

# Camels rating system for banking industry in pakistan: does CAMELS system provide similar rating as PACRA system in assessing the performance of banks in Pakistan?

Babar, Haseeb Zaman

Umeå University, Faculty of Social Sciences, Umeå School of Business.

Zeb, Gul

Umeå University, Faculty of Social Sciences, Umeå School of Business.

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### Abstract [en]

Financial sector of an economy plays an important role in its economic development and prosperity of the country. Banking industry serves as the backbone of the financial sector that accumulates saving from surplus economic units in the form of deposits and provides it to deficit economic units in the form of advances. Banking industry provides support to economy and industries in specific in the time of recessions and economic crisis. But when banks are at the heart of economic recession or banks are the cause of financial crisis like the recent past financial crisis 2007-09, it makes the situation worst for economic recovery. So it is of great importance to keenly observe the performance of the banks and their compliance with the regulatory requirements.

Performance of the banks is measured at two levels, one is at the management and regulatory level of the banks and another is at external rating agencies. Purpose of regulatory and supervisory rating systems is to measure the bank performance at internal level and its compliance with regulatory requirements to keep the bank on right track. These ratings are highly confidential and are only available to the bank management. External credit rating agencies examine and evaluate the banks and issue ratings for the general public and investors in particulars. It is of great importance that both these ratings present the same results about the condition of the banks to provide clear information to investors and management. In past several banks suffer from bankruptcy that was the failure of both internal rating systems and credit rating agencies.

CAMELS is the supervisory and regulatory rating system implemented by State Bank of Pakistan. It takes into account six important components of a bank when it evaluates performance of the bank. These components are Capital, Assets, Management, Earning, Liquidity and Sensitivity to market risk. Ratings is assigned to theses components on the scale of 1 to 5 and that is a base for composite rating that also ranged from 1 to 5. PACRA rating agency is the dominant credit rating agency of Pakistan that performs ratings for most banks and industries in the country. In our research we examine the similarities in the results generated by CAMELS rating system and PACRA rating agency. For that purpose we sample seventeen commercial banks of Pakistan Banking industry.

We observed that results generated by sample banks do not show any similarities with each other. This might be an indication of the banks that went on to bankruptcy in past three to four years or a future threat to financial sector of Pakistan.

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