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A Comparative Study of Profitability Analysis in Banking Sector of Bangladesh

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ACOMPARATIVESTUDYOFPROFITABILITYANALYSISINBANKINGSECTOROFBANGLADESH

A Comparative Study of Profitability Analysis in Banking Sector of Bangladesh

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Abstract- Bangladesh is a developing country with an underprivileged banking system. In the last two years, Bangladesh's economic extension was quite remarkable from the viewpoint of GDP growth rate. However, the scenario of the developed countries banking sector is opposite of the banking sector in Bangladesh. Although Bangladesh has many other economic sectors, in contributing the nation, banking is one of the major areas. In various categories with several banks the sector forms. Considering proprietorship the segments are classified into four major categories- such as Nationalized Commercial Bank, Private Commercial Bank, Development Financial Institutions, and Foreign Commercial Banks. This study made a comparison of profitability in these four sectors of banks in Bangladesh. The research objective was to compare the trends of profitability ratios by types of banks in Bangladesh, and the data used in this paper was collected from secondary sources.

Keywords: bank, banking system, profitability ratio, return on asset (ROA), return on equity (ROE).

I. Introduction

The very timeworn institution that is contributing towards the development of any economy and is considered as an important service in today's modern world is termed as Bank. Currently, the purpose of a bank is not restricted to within the same geological boundary of any country. It is because of globalization and free market economy, this industry is going through huge antagonism in any country and execution of WTO will further increase competition. As bank operates on the economy of a country so its performance also relies on it along with the banking industry. As a developing country, the scenario of the banking sector in Bangladesh is completely reverse with the banking sector in developed countries. Along with other service sectors in Bangladesh economy, the banking sector is considered as one of the major service areas and can be divided into four categories: Nationalized Commercial Bank, Private Commercial Bank, Development Financial Institutions and Foreign Commercial Banks. After the liberty, the banking industry in Bangladesh started its journey with 6 nationalized commercialized banks, 2 State-owned specialized banks and 3 Foreign Banks.

Performances of individual banks are evaluated based on their specified objectives. A bank managerial body, for example, may find it necessary to classify and draw attention to banks that are experiencing unbroken financial sufferings that they may fix them before they get out of control. Alternatively, it is vital for the shareholders to evaluate which banks would be suitable to financially invest in. Predictably, commercial banks are observed their performance over a given period consequently determining the efficiency and long term feasibility of management decisions or goals and therefore can change the course and make changes whenever it is appropriate. With regular and typical monitoring of performance, fundamental tribulations may remain imperceptible and escort to financial failures added down the line.

The overall objectives of this research is to compare the profitability analysis of four types of banks namely; State Commercial Banks (SCBs), Development Financial Institutions(DFI), Private Commercial Banks (PCBs), Foreign Commercial Banks (FCBs) in terms of Return on Assets (ROA) and Return on Equity (ROE) that will indicate the performance developments over the period 2009-2016.

II. Literature Review

Syed Moudud-Ul-Huq (2017) in his paper, primarily measured the financial performance of the banking industry of Bangladesh for the 2013-2014 and rated them according to the composite rating system. In this paper, only ten private commercial banks have been considered, and CAMEL has been used to analyze the financial performances of these banks. The paper found out that the act of most banks is reliant more on the managerial capability in formulating strategic plans and the competent execution of its strategies. Upholding of asset quality is the major challenge seen in the paper and forecasted that it would remain so. The banking sector in Bangladesh has passed an average year in terms of ascendancy, prosperity, and dependability in 2013.

A random survey was conducted on six commercial banks of Bangladesh by Jahan (2012). The determinants of banks profitabilities were used widely, namely ROA, ROE, and ROD and these are also commonly used a criterion of Bangladesh Bank to evaluate banks performance. The results obtained from the regression analysis are the explanatory variables – operational efficiency, asset size, and ROD to be positively related and asset utilization to be negatively

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related to ROA, but these associations are statistically insignificant.

Uddin and Suzuki (2011) analyzed data from 38 commercial banks for the period 2001-2008 and found that income and cost efficiency of the considered sample banks have risen up by 37.84 percent and 15.28 percent respectively in 2008 compared to 2001. Likewise, non-performing loans and return on assets also were responsible for the improvement in bank performance. The results that were outshone by regression models represent that foreign ownership has a statistically positive impact on bank performance. On the other hand, private ownership has a constructive impact on income efficiency, return on assets, and non-performing loans, while the negative impact on cost efficiency.

