next 3 years and in 2012 it was better than 2008 by 0.7. For the NBK was in control and its ROA is stable and there is a profit in this bank. It increased during the four years until 2011 and then it decreased slightly in 2012.

4.2.3.5 Liquidity Risk

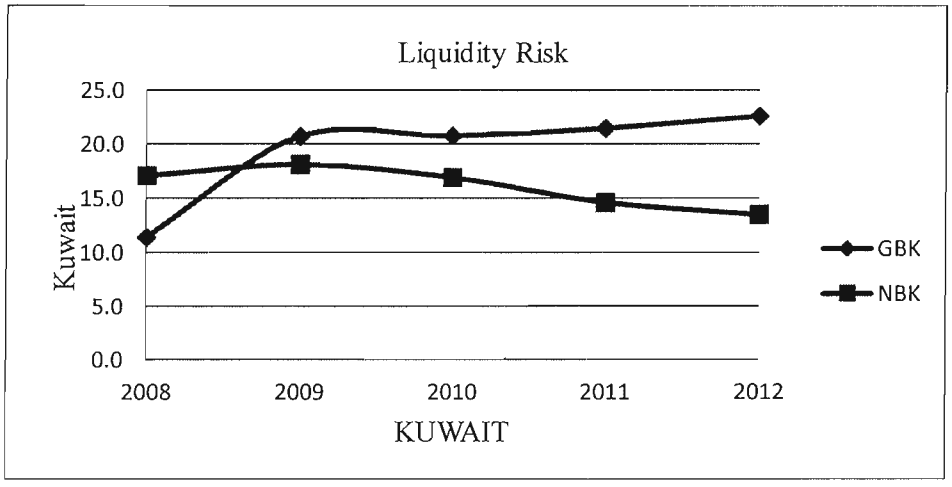

Figure 4.18 liquidity Risk of Banks in Kuwait

Figure 4.18 shows that the Gulf Bank of Kuwait is liquid and there is no any worry about the cash liquidity from the bank. The liquidity risk measures by Cash due from bank + treasury securities to total assets. This ratio indicates the liquidity of the cash in the bank. From the trend above it shows that the GBK liquidity ratio was increasing every year in a good manner until 2012. For NBK the liquidity ratio was volatile during the five years. For all these two banks, they have a liquid cash flow.

4.2.4 Trend Analysis of Oman Banks

4.2.4.1 Capital Adequacy

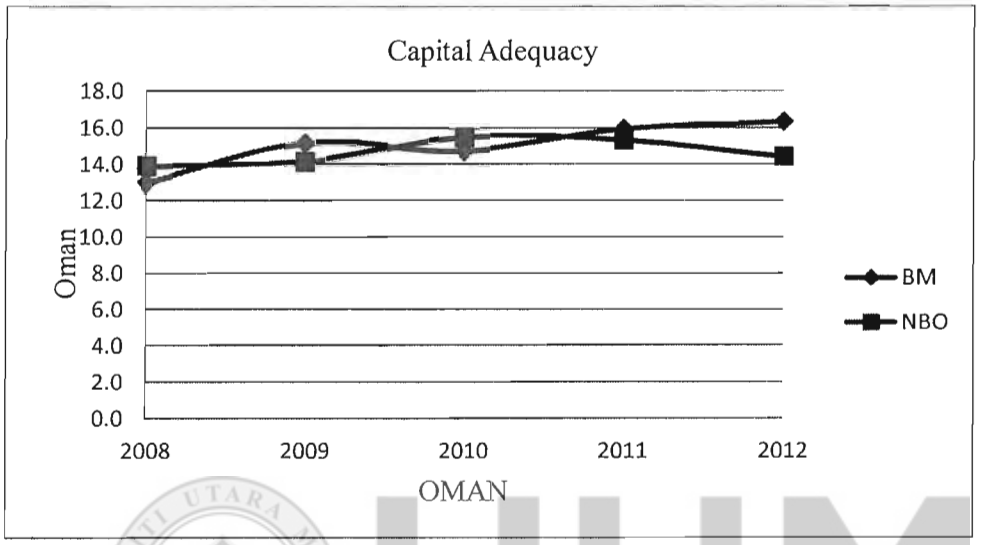

Figure 4.19 Capital Adequacy of Banks in Oman

Referring to figure 4.19 capital adequacy indicated that bank Muscat showed a percentage of 13 % in 2008 and that revealed the capital of a bank is stable and the bank no need to such an external funds. Furthermore, it increased in 2009 to obtain 15.2 % percentage and in 2010 it slightly decreased to 14.8% but in 2011 increased to 15.9 and it keeps increasing until 2012 by obtaining 16.3% which is the highest percentage during the study. Finally, we can concluded that bank Muscat was performs well according to capital adequacy which a good techniques to evaluate bank performance. According to the above figure it can be seen that national bank of Oman has adequacy ratios which is fluctuated from year to year for example, in year 2008 it was 13.9% and it increased to 14.2% and in 2010 increased to 15.5% and keep constant until 2012 which is slightly

deceased to 14.4. In short, capital adequacy of national bank of Oman indicated than the bank in good condition and has enough capital and there is need for extra funds.

