CLEAR IJRMST *Volume-04* *Issue-07* *Jan-Jun 2014*
Online-ISSN: 2249 -3506
Print-ISSN: 2249 -3492
www.thaavan.org

Financial Analysis of Commercial Banks - A Comparative Study

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Abstract

Banking Sector plays an important role in economic development of a country and is featured by a large network of bank branches, which serves many kinds of financial services of the people. State Bank of India (SBI) and Housing Development Finance Corporation Limited (HDFC) are selected as sample banks for the study as they are top banks in the domain of public and private sectors. The State Bank of India, popularly known as SBI is one of the leading public sector bank in India. In this paper, an effort has been made to analyze the financial performance of public and private sector banks. The study is a case method of Research and comparative analysis in nature. The study used only secondary data that was collected from research articles, books related and thesis works already done on the topic and particularly from annual reports of SBI and HDFC Bank.

***Keywords**: Financial Analysis, Commercial Banks, financial performance, ratios.*

Introduction

India's banking sector is constantly growing. With the potential to become the fifth largest banking industry in the world by 2020 and third largest by 2025, India's banking and financial sector is expanding very quickly. The Indian Banking industry is currently worth Rs. 81 trillion (US $ 1.31 trillion) and banks are now utilizing the latest technologies like internet and mobile devices to carry out transactions and communicate with the masses. The Indian banking sector consists of 27 public, 20 private sector banks and 43 foreign banks along with 61 regional rural banks (RRBs).

The Banking Laws (Amendment) Bill that was passed by the Parliament in 2012 allowed the Reserve Bank of India (RBI) to make final guidelines on issuing bank licenses. The role of the Indian Government in expanding the banking sector is noticeable. It is expected that the new guidelines issued by RBI will curb practices of impish borrowers and streamline the loan system in the country. In the coming years, India could see a rise in the number of banks, a shift in the style of operation, which could also evolve by including modern technology in the industry. The banking system of India is featured by a large network of bank branches, which serves many kinds of financial services of the people. State Bank of India (SBI) and Housing Development Finance Corporation Limited (HDFC) are selected as sample banks for the study as they are top banks in the domain of public and private sectors. In this paper, an effort has been made to analyze the financial performance of public and private sector banks.

Financial statements are prepared primarily for decision-making and they play a dominant role-in setting the framework of decision making. The information provided in financial statements is not an end in itself as no meaningful conclusions can be drawn from these statements. The information provided in the financial statements is of immense use in making decisions through financial analysis. Financial analysis is "the process of identifying the financial strengths and weakness of a firm by properly establishing relationship between the balance sheet and profit and loss account". The techniques of financial analysis are comparative balance sheets statements, trend analysis, common size statements, funds flow and cash flow statement, cost volume-profit analysis, and particularly in banking, the financial analysis is very much essential as they deal with money of the public. Ratio analysis methodically classifies the data of banks income statement and Balance sheet by establishing the relationship among various items of those statements, wherefrom many performance indicators can be received by the managers and can understand well about the functioning and financial performance of a bank. It is very vivid that the financial performance of individual banks differ from one to another, however, the performance as discussed is also distinguishable between public sector banks and private sector banks.

Literature Review

1. **K. Sriharsha Reddy(March 2012)** suggested CAMEL Approach to evaluate relative performance of banks in India. It is found that public sector banks have significantly improved indicating positive impact of the reforms in liberalizing interest rates, rationalizing directed credit and Investments and increasing competition.
2. **Amitava Mandal, Santanu Kumar Ghosh(2012),** made an attempt to investigate empirically the relationship between intellectual capital and financial performance of 65 Indian banks for a period of ten years from 1999 to 2008. The analysis indicates that the relationships between the performance of a bank's intellectual capital, profitability and productivity are varied.
3. .**Mohammad Firoz(2011)**, made an attempt to analyze the preparations carried out by the Indian banking industry for the implementation of the International Financial Reporting Standards on and after 1 April 2011. The main finding of this paper is that the Indian banking industry is preparing according to the target for convergence from 1 April 2011, but alteration in the various statutory laws of India are yet to be implemented / approved by the government.
4. **Pankaj Gupta and Seema Garg(2011**), states that it is due to fierce competition with financial corporate, banks have to use various performance measurement tools to improve the quality of their services. The study investigates, analyses and compares the efficiency of 49 Commercial Banks by employing the Data Envelopment Analysis (DEA) resulting in the delineation and identification of the causes of inadequate performance. The study reveals that there is a variation in the technical efficiency and the scale efficiency of most of the banks.

Objectives of the Study

1. To find out various financial services and facilities offered by the public and private sector banks.
2. To compute and compare the financial performance of SBI and HDFC through Investment valuation ratios.

Hypothesis of the Study

H_0 : The financial performance in terms of Investment Valuation Ratios of SBI and HDFC bank does not differ significantly

H_1 : The financial performance in terms of Investment Valuation Ratios of SBI and HDFC bank does differ significantly

Scope and Limitations of the Study

The present study focuses on a critical evaluation of financial performance of select public sector and private sector banks through Investment Valuation ratios. Though the study is very comprehensive in nature, it is subjected to the limitations as under:

1. One of the major limitations of this study is all the banks in Hyderabad were not considered as the network of operation of all the banks is quite distinguishable.
2. The banks considered are SBI from Public sector Banks and HDFC from private sector banks as they are the leading banks.
3. Co-operative banks and foreign banks are kept out of the study as they follow different set of guidelines given by RBI.