Sufian and Habibullah (2009) considered the performance of 37 Bangladeshi commercial banks for the period 1997 to 2004 and observed that bank-specific characteristics, loan intensity, credit risk, and cost have positive and noteworthy impacts on bank performance, whereas non-interest income exhibits negative affiliation with bank profitability. The pragmatic findings suggest that size hurts on return on average equity (ROAE), while it is the opposite in case of return on average assets (ROAA) and net interest margins (NIM). As for the influence of macroeconomic indicators, they found no noteworthy impact on bank profitability, excluding for inflation, which has a pessimistic relationship with banks profitability.

From the above review of literature, I have studied that financial performance of banks was measured by CAMEL tool with only a few private banks of two years, whereas in the present more than 40 private banks are in Bangladesh. My other observation was, in one study where the taken years of remark was very backdated, which is now not that much substantial as the current scenario is much different than previous ones. Alongside, it was found that comparison make based on income and cost efficiency for the year of 2001 compared with 2008 data, which in my view not sufficient to compare the profitability of banks. In the last ten years, the economic and political situation of Bangladesh has gone through many changes. So, in my observation, profitability comparison should be making for recent years, considering more number of banks with different tools. These were the reason that, in my study, trends of profitability was compared by calculating ROA and ROE of four different types of banks in Bangladesh for the year of 2009-2016.

III. Objectives of the Study

The main objective of the paper is to compare the trends of profitability ratios by types of banks in Bangladesh. A total of four types of banks are studied from the period 2009-2016, respectively. The specific objectives of the study are:

1. To find out some glaring reasons for lower efficiency in SCB and DFI banks and suggest ways and means improve the efficiency of these two banks.
2. To suggest the future prospect of these four types of banks.

IV. Research Methodology

- Tools for Data Collection: The data collected for this study is secondary. Along with data collected from the Annual Report 2016 from Bangladesh Bank, various data from different annual reports of different respective banks, journals, reports on trends, newspapers, magazines, books, and websites have been followed.
- Tools for Data Analysis: SPSS software has been used to calculate the deviation mean and therefore analyze the results.

V. Importance of the Study

The Bangladesh banking industry is going through a phase of customers market. Apparently, customers have more choices in their bank. The competition is getting stiffer day by day. With enormous competition and advanced technology, the services provided by the banks are becoming convenient. This study will give a further base involved in this field.

VI. Analysis

Considering the following Table obtained from the online source of Bangladesh Bank, the Standard Deviation of all the enclosed banks have been studied:

Table 1: Trends of Profitability ratios by types of Banks

	Return of Assets (ROA)								Return on Equity (ROE)							
Bank Types	2009	2010	2011	2012	2013	2014	2015	2016	2009	2010	2011	2012	2013	2014	2015	2016
SCBs	1.0	1.1	1.3	-0.6	0.6	-0.6	-0.04	-0.16	26.2	18.4	19.7	-11.9	10.9	-13.6	-1.5	-6.0
DFIs	0.4	0.2	0.1	0.1	-0.4	-0.7	-1.2	-2.80	171.7	-3.2	-0.9	-1.1	5.8	-5.97	-5.8	-13.9
PCBs	1.6	2.1	1.6	0.9	1.0	1.0	1.0	1.03	21.0	20.9	15.7	10.0	9.8	10.3	10.8	11.1
FCBs	3.2	2.9	3.2	3.3	3.0	3.4	2.9	2.56	22.4	17.0	16.6	17.3	16.9	17.7	14.6	13.1
Total	1.4	1.8	1.5	0.6	0.9	0.6	0.8	0.68	21.7	21.0	17.0	8.2	11.0	8.1	10.5	9.4

Source: Bangladesh Bank Annual Reports (2009-2016)

- Return on Assets (ROA)

Return on Assets (ROA) indicates the productivity of assets, i.e. how much income is generated from per unit of assets.

Table 2: Return on assets (ROA) (Percent)

	Return of Assets (ROA)							
Bank Types	2009	2010	2011	2012	2013	2014	2015	2016
SCBs	1.0	1.1	1.3	-0.6	0.6	-0.6	-0.04	-0.16
DFIs	0.4	0.2	0.1	0.1	-0.4	-0.7	-1.2	-2.80
PCBs	1.6	2.1	1.6	0.9	1.0	1.0	1.0	1.03
FCBs	3.2	2.9	3.2	3.3	3.0	3.4	2.9	2.56
Total	1.4	1.8	1.5	0.6	0.9	0.6	0.8	0.68

Source: Bangladesh Bank Annual Reports (2009-2016)