4.2.4.2 Asset Quality

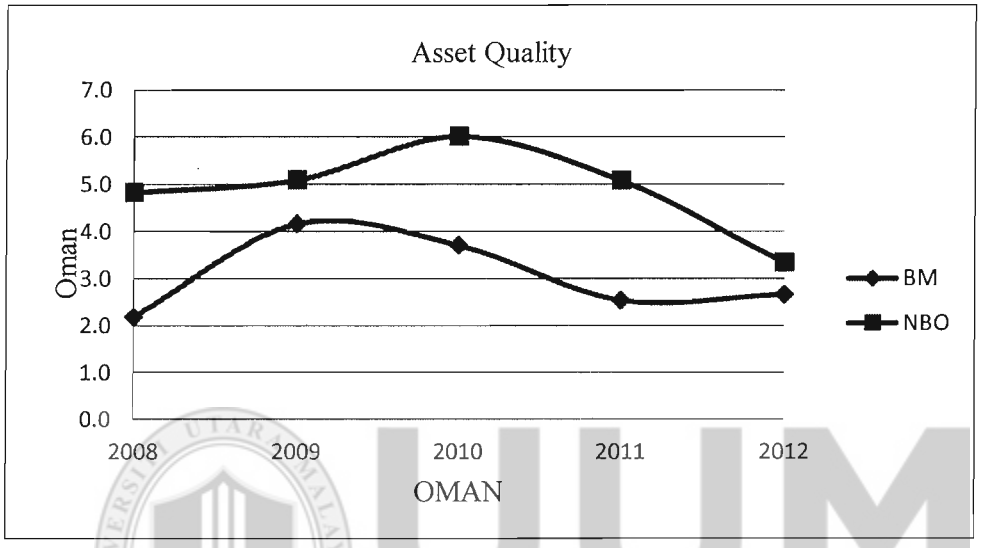

Figure 4.20 Asset Quality of Banks in Oman

Figure 4.20,shows that asset quality ratio of bank Muscat demonstrates a lower percentage in 2008 about 2.2 % and that reflect a little weaknesses in the asset quality and meaning that non-performing loan is very high compare to total loan. Asset quality was fluctuating up and down in 2009 to 2012 and it indicated a low percentage about 2.5 and 2.7 in 2011 and 2012 perceptively. In addition, national bank of Oman shows than the asset quality ratio was very high during all the period and that reflected high amount of non-performing loan in this bank.

4.2.4.3 Management Quality

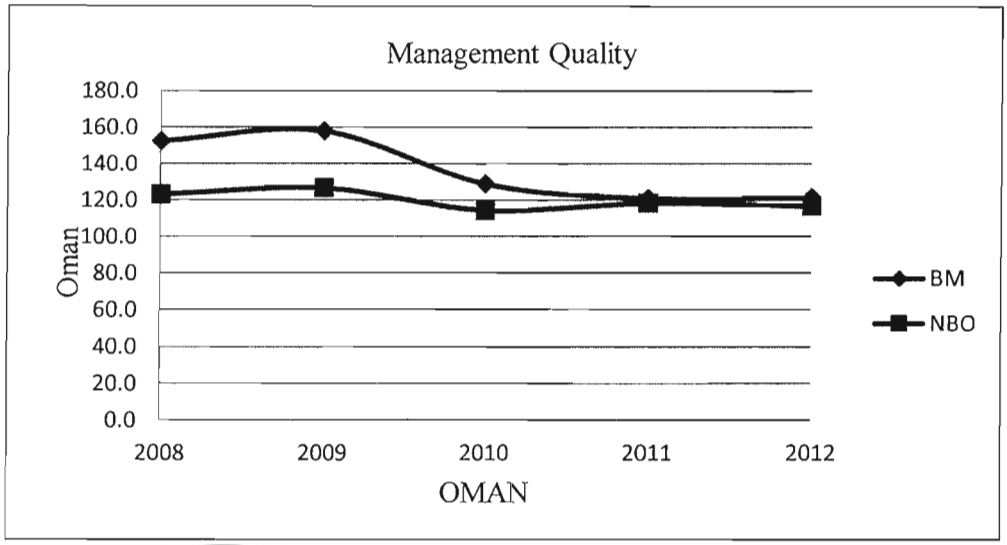

Figure 4.21 Management Quality of Banks in Oman

Figure 4.21 identified that management quality in bank Muscat and national bank of Oman in Oman are quite high and that indicated the management quality is not efficient because all ratios were more the 110 % and that revealed the total loan was high compare to total deposit. These banks are facing bad loan and the banks should reduce the loan and increase the deposits. It could be seen that most of conventional banks in GCC are facing this problem.

4.2.3.6 Earning Ability

i) Return on Equity

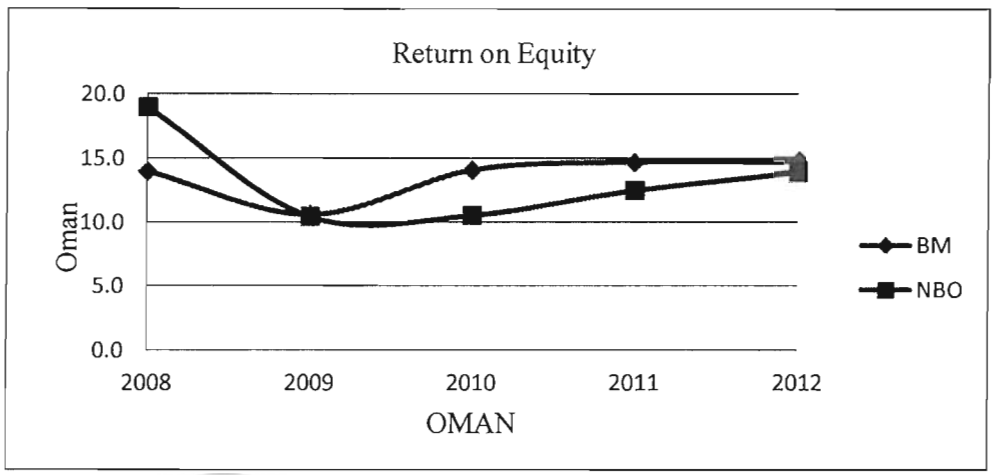

Figure 4.22 Return on Equity of Banks in Oman

As per Figure 4.22 ROE of bank Muscat was 14 % in 2008 and it decreased in 2009 to 10.6% but in 2010 increased to 14.1% and keep constant with slightly increase until 2012. On the other hand, national bank of Oman ROE shows high percentage in 2008 by achieving 19% which is the highest ratio during the period of study. ROE in 2009 and 2010 was dropped down to 10.4% and 10.5% respectively. In 2011 and 2012 it increased to achieve 12.5 and 123.9 % respectively. The ROE average was good for both banks and reflects the ability of bank's management to create income from total equity.

