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Financial Performance Analysis of Banks – A Study of IDBI Bank

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Abstract

Indian Banking industry is led by public sector banks (PSBs) with 80 percent market share. The present study is to compare the financial performance of IDBI Bank with the industry averages on the basis of financial ratios for the period 2011-12 to 2015-16. It was found that the solvency position of IDBI Bank and the employment of assets are in tune with the industry averages. The employment of shareholders' funds and the CASA which is relatively lower than the bellwether suggests that the bank should improve its deposits that provide cheaper funds which can translate in strong financial performance.

Key Words: CASA, IDBI Bank, Profitability Ratios, Public Sector Banks, Shareholders' Fund.

1. Introduction

The Indian economy has weathered the turbulent global economy and emerged as a strong and disciplined economy. It is on the brink of a major transformation with several policy initiatives being announced regularly. Enhanced spending on infrastructure and continued economic reforms has fuelled the growth of the economy suggesting that India's banking sector is also poised for robust growth as the rapidly growing business would turn to banks for their credit needs. The Indian banking system consists of 27 public sector banks and 25 private sector banks. Public sector banks control nearly 80 percent of the market, thereby leaving comparatively much smaller share of the market to the private players.

The core activities of commercial banks are lending funds and accepting deposits to provide payment, liquidity, and credit intermediation services. The foundation of the financial infrastructure is important for the overall health of an economy and its growth. Studies show that both financial intermediaries and markets are important for economic growth, important forms of urban financial investment are bank deposits, shares and securities (Narayana, 1976). Banks are the intermediaries to channelize the savings into investment; they form the backbone of any economy, they take in savings typically as deposits and provide funding primarily in the form of loans. Mudra-SAMIR'S (1992) finds that the working women in urban India save 20 percent of their earnings as savings. The access to low cost deposits enables them to lend the corporate at competitive rates (Pathak, 2005). The banks work closely with their customers and collect the necessary information from the clients during the process of providing funds to the clients who approach them, lay down the covenants that work in favour of both the bank and the customer, unlike the capital markets, where the investments are based on the investor's knowledge thus are risky for the customer. Research shows that the savings are parked in the banks when compared to other medium of investment. Kumar, Banu and Nayagam (2008) found in their study that investors in Tiruchirapalli prefer post office savings, bank deposits, gold, real estate, equity investments and mutual funds in the ranking order. In an economy where a large percentage of the gross domestic savings are invested in the banks, a strong banking system is essentially the order of the day. Indian banks are increasingly focusing on adopting integrated approach to risk management complying with Basel II accord.

Stake holders measure the financial performance, forecast the firm's future earnings and evaluate the financial structure, capital structure along with other components of the statements of the company from the financial statements published by the firm. Financial structure refers to the balance between all of the company's liabilities and its equities. Capital structure, by contrast, refers to the balance between equities and long term liabilities. Financial structure is more sensitive for comparing the firm's debt to its equities. It reflects the status of working capital and cash flow. Capital structure refers to the combination of equities and long term debt. Each business has a different mix depending on its necessities. To assess the financial structure of the companies the analysts perform a static and dynamic analysis of financial statements.

IDBI Bank is among the young public sector banks, incorporated as a commercial bank in the year 2004. The IDBI Bank offers personalized banking and financial solutions to its clients. The IDBI Bank had an aggregate Balance sheet size of Rs.3,74,372 crore and total business of Rs.4,81,613 crore as on March 31, 2016. The Government of India has a dominant shareholding to the tune of 73.98 percent shares followed by Life Insurance Corporation of India, which holds approx. 14.37 percent of the shares. This paper examines the performance of IDBI Bank, the young public sector bank in the face of competition in the banking sector. This paper consists of four sections. The first section presents the introduction

and discusses the background of the financial intermediaries. The second discusses the literature on the financial structure and its impact on the firms. The third section discusses the objectives, methodology and the background. The concluding section summarises the main results.

2. Literature Review

Yusuf and Hakan, (2011) described the short term creditors of a company like suppliers of goods of credit and commercial banks providing short-term loans are primarily interested in knowing the company's ability to meet its current or short-term obligation as and when these become due.

Ross et al., (2007) implied that the most researchers divide the financial ratios into four groups i.e. profitability, solvency, liquidity and activity ratios for detailed analysis.