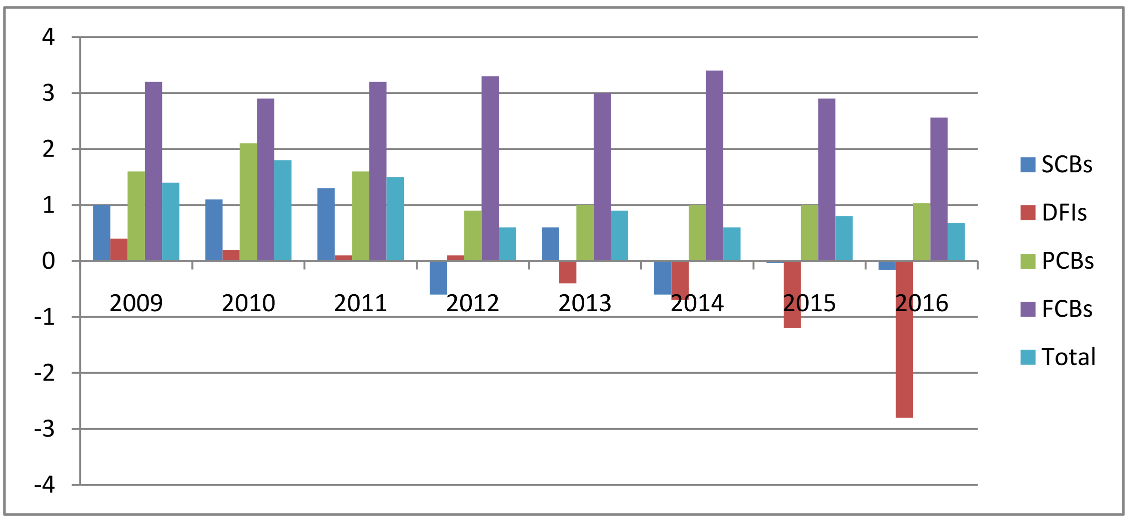

Figure 1: Return on Assets

The above table and figure show that SCB's had an uprising figure with more than 1 percent from the year 2009 till the year 2011.However, the year 2012 showed drastic decline with -06 percent, which was recovered by the year 2013 to.6 percent. Consequently, for the further years, SCB's showed continuous fall till 2016.The development is much worse in the case of DFI, where most of the time, ROA was negative. The reason is provision shortfall and insignificant profit during the period. PCB's had risen after a fall in the year 2012 to 1.03 percent in the year 2016. FCB had comparatively strong ROA over the whole studied period.

- Return on Equity (ROE)

Return on Equity (ROE) is another measure of earning and profitability determination, which indicates net income after tax to total equity. The amount of profit generation for the equity shareholders is found from the ratio. A higher value of ROE is an indication of high productivity of impartiality.

Table 3: Return on equity (ROE) (Percent)

	Return on Equity (ROE)							
Bank Types	2009	2010	2011	2012	2013	2014	2015	2016
SCBs	26.2	18.4	19.7	-11.9	10.9	-13.6	-1.5	-6.0
DFIs	-171.7	-3.2	-0.9	-1.1	5.8	-5.97	-5.8	-13.9
PCBs	21.0	20.9	15.7	10.0	9.8	10.3	10.8	11.1
FCBs	22.4	17.0	16.6	17.3	16.9	17.7	14.6	13.1
Total	21.7	21.0	17.0	8.2	11.0	8.1	10.5	9.4

Source: Bangladesh Bank Annual Reports (2009-2016)

Figure 2: Return on Equity (ROE)

The above table and figure show that SCB's had a decreasing amount with more than 20 percent from the year 2009 till year 2012.However, the year 2013 showed a radical turn up with 10.9 percent, which was beaten by the year 2014 to 13.6 percent. Consequently, for the further year, SCB's showed continuous fall till 2016.The situation is much worse in the case of DFI, where most of the time ROE was negative regardless of the year 2013. The reason may be huge asset turnover, less number of the share issue, and high distribution of dividend during the period. PCB's had risen after a fall in the year 2013 to 11.1 percent in the year 2016. FCB had comparatively strong ROE over the whole studied period without any fall.