ii) Return on Assets

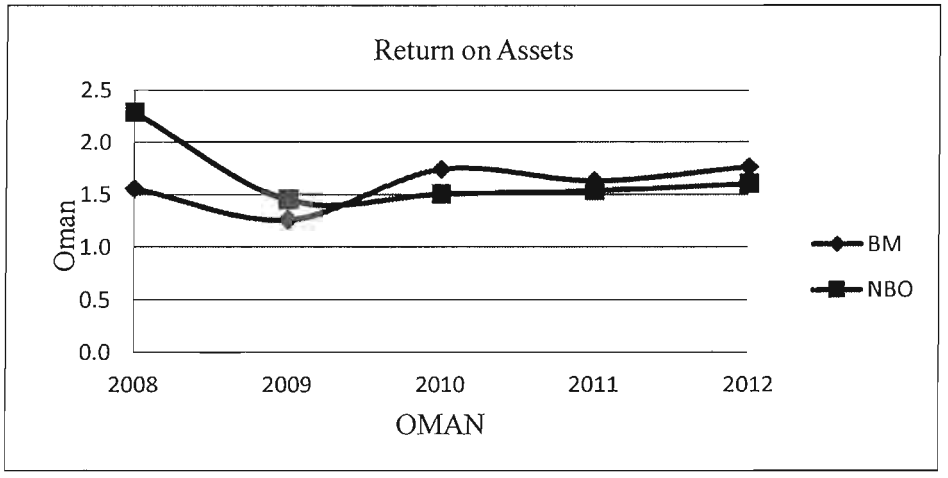

Figure 4.23 Return on Assets of Banks in Oman

Figure 4.23 which provide the movement of the ROA ratio of the two banksin Oman namely bank Muscat and National Bank of Oman. ROA for both banks was fluctuated along in the five years between 1.3% and 2.3% and it can be seen that the output of ROA was slightly low compare to the huge asset of these banks. CAMEL framework is a good model to indicate the effect of the financial ratios to bank's performance.

4.2.4.5 Liquidity Risk

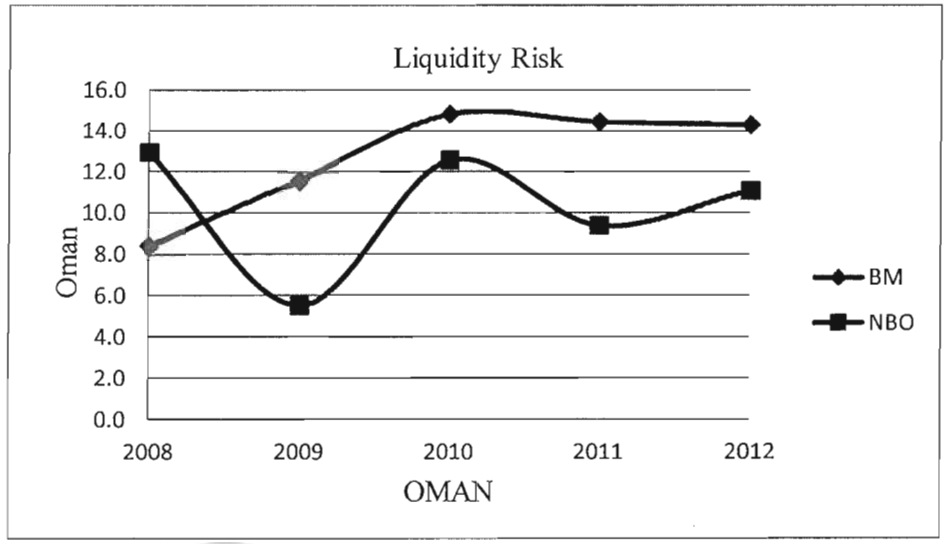

Figure 4.24 liquidity Risk of Banks in Oman

For the financial organization, liquidity is very important because the more liquid asset is the more profitable. According to figure 4.24 bank Muscat liquidity was 8.4% in 2008 and increased in 2009 to abstain 11.6 % and it increased again in 2011 to 14.8 and keep constant to 2012. Overall, bank Muscat liquidity reflects that the bank has the ability to meet its obligations. In addition, national bank of Oman liquidity ratios was fluctuated in all the five years with stating of 12.9% in 2009 and it decreased in 2009 to 5.5 % which is consider slightly low but it increased in 2011 to obtain 12.6 and decreased again to 9.4 % in 2011 and in 2012 it increased to 11.1% and one can say that national bank of Oman has a good level of liquidity and has the ability to meet its financial obligations.

4.2.5 Trend Analysis in Qatar Banks

4.2.5.1 Capital Adequacy

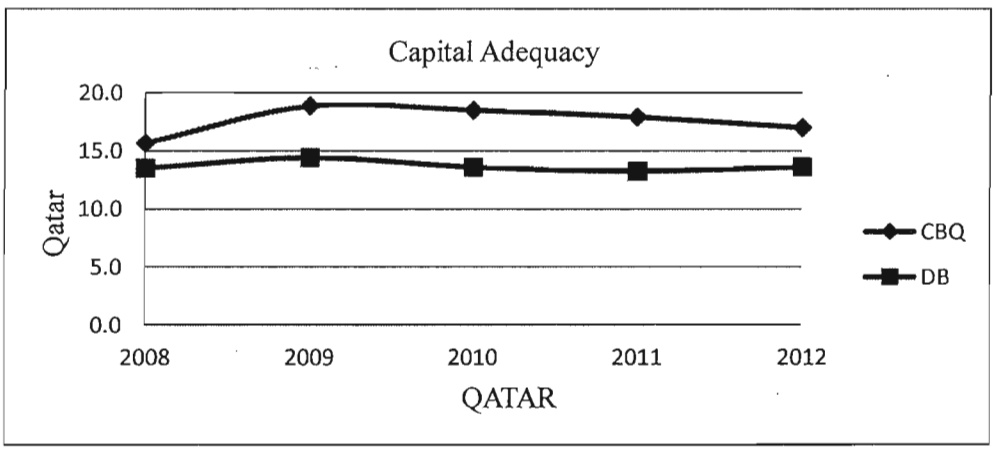

Figure 4.25 Capital Adequacy of Banks in Qatar

For the Qatar banks analysis, it begins with the capital adequacy analysis in Commercial Bank of Qatar and Doha Bank. From the above figure 4.25, it shows that the capital adequacy was more than 13 % in the year of 2008 for DB and then it continue increasing in 2009, after that it keeps steady movement in the rest 4 years. CBQ was better than DB in term of improvements during the five years. From the above trend it shows that the two banks are able to meet any capital requirements.