Research Methodology

The study is a case method of Research and comparative analysis in nature. The study used only secondary data that was collected from research articles, books related and thesis works already done on the topic and particularly from annual reports of SBI and HDFC Bank. State

Bank of India (SBI) and Housing Development Finance Corporation Limited (HDFC) are selected as sample banks for the study as they are top banks in the domain of public and private sectors. The total time period of the study is 5 years, i.e. 2008-2012. To prove the authenticity of the findings, t-Test and Test of difference between proportions are employed.

Data Analysis & Interpretation

Dividend per Share:

The amount of dividend that a stockholder will receive for each share of stock held is called Dividend per Share. The formula for calculating DPS is the total amount of dividends paid divided by the total shares outstanding. The following table is a modest attempt to analyze Dividend per Share of SBI and HDFC.

Dividend Per Share		
Years	**SBI**	**HDFC**
2008	35	**4.3**
2009	30 (-14.3)	**16.5** **283.7**
2010	30 0	**12** **(-27.3)**
2011	29 (-3.3)	**10** **(-16.7)**
2012	21.5 (-25.9)	**8.5** **(-15)**
Average	29.1	**10.26**
	t-Value	**6.37**
	t-Critical	**2.31**

Source: Secondary data

It is clear from the above table that the Dividend per Share of SBI is completely declined whereas the Dividend per Share of HDFC Bank initially increased and afterwards declined.

Operating Profit per Share

Operating profit per share ratio establishes the relationship between operating profit and sales. In other words, it indicates the portion remaining out of every rupee worth of sales after all operating costs and expenses have been met. In the following table, an attempt has been made to analyze the operating profit per share of select banks.

Operating Profit Per Share		
Years	**SBI**	**HDFC**
2008	289.44	**37.71**
2009	255.39 (-11.76)	**160.36** **(+325.2)**
2010	229.63 (-10.1)	**106.25** **(-33.7)**
2011	230.04 (+0.18)	**92.36** **(-13.1)**

2012	173.61 (-24.5)	**107.32** **(+16.2)**
Average	235.62	**100.8**
	t-Value	**4.94**
	t-Critical	**2.31**

Source: Secondary data

It is evident from the above table that the Operating Profit per Share of SBI and HDFC Bank reported a mixed trend. It is because of the dynamics in the business profits of both the banks. As the size and operational levels are quite different, the two banks are differing absolutely in terms of operating profits.

Net Operating Profit per Share

Net operating profit represents the profitability of a company after accounting for cost of goods sold and operating expenses. In the following table, an attempt has been made to present the net operating profit per share of select banks.

Net Operating Profit Per Share

Years	SBI	HDFC
2008	1776.47	**138.66**
2009	1504.34 (-15.32)	**524.34** **(+278)**
2010	1353.15 (-10.05)	**436.3** **(-16.8)**
2011	1179.45 (-12.84)	**464.77** **(+6.6)**
2012	899.83 (-23.7)	**348.57** **(-25)**
Average	1342.648	**382.53**
	t-Value	**5.91**
	t-Critical	**2.31**

Source: Secondary data

The above table exhibits Net Operating Profit per Share of SBI and HDFC Bank. It can be observed that the Net Operating Profit per Share is completely declined whereas it reported a mixed trend in case of HDFC Bank. The declining trend of net operating profit might be caused by the volatility of interest rate.

Test of Hypothesis I

H_0 : The financial performance in terms of Investment Valuation Ratios of SBI and HDFC bank does not differ significantly

H_1 : The financial performance in terms of Investment Valuation Ratios of SBI and HDFC bank does differ significantly

Type of Ratios	Name of the Test	Degrees of freedom	Level of significance	Calculated Value	Critical Value	Decision
Dividend Per Share	t-test	8	5%	6.37	2.31	Rejected
Operating Profit Per Share				4.94	2.31	Rejected
Net Operating Profit Per Share				5.91	2.31	Rejected

Source: Primary data

With the help of t – test, it is examined that there is a significant difference in the financial performance in terms of Investment Valuation Ratios of SBI and HDFC Bank. The calculated t-value of Dividend per Share, Operating Profit per Share and Net Operating Profit per Share is greater than Critical Value and therefore the hypothesis is rejected.

Findings of the study

1. The Dividend per Share of SBI is completely declined whereas the Dividend per share of HDFC Bank initially increased and afterwards declined.
2. The operating profit per share of SBI and HDFC reported a mixed trend. It is due to dynamics in the business profits of the individual banks.
3. The net operating profit per share of SBI is found declining whereas, HDFC Bank reported very least growth as the operating profits of SBI differed significantly from HDFC bank.

Conclusion

With regard to banking activities, the performance of HDFC is better than SBI and for the investors who are intended for long term investments HDFC is better but with respect to the growth in the market, SBI is more appropriate. The analysis shows that HDFC Bank has satisfactory NPA's, Net profit margin, Net Interest margin & Return on equity which states that it is managing it assets far better than SBI but with regards to share value performance SBI share value is better in the market when compared to HDFC. Overall analysis states that financial performance of HDFC is better than SBI.

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