Eugene F Brigham and Michael C Ehrhardt (2010) stated that financial ratios are designed to help in evaluating financial statements and used as a planning and control tool.

Nadia Zedek (2016) investigated the controlling shareholders affects product diversification performance of 710 European commercial banks, it was found that when banks have no controlling shareholder or have only family and state shareholders diversification yields diseconomies, while the involvement of banking institutions, institutional investors, industrial companies or any other combination of these shareholder categories, produce diversification economies: they display higher profitability, lower earnings volatility and lower default risk.

Abe De Jong, et al (2008) analysed the importance of firm-specific and country-specific factors in the leverage choice of firms around the world. Data suggested that firm-specific determinants of leverage differ across countries, and that there is an indirect impact of country-specific factors on the roles of firm-specific determinants of leverage.

Dimitios Louzius (2012) In his study of Banking sector in Greece found that for all loan categories, NPLs in the Greek banking system could be explained mainly by macroeconomic variables (GDP, unemployment, interest rates, public debt) and management quality.

Muhammad Saifuddin Khan, et al (2016) in his research paper examines the relationship between funding liquidity and bank risk taking in the U.S. bank holding companies from 1986 to 2014, results showed that bank size and capital buffers usually limit banks from taking more risk when they have lower funding liquidity risk.

Malcom and Jeffrey Wurgler (2002) found that effects on capital structure are very persistent. Results suggest that capital structure is the cumulative outcome of past attempts to time the equity market.

Zeitun (2007) investigated the effect which capital structure has had on corporate performance using a panel data sample representing of 167 Jordanian companies during 1989-2003. Results showed that a firm's capital structure had a significantly negative impact on the firm's performance measures, in both the accounting and market's measures.

3. Objectives of the Study

The objectives of this study are

a. To examine and compare the financial performance of IDBI Bank with the industry averages from the viewpoint of a neutral onlooker.
b. To examine and compare the overall profitability of the IDBI Bank with the industry averages.

4. Methodology

The present study is based on secondary data collected from the annual reports of IDBI Bank, State Bank of India (SBI) and Bank of Baroda (BOB) for the period 2011-12 to 2015-16. The large public sector banks i.e. State bank of India and Bank of Baroda, which are listed on the Nifty 50 are considered as proxy for industry averages for the purpose of comparing the performance of IDBI Bank. Ratio Analysis was applied to analyze and compare the trends in banking business and financial performance. Compound Average Growth Rate (CAGR) and ratios have also been deployed to analyze the trends in banking business profitability

5. Results and Analysis

5.1 Shareholders' Funds: Shareholders' funds are made up of the called up share capital and reserves. The IDBI Bank Shareholders' Funds in Table 1 exhibits a 92.40 percentage of reserves as compared to the industry averages given in Table 2 and Table 3 stands at 99.23 percent. The reserves percentage indicates the performance of the bank as the reserves are funds that are set aside from the profits of the bank. The shareholders' funds of IDBI Bank have shown a growth of CAGR of 5.91 percent, while the share capital has exhibited a growth of CAGR of 12.65 percent. This is due to the fact that the reserves and surplus in the last two years showed a slowdown with a negative growth in the year 2016 and the shareholders have pumped in funds gradually every year to meet the capital adequacy norms. IDBI Bank's capital adequacy has fallen to 11.67% as of 31st March due to a surge in bad loans and provisioning in the last two quarters of 2016, following the Reserve Bank of India's asset quality review. The IDBI Bank's performance in the last year is in contrast to the largest public sector bank in India (SBI), which exhibited a strong performance consistently. The trend of the shareholders' funds and its comparison with the bellwether indicates that the IDBI Bank has to improve its operational functioning.

Table 1. Shareholders' Funds of IDBI Bank; 2012-2016 (Rs. in crore)

Year	Share Capital	Reserve & Surplus	Shareholders' Funds	CAGR (Shareholders' Funds)
2011-12	1,278.38	16,294.75	17,573.98	5.91%
2012-13	1,332.75	18,139.73	19,473.25	
2013-14	1,603.94	20,322.08	21,926.47	
2014-15	1,603.96	21,050.11	22,654.26	
2015-16	2,058.82	20,055.15	22,113.97	

Source: Compiled from Annual Reports

Table 2. Shareholders' Funds of SBI; 2012-2016 (Rs. in crore)