4.2.5.2 Assets Quality

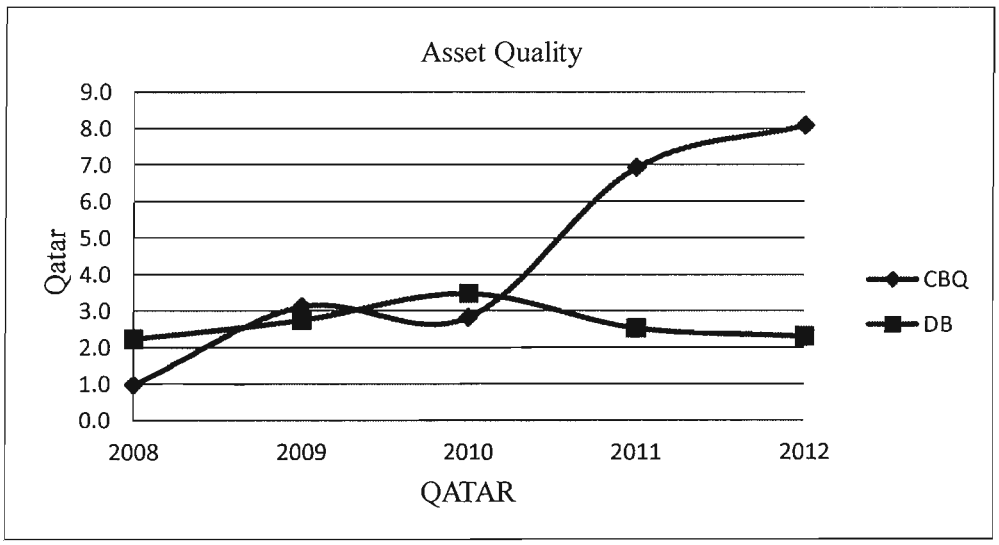

Figure 4.26 Asset Quality of Banks in Qatar

Figure 4.26 showed that asset quality in CBQ was in the best rate at year of 2008 about 1.0 % it means that the bank non-performing loans are less that the total loan in that year, unexpectedly AQ jumps to 3.1 % in the year 2009, in this case the bank should look for the reasons of what is happening in the Asset quality and infers the problem to be solved. Again in 2010 it decreased until 2.8 5 and then it increased up to 6.9 in 2011 and 8.1 in 2012 and it recorded the worst rate during the five years. Bank of Doha AQ ratio was volatile during the five years and the rates could be under bank control, all the years rates was normal except in 2010 it was 3.5 %.

4.2.5.3 Management Quality

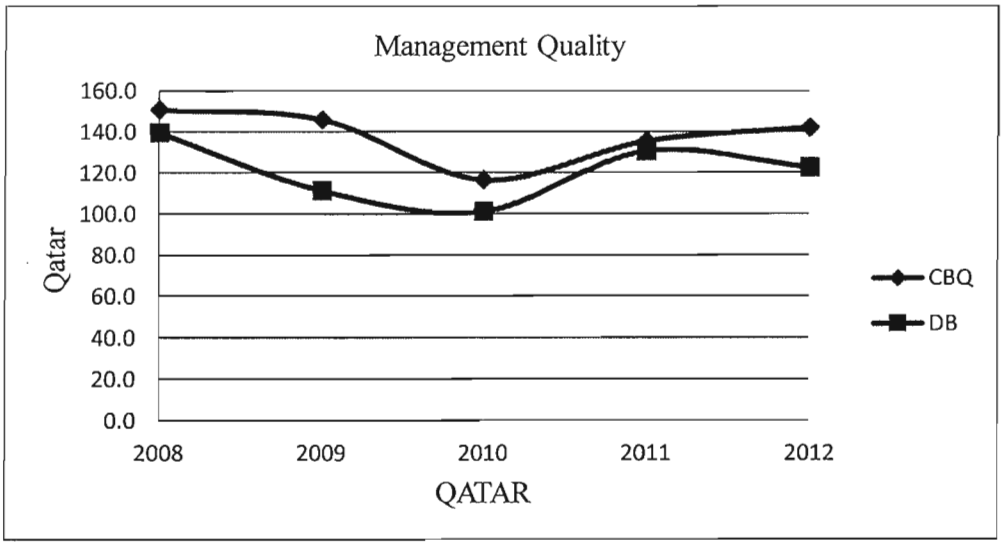

Figure 4.27 Management Quality of Banks in Qatar

Management quality in Qatar was not that efficient because the above figure 4.27 shows that the management quality not performing well in term of management for the total loans to total deposits.CBQ exceed 100% in 2008 and it reached 150% in 2008 and then it declined in2009 to 145.8 also it continues to decrease until 142% in 2012. However the MQ decline but it still more that 100 % and this is will affect the bank performance in Qatar. For DB, the MQ was very high in 2008 about 140% and then it fluctuated during the next four years. Overall the Total loan in Qatar banks was high compare to total deposits and this result infer there is a bad management quality in these two banks.

4.2.5.4 Earning Ability

i) Return on Equity

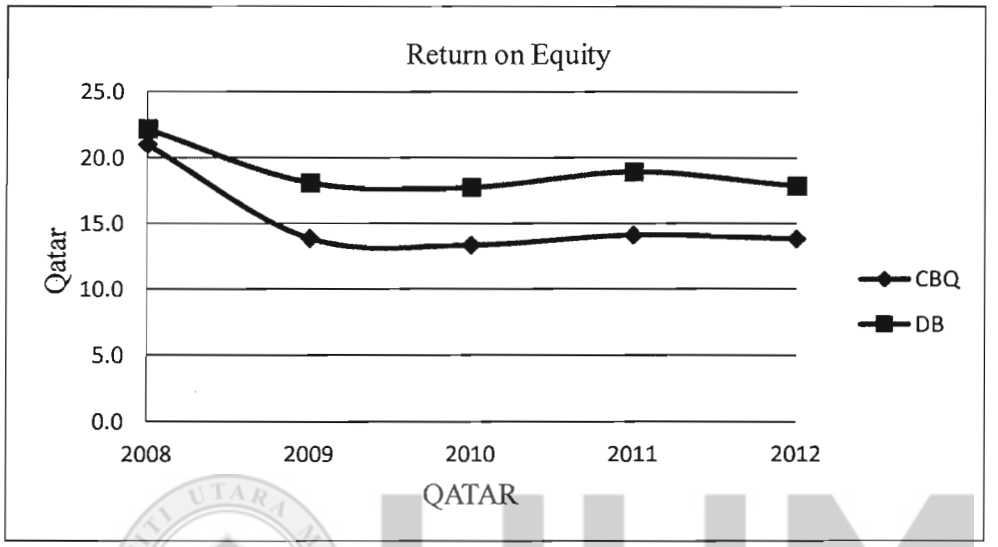

Figure 4.28 Return on Equity of Banks in Qatar

Overall the ROE in the CBQ and DB banks was very profitable to the shareholders and investors and it show that the high performance of these two banks during the five years period. The ROE was high in the 2008 for both banks and then it started to volatile during the four years. It means that the banks were in a good condition and there is a chance to increase the performance of the banks. CAMEL rating system is the best useful model to examine the real performance of banks. The ROE is able to assess the bank performance and evaluation.

