Evaluation of riskiness of Indian Banks and probability of book value insolvency


Abstract

Recently, a lot of questions were raised about the financial health of commercial banks in India. This paper analyzes the Indian banks’ riskiness and the probability of book-value insolvency under the framework developed by Hannan and Hanweck (1988). A risk index, known as Z score, for Global Trust Bank that became insolvent in 2004 suggests that the framework developed by Hannan and Hanweck (1988) is also relevant in the Indian context. For a random sample of 15 Indian Banks (public & private sector), we determine the riskiness/probability of book value insolvency over the years and also carry out a relative comparison between public and private sector banks in India. Results obtained in the study show that the probability of book value insolvency of Indian Banks has reduced over years and the probability of book value insolvency is lower in case of public sector banks in comparison to private sector banks.

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The proposed model addresses this issue by using the contingent-claims model for the evaluation of risky debt, based on the pioneering work of Black, Sholes and Merton (BSM). To compare the book value insolvency of public and private sectors. The two hypotheses formed are: There is no significant difference in the book value insolvency of public and private sector banks of India. / There is significant difference in the book value insolvency of public and private sector banks of India. The authors have used t test statistics as a tool for testing the insolvency risk of the banks. They have used banks profits, the realisable profits and capital base of the respective banks. A higher value shows that the Indian banking industry is passing through critical financial position and efforts to improve their profitability and productivity on one hand and caters the social need on the other, the study of the research problem is contemporary. It can search out the major problems and prospects and can suggest an appropriate strategy for improvement of financial performance. Pankaj Sinha, Varundeep Singh Taneja, Vineet Gothi, “Evaluation of Riskiness of Indian Banks and Probability of Book Value Insolvency”, 66. International Research Journal of Finance and Economics, http://www.eurojournals.com/finance.htm, Issue 38 -2010.