Year	Share Capital	Reserve & Surplus	Shareholders' Funds	CAGR (Shareholders' Funds)
2011-12	671.04	83,280.16	83,951.20	14.50%
2012-13	684.03	98,199.65	98,883.68	
2013-14	746.57	117,535.68	118,282.25	
2014-15	746.57	127,691.65	128,438.22	
2015-16	776.28	143,498.16	144,274.44	

Source: Compiled from Annual Reports

Table 3. Shareholders' Funds of BOB; 2012-2016 (Rs. in crore)

Year	Share Capital	Reserve & Surplus	Shareholders' Funds	CAGR (Shareholders' Funds)
2011-12	412.38	27064.47	27476.80	9.98%
2012-13	422.52	31546.92	31969.44	
2013-14	430.68	35555.00	35985.68	
2014-15	443.56	39391.79	39835.35	
2015-16	462.09	39736.89	40198.98	

Source: Compiled from Annual Reports

5.2 Leverage Ratio: Leverage ratios measure the relative amount of funds supplied by equity and debt holders. Debt Ratio is selected for the present study.

5.2.1Debt Ratio: The debt ratio known as debt to assets ratio, measures the financial leverage of the company, determining the firm's ability to pay off the debt in future. It is calculated as total liabilities divided by total assets. A lower debt ratio indicates that a company relies less on borrowing for financing its assets. The debt ratio of the IDBI Bank is consistently maintained at 0.93 times as given in Table 4 indicating a leveraged balance sheet. Companies with higher debt ratios signal that it is time to switch to equity financing to grow their operations. The IDBI Bank has worked in the same direction, which is evident by the increase in its growth in the share capital that has increased gradually from the year 2011. A Comparison with the industry averages given in Table 5 and Table 6 indicates that IDBI Bank has been maintaining the industry averages, if not better in case of debt ratio.

Table 4. Debt Ratio of IDBI Bank; 2012-2016 (Rs. in crore)

Year	Total Liabilities	Total Assets	Debt Ratio
2011-12	270888.41	290316.33	0.93
2012-13	301532.49	322768.51	0.93
2013-14	305357.33	328996.63	0.93
2014-15	331713.47	356030.57	0.93
2015-16	346650.34	374372.13	0.93

Source: Compiled from Annual Reports

Table 5. Debt Ratio of SBI; 2012-2016 (Rs. in crore)

Year	Total Liabilities	Total Assets	Debt Ratio
2011-12	1251568.02	1335519.24	0.94
2012-13	1467377.35	1566261.03	0.94
2013-14	1673952.35	1792234.60	0.93
2014-15	1919641.58	2048079.80	0.94
2015-16	2114788.60	2259063.05	0.94

Source: Compiled from Annual Reports

Table 6. Debt Ratio of BOB; 2012-2016 (Rs. in crore)

Year	Total Liabilities	Total Assets	Debt Ratio
2011-12	419844.62	447321.46	0.94
2012-13	515166.00	547135.44	0.94
2013-14	623518.86	659504.53	0.95
2014-15	675153.20	714988.55	0.94
2015-16	631177.49	671376.48	0.94

Industry Averages Debt Ratio: 0.94

Source: Compiled from Annual Reports

5.3. CASA Ratio: CASA stands for current and savings account. CASA ratio indicates the proportion of current and saving account deposits to total deposit. A higher CASA ratio indicates the availability of low cost funds leading to better operating efficiency of the bank. The CASA ratio of the IDBI Bank presented in Table 7 had climbed from 24 percent to a high of 25.97 percent. The CASA ratio of the IDBI Bank when compared with the industry averages given in Table 7 is lower, indicating the need to increase the ratio so as to improve its bottom line. A declining CASA of SBI, the industry leader suggest an overall stress in raising cheaper sources of funds, the macro environment also may have adversely effected the CASA of IDBI bank.

Table 7. CASA Ratio (in percentage)

Year	IDBI	SBI	BOB
2011-12	24.10	46.64	26.90
2012-13	25.10	46.50	25.32
2013-14	22.60	44.43	25.75
2014-15	25.10	42.88	26.39
2015-16	25.97	43.84	26.36

Source: Compiled from Annual Reports

5.4 Profitability Ratios: are also known as profit margin ratios. They are used to evaluate the overall performance of a company and how well the company is performing in terms of profit. The ratios are indicators of the company's efficiency in using the capital committed by shareholders and lenders. It is the most common method of financial ratios which is used to measure the performance of banks. The RONW, ROA, NPM and OPTWF ratios are selected for the present study.