ii) Return on Assets

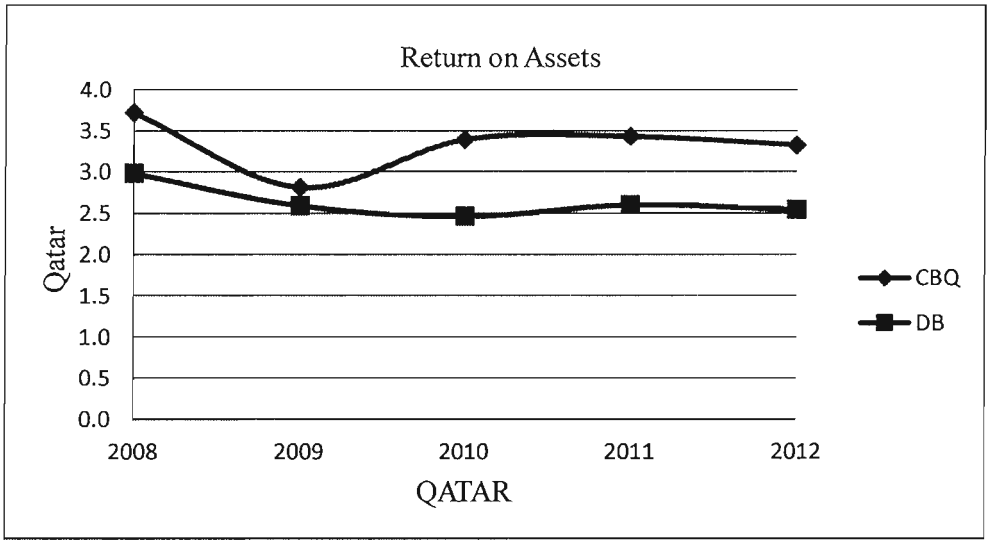

Figure 4.29 Return on Assets of Banks in Qatar

According to the above Figure 4.29, ROA for CBQ was 3.7 % in 2008 and then it decreased in 2009 to 2.8 %, suddenly it increased to 3.4 and it continues fluctuating in the three years. DB ROA was in the same level as CBQ 2008 about 3 % and then it continue steady until the end of year 2012. From this result it infers that the ROA was performing well in the five years and the performance of bank in very good.

4.2.5.6 Liquidity Risk

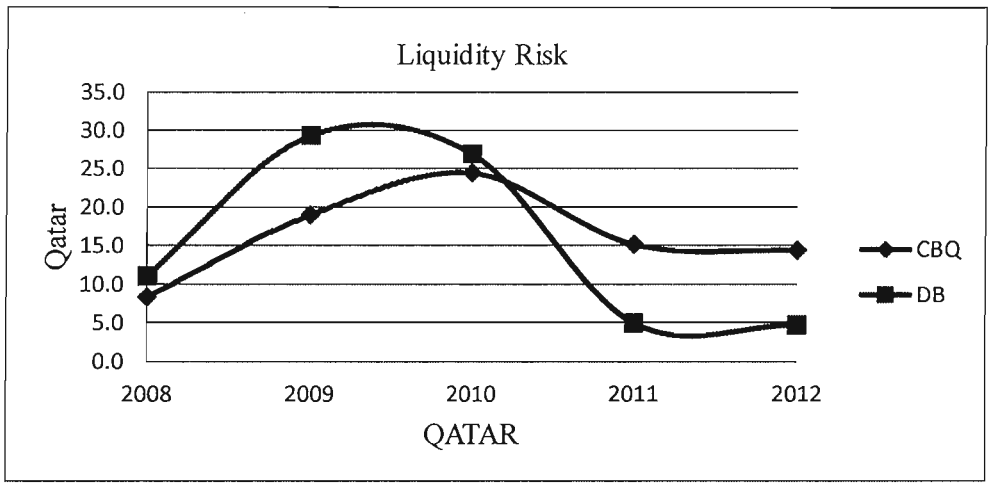

Figure 4.30 Liquidity Risk of Banks in Qatar

Figure 4.30 shows the result of Liquidity risk in the two banks of Qatar. In CBQ the liquidity ratio was 8.3 % in 2008 and it jump up in 2009 and 2010 to 24.4% and then it decreased slowly in the next 2 years. However, DB was 11% in 2008 and it increased in the 2009 and 2010 and it decline again in 2011, 5.0% and in 2010 4.7. Overall, from the result above it show that the CBQ and DB were in unstable situations and they faced lack in the cash inflow in some years and the opposite happened too.