SCBs

Statistics

ROA (2009-2016)

N	Valid	8
	Missing	0
Mean		.3250
Std. Deviation		.77110

Statistics

ROE (2009-2016)

N	Valid	8
	Missing	0
Mean		5.2750
Std. Deviation		15.46478

DFIs

Statistics

ROA (2009-2016)

N	Valid	8
	Missing	0
Mean		-.5375
Std. Deviation		1.05822

Statistics

ROE (2009-2016)

N	Valid	8
	Missing	0
Mean		-24.5962
Std. Deviation		59.70101

PCBs

Statistics

ROA (2009-2016)

N	Valid	8
	Missing	0
Mean		1.2787
Std. Deviation		.43413

Statistics

ROE (2009-2016)

N	Valid	8
	Missing	0
Mean		13.7000
Std. Deviation		4.85151

FCBs

Statistics

ROA (2009-2016)

N	Valid	8
	Missing	0
Mean		3.0575
Std. Deviation		.27181

Statistics

ROE (2009-2016)

N	Valid	8
	Missing	0
Mean		16.9500
Std. Deviation		2.69550

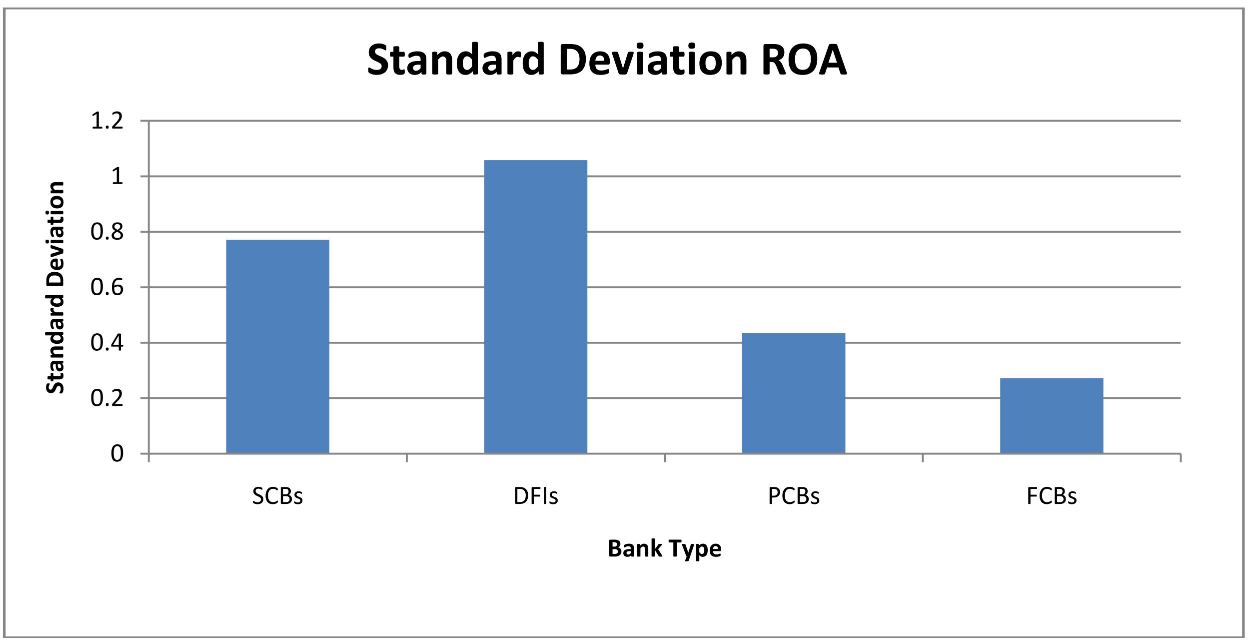

Figure 3: ROA standard deviation comparison

The reason for fluctuating records in ROA is a permutation of several impacts - declining profits, diminishing asset productivity, working capital inefficiencies, considerable asset acquirement, etc. Nevertheless, the most evident causes can be categorized at the very top as either i) negative impacts on net income or ii) "heaviness" in an entity's asset holdings.

- To be more specific ROA in the above-mentioned banks have fallen for the following causes:

1. A reduction in credit supply by the specified banks has reduced its market share as well as its income (e. g, fees and interest) and profits. This reduction created a negative impact on banks' profitability and on their ability to keep hold of earnings in the future.
2. Under-utilization of fixed assets
3. High working capital (A/R + Inventory - A/P)
4. Reduced profit margin.

- Ways of enhancing ROA are as follows:

Magnification in the percentage of return on assets is a manifestation of profitability for a business.

1. An increase in the percentage of return on assets is caused by control of business expenses. It is one of the reasons behind it. When there is a gross profit in business, it can be anticipated to improve and even increase its return on assets.

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2. An elevation in the percentage of return on assets refers, that a company has invested its debt shrewdly. When finance debt capital is paid more by the company than the amount that it is receiving from investing this debt capital, the return on asset is low.
3. An enhancement in the sale, while decreasing expenses, may enhance the percentage of return on assets. Improving sales to influence on ROA necessitates a commensurable reduction in expenditures. While sustaining, increasing the cost of goods sold, the current assets may also increase the percentage of ROA.
4. The number of sales generated by an asset can be defined as asset turnover. An escalation in asset turnover calls for escalating sales with the same number of properties as retaining sales with a reduced number of assets.