5.4.1 Return on Networth (RONW): It measures the rate of return on the resources provided by the shareholders. Networth includes Share capital and Reserves & surplus (after adjusting fictitious assets). This ratio measures the amount of earnings for each rupee that the equity shareholders have invested in the company. The higher the ratio, the better it is for the shareholders. The return on Networth ratio of IDBI Bank given in Table 8 indicates that the shareholders are not compensated for their investment

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when compared with the industry averages given in Table 9, suggesting the need for improving its bottom-line.

5.4.2 Return on Assets (ROA): Return on Assets ratio is the relationship between profits and total assets. It is used to measure how effectively a company utilizes its assets to make a profit. It is commonly used to measure the performance of a company. High ROA implies a higher asset-intensity and profitability of the bank. In the case of IDBI Bank the ROA ratio given in Table 8 is showing a declining trend and the comparison with the industry averages given in Table 9 indicates that the IDBI Bank should pay attention towards the utilisation of its assets more effectively.

5.4.3 Net Profit Margin (NPM): Net Profit Margin ratio measures the profitability on the revenue earned. If the ratio is high then it is considered as efficient and profitable. Net profit margin of IDBI Bank shown in Table 8 indicates that the profits of the bank is declining and is well below the industry averages shown in Table 9, suggesting that the operations of the bank has to improve.

5.4.4 Operating Profit to Working Fund (OPTWF): This ratio determines the operating profits generated by employing working funds. It measures the percentage of average of working fund earned by banks as net profit. If the ratio is high than it is considered as better earning potential of the bank. As given in Table 8 IDBI Bank has in the last fiscal has managed a profit of 1.6 percent of the working funds which has drastically been reducing, when compared with industry averages given in Table 9.

Table 8. Profitability Ratios of IDBI Bank; 2012-2016

Year	Return on Networth (RONW)	Return on Assets (ROA)	Net Profit Margin (NPM)	Operating Profit to Working Funds (OPTWF)
2011-12	11.56	0.83	8.69	1.64
2012-13	9.66	0.72	7.50	2.10
2013-14	5.11	0.41	4.21	2.06
2014-15	3.85	0.29	3.10	1.92
2015-16	-16.57	-1.09	-13.06	1.60
Averages	2.722	0.232	2.088	0.082

Source: Compiled from Annual Reports

Table 9. Industry Averages; 2012-2016

Return on Networth	9.28
Return on Assets	0.62
Net Profit Margin	8.23
Operating Profit to Working Funds (OPTWF)	1.85

Source: Compiled from Annual Reports

5.5 Activity Ratios: They are also known as turnover ratios. Turnover ratio means the number of times the assets are converted into sales. Assets Turnover ratio is selected for the present study.

5.5.1 Assets Turnover Ratio: Assets turnover ratio is the relationship between sales and assets. It measures the efficiency of a company in utilising its assets to generate sales. A high assets turnover ratio indicates that the company is efficiently utilizing its assets to generate sales. The assets turnover ratio of IDBI Bank given in Table 10 indicates that it consistently maintained 0.08 throughout the study period and matches with the industry averages given in Table 11

Table 10. Assets Turnover Ratio of IDBI Bank

Year	2011-12	2012-13	2013-14	2014-15	2015-16
Assets Turnover Ratio	0.09	0.08	0.08	0.08	0.08

Source: Compiled from Annual Reports

Table 11. Industry Averages

Year	2011-12 to 2015-16
Assets Turnover Ratio	0.08

Source: Compiled from Annual Reports

6. Conclusion

The solvency position of IDBI Bank and the employment of assets are in tune with the industry averages. The employment of shareholders' funds and the CASA which is relatively lower than the bellwether suggests that attention has to be paid in these areas. Net profit margin of IDBI Bank indicates that the profits of the bank is declining and is well below the industry averages suggesting that the operations of the bank has to improve. The IDBI Bank should improve its deposits that provide cheaper funds, which can translate into strong financial performance. The ROA of IDBI Bank is showing a declining trend and the comparison with the industry averages indicates that the IDBI Bank should pay attention towards the utilisation of its assets more effectively.

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