4.2.6 Trend Analysis in Bahrain Banks

4.2.6.1 Capital adequacy

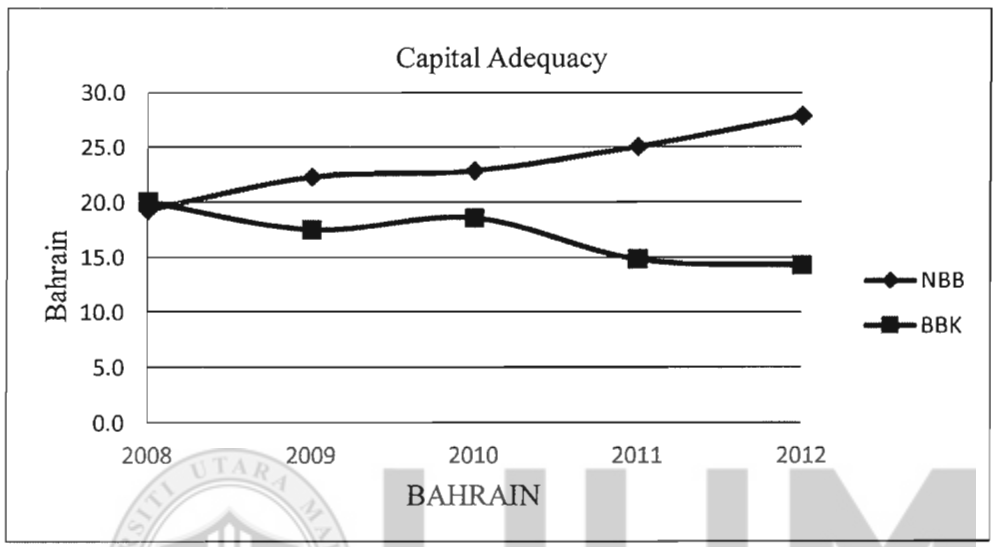

Figure 4.31 Capital Adequacy of Banks in Bahrain

Capital adequacy ratio (CAR) is a ratio of bank's capital to its risk. As per figure 4.31, National bank of Bahrain and Bank Bahrain and Kuwait CAR was fluctuated between 14.3% and 27. % and that indicated the banks ensure that they have the ability to meet their liabilities obligations since their capital adequacy more than 8%. Thus, both banks have the ability to avoid the risk and also the depositors and lenders would be protected from getting losses.

4.2.6.2 Asset Quality

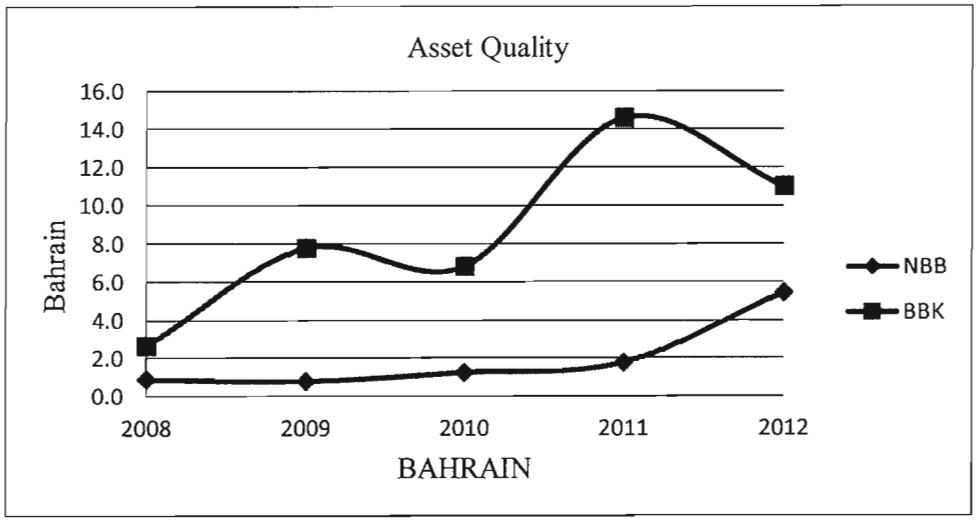

Figure 4.32 Asset Quality of Banks in Bahrain

As per figure 4.32 asset quality ratio of National Bank of Bahrain was stable and achieving the good standard for asset quality which fluctuated between 0.8 to 1.8 in the first four years and that reflected the normal ratio. In 2012 the asset quality ratio was 5.4% which consider very high and meaning that the non-performing loan was very high in 2012 compared to total loan. Bank Bahrain and Kuwait asset quality ratio was quite high in 2008 but it increased in 2010 to obtain 7.8% and it decreased in 2010 to 6.8%. The highest asset quality was in 2011 which achieved 14.6 and that mean the bank in a risk because non-performing loan is very high and that lead to more losses. Finally, in 2012 asset quality ratio decreased to 11% but it is still high compared to total loan.

4.2.6.3 Management Quality

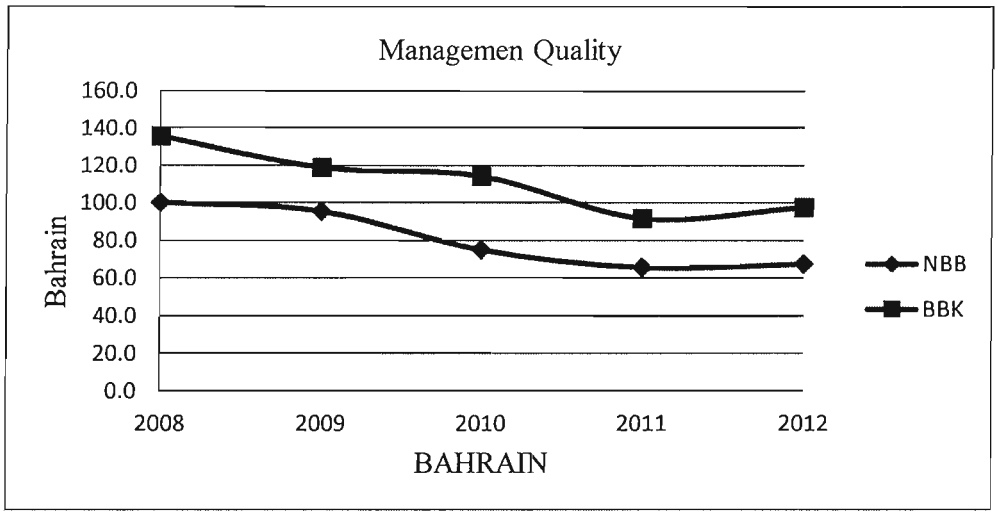

Figure 4.33 Management Quality of Banks in Bahrain

Figure 4.33 identified that management quality ratio in National Bank of Bahrain was 100 which in indicated that total loan was high compared to total deposit and it decreased in 2009 to 95.4% and it continue decreasing for the rest period of study and it revealed that asset quality getting much better than the previous years. On the other hand, Bank Bahrain and Kuwait management ratio was very high which is over 100 in the beginning three years and that showed Bahrain and Kuwait bank was having more loan to deposit. Finally, in 2011 asset management ratios was slightly decreased to 91.6% and it increased in 2012 to obtain 97.3. These banks are facing bad loan and the banks should reduce the loan and increase the deposits. It could be seen that most of conventional banks in GCC are facing this problem.