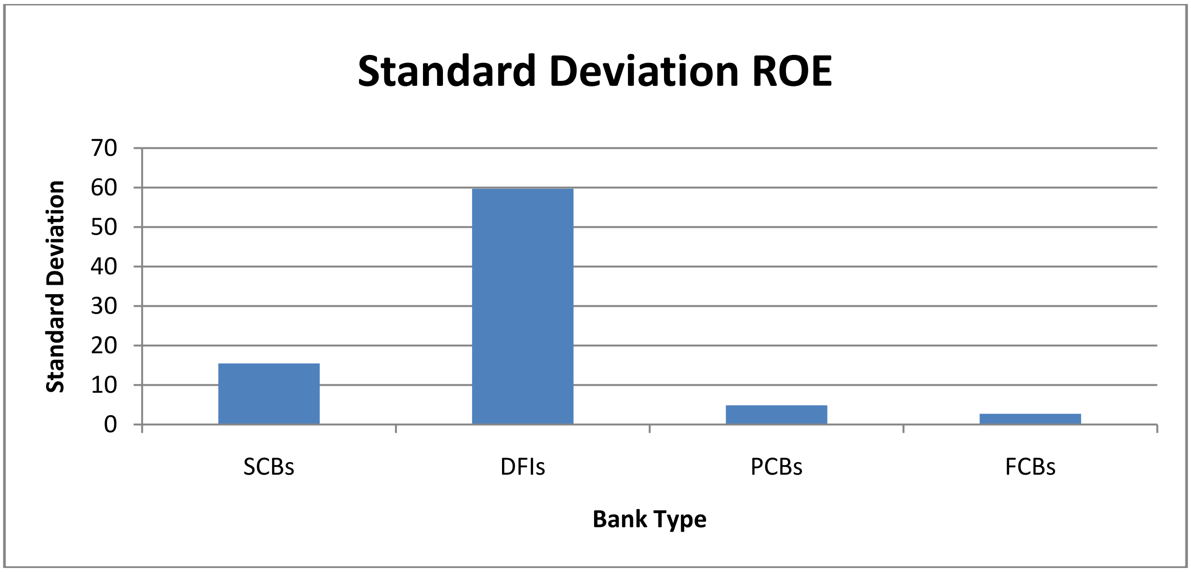

Figure 4: ROE standard deviation comparison

- Ways to improve ROE:

For improving ROE, banks have three other instruments in addition to enlightening their profitability, to meet the desires: decreasing dividend payouts to increase their equity, equity rising by allowing new shares (or similar forms of bank capital) or decreasing risk-weighted assets by withdrawing parts of their portfolio.

- Other ways to improve ROE are:

1. A company's return on equity is increased artificially often by tax rates.
2. Growing profits comparing to parity increases a company's return on equity as profits are the numerator of the return on equity ratio.
3. Asset turnover is calculated by dividing sales by the company's total assets, and it is a degree of a company's proficiency. Commonly, a company should be more profitable and should earn an upper return on equity when it can produce added sales comparing with its assets.
4. To leverage a company and lift its return on equity, idle cash should be circulated among the shareholders.
5. Risk-weighted assets are another reason for decreasing ROE. So, to improve capital ratios, this kind of assets should be reduced by selling parts of their portfolio.
6. The tool obtainable for banks to raise their equity is to give a slighter share of their profits in the form of dividends (retained earnings).
7. Share issuance helps increasing equity relatively quickly and substantially.
8. When the company's return on equity is higher than the after-tax cost of debt, financial leverage increases a company's return on impartiality.

VII. Conclusion

The aim of this paper was to evaluate the trends of profitability ratios of different banks in Bangladesh. The analysis period was of 2009-2016. A substantial rise in a collection of loans in a particular bank adversely affected ROA and ROE of the banking industry. A reduction in credit supply by an individual bank would reduce its market share as well as its income and profits. This would hurt banks' profitability and on their ability to retain earnings in the future.

Both the factors substantially increased the provision maintenance requirement and hence reduced the net income. Accordingly, banking sector return on equity (ROE) had decreased, equivalent to the drop in net profit. The moderation in the loan rescheduling standard allowed banks to preserve inferior requirements, which ultimately helped to enhancement profitability. Bangladesh Bank, usually, supervises the banks to ensure that actual provision is kept by the banks in compliance with their higher provision requirements. It was necessary for Bangladesh Bank to uphold its observation, and the bank had to maintain its provision.

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