4.2.6.3 Earning Ability

i) Return on Equity

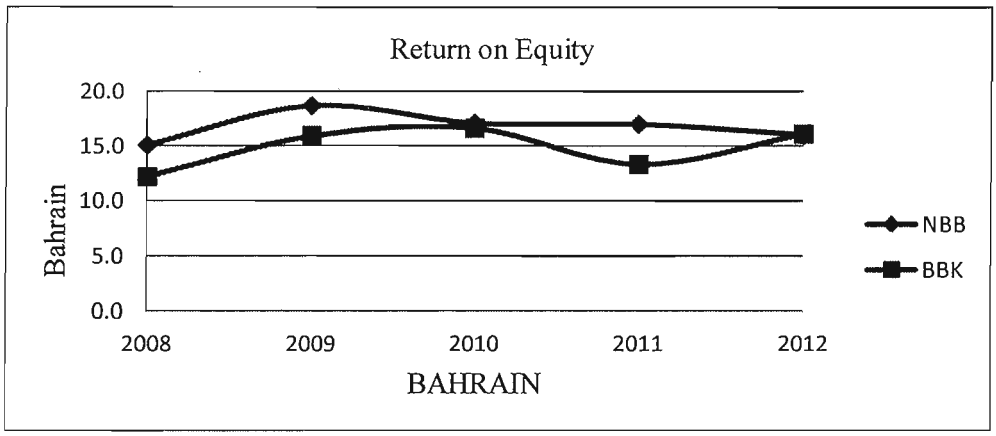

Figure 4.34 Return on Equity of Banks in Bahrain

Figure 4.43, ROE of National Bank of Bahrain was 15.1 % in 2008 and it increased in 2009 to 18.7% and in 2010 it slightly decreased to 17.1% and keep constant with slightly decrease until 2012. On the other hand, bank Bahrain and Kuwait ROE shows stable performance. In2008 ROE was 12.1% which is it increased in 2009 to obtain 15.9% and it keep increasing in 2010 to achieve the highest ratio during the period of study. It decreased slightly decreased in 2011 to 13.3% and it increased again in 2012 to obtain 16.1%. The ROE average was good for both banks and reflects the ability of bank's management to create income from total equity.

ii) Return on Assets

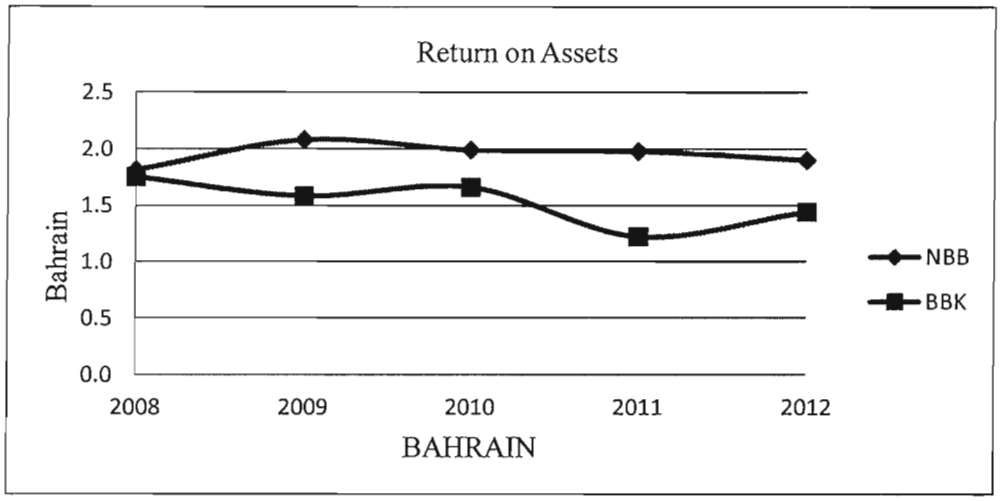

Figure 4.35 Return on Assets of Banks in Bahrain

Figure 4.35, ROA of National bank of Bahrain was 1.8 % in 2008 and it increased in 2009 to 2.8% and in 2010 it slightly decreased to 2 % and keeps constant with little decrease until 2012. Bahrain and Kuwait ROA shows fluctuation performance. In2008 ROA was1.8% and it decreased in 2009 to obtain 1.6 % and it keep increasing in 2010 to achieve the highest ratio during the period of study. It decreased slightly decreased in 2011 to 1.2 % and it increased again in 2012 to obtain 1.4%. The ROA average was good for both banks and reflects the ability of bank's management to create income from total assets in Bahrain banks for the five years

4.2.6.6 Liquidity Risk

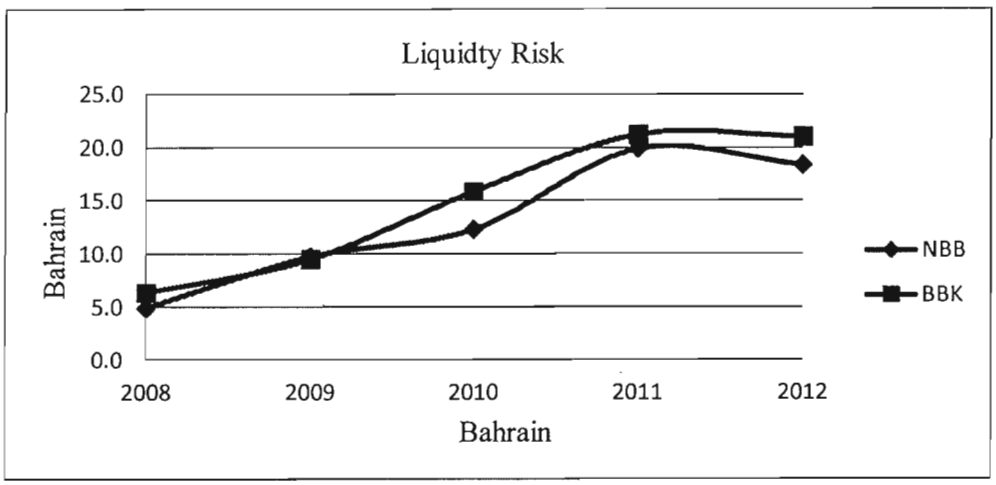

Figure 4.36 Liquidity Risk of Banks in Bahrain

Figure 4.36, liquidity of national bank was 4.9% in 2008 which is quite low but in increased in to 9.7% in 2009. Liquidity in 2010 was increased to 12.3% and it keep increasing in 2011 and obtain 29.9% which is the highest liquidity ratio during the period of study and in 2012 it was 18.3 which is consider the bank have the ability to meet its obligations. In addition, Bahrain and Kuwait bank liquidity ratio indicated that decreasing in 2006 to 6.3% and it increased in 2009 to obtain 9.5 %. In 2010 liquidity increased to 15.8% and it keep increasing until it achieved 21.2% and 21% in 2011 and 2012 respectively and that indicated the highest liquidity on the period.

4.3 **Summary of the Chapter**

In conclusion, the performance of conventional banks in GCC countries is affected by the non-performing loan to total loan and total loan to total deposits. The CAMEL rating system can be explained by five variables as it is useful to evaluate the performance of banks in the GCC countries. ROE in Gulf Bank of Kuwait was negative at the same time ROA was negative. Capital adequacy is not that efficient as expected. Asset quality and management quality examined by the CAMEL and there is low performance in the six countries bank.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

This study investigated the performance of the GCC countries' conventional banks for the period from 2008 to 2012. The chapter summarizes the overall findings and provides discussion on the contribution of the research and recommendations for the future research.

5.1 Summary of Findings and Discussion

CAMEL provides a measurement of banks current overall financial, operational and managerial compliance performance. This study has been conducted to evaluate the bank's performance of the GCC countries using CAMEL framework.

The descriptive analysis suggested that the mean average of capital adequacy for the GCC conventional banks during the study period was at 17.8123 % and the standard deviation was at 3.0328. However it's much better than the other rations result. Asset quality mean average during the five years period was at 5.1967 % it indicated that the non-performing loan rate in GCC countries is very high compare to total loans while the best rate under CAMEL rating system is 1% and the worst is 5 % and above. Management quality ratio, it was more than 100 % and the measurement rate of the CAMEL rating system stated 100 % as a bad loan, however, the rate in general for most of the GCC countries was 121%.Furthermore, ROE average mean rate was 4.8408 in the year of 2008 and then it increased in the next four years. ROA average mean was

1.7414% and that indicated that the GCC banks are profitable during the five years. Liquidity average mean during the five years was 12.8587% and it reflected that there is cash liquidity in all the GCC countries banks.

The findings have answered the research objectives as follows:

Objective1.To determine if capital adequacy affect bank performance. The result of the study indicated that capital adequacy for all the 12 banks in the six GCC countries was above the minimum requirement of CAMEL rating system rates and above the industry average except in Kuwait it was about 0.7 in Gulf Bank of Kuwait at 2008 due to the global financial crises. Overall, the output of trend analysis for capital adequacy shows that these 12 banks in GCC countries can absorb reasonable level of losses occurred due to any operational losses and it will be the protections to the depositors and investors. Furthermore, the banks have ample capital and they no need to external funds. From the above result it infers that the CAMEL framework is suitable techniques to evaluate the performance of a bank.

Objective2.To determine if asset quality affect bank performance. The asset quality is very important parameter to gauge the strength of bank. The result of the study found that the asset quality for all the 12 banks in the GCC countries affected the bank performance during the five years. Asset quality is to measure the non-performing loan to total loan. It found that the non-performing loans in GCC countries are very high compare to total loan. In the banks of Kingdom of Saudi Arabia, the asset quality was 2.14% as satisfactory rate compare to the other GCC countries rates. CAMEL framework stated a rate of 1% is strong and 5% is very weak and used to be called bad

loan. From the above result, the GCC countries banks have a critical situation in term of asset quality and that may affect the internal performance of the banks and it will lead to bankruptcy if the rate of non-performing loans increased in the coming years. According to (Khamis and Senhadji, 2010) and (IMF 2010) found non-performing loan was very high in GCC countries. Moreover, CAMEL framework indicated that the GCC countries facing the same issue and this will affect the banks performance.

Objective3.To determine if management quality affect bank performance. Management quality is important element of the CAMEL Model. The result of this study found that there is a very high rate of the total loan to total deposits in all the six GCC countries except in Saudi Arabia Banks it was average of 68 %. The CAMEL rating system specify maximum standard of loan percentage as 100 % but this study indicated that there is over loan percentage. CAMEL framework is useful model to investigate the critical issues happening in the GCC countries banks. The GCC banks would be unable to meet their obligations in the future and there will be cash flows issues. Financial ratios are the best indicator for evaluating banks performance. The asset quality affected the banks performance in GCC countries during the five years period.

Objective4.To determine if earning ability affect bank performance. It is a very important ratio to measure the financial performance, higher income reflects a lack of financial difficulties and it would be expected to reduce the likelihood failures also it represents the quality of a bank's profitability and its capability to obtain sustainability and growth of the future earnings. This study found that the 12 GCC banks were highly profitable and they are not worry about the financial flow. ROE was calculated by dividing the profit after tax to total equity and ROA calculated as well by dividing profit

after tax to total assets. Both ratios was efficient and highly performance. CAMEL framework used to evaluate the banks performance by using financial ratios to measure the banks internal working cycle. The GCC banks are very rich in term of financial resources. Those banks in the hub of Oil and Gas industrial company's and this help the banks there to stay in a healthy financial situation. The shareholders and investors get very good income from their investments in the GCC banks. In Kuwait, the Gulf Bank of Kuwait was in financial downturn at year 2008 and 2009 and both ROE and ROA was negative but it recover again in the 2010 and the other two years. CAMEL framework is the best indicator for the Banks financial situations. Earning ability has a good impact on the GCC countries banks.

Objective5.To determine if liquidity risk affect bank performance. Liquidity represent the image of bank, liquidity is important aspect which reflects banks capability to meet its financial obligation and new requirements occurred to the banks. This study investigated the liquidity for the GCC banks during the five years period and the result was the 12 GCC banks are highly liquid and there is not any worry about the cash flow of the bank. Their banks are able to meet the obligations and requirement of new business or projects. CAMEL framework is the best measurement for banks performance in GCC countries and over the world. It's the critical and pre size model that will indicate the hidden issues of banks performance. Liquidity highly assessed the banks performance in the Middle East region specifically the six GCC countries.

5.2 Recommendation

This study evaluated the performance of the GCC conventional banks by using the CAMEL framework that included the five components which are capital adequacy, asset quality, management quality, earning ability and liquidity risk. This study used financial ratios as bank performance indicators. To obtain better results, further research should analyze the banks based on longer periods of data and include other financial ratios which are not tested in this study.

Overall CAMEL framework indicated that asset quality and management quality (specifically non-performing loans to total loans and total loans to total deposits) affected the bank's performance of the 12 banks of GCC countries that were evaluated during the study period.

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