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# Financial Analysis of Public Sector Undertaking: A case study of Allahabad Bank

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**ABSTRACT** The Bank is derived from a French word 'Banque' which means bench. The Jews were believed to be early bankers, who used to transact business over the benches within the market. In India, Banking is experienced since Vedic Period, which can be proved through the writings of Jurist Manu which was related to advances, interest and deposits. During the Mughal period, the development of indigenous banker worked significantly in the expansion of trade and commerce via lending money. Later, during the rule of the East India Company, the banking sector was handed by agency houses. In the year, 1990 the economic reforms introduced by Indian Government played a significant role in setting up the banking sector which is experienced currently. Introduction of Liberalization gave a gateway to the development of private sector bank which pushed the competition in the banking sector. It also led to the arrival of new technology, less intervention of government etc. The reason for portraying the thesis as Phd. Thesis was to incur in-depth knowledge of Allahabad Bank's financial statement and the working of the bank through comparative analysis and ratio analysis for 2014 and 2015.

**KEYWORDS** : Bank, Public sector, Financial Analysis

## INTRODUCTION

The process of conversion of raw information which is delivered from the financial statement into useful financial information is known as Financial Analysis. All the decisions undertaken by the organization are based on the financial analysis. Such decisions include programmed decisions which are related to the problems of routine type, non–programmed decisions are decision made in difficult situations and the problem is not routine type, strategic decisions are decision which has to be precisely taken care of and which affects the objectives, important policies and organizational goal of an organization. Such decisions are of non–repetitive nature and taken by top level management. Another type of decision is tactical and operational decision, where on one hand, tactical decision is concerned with organizational policy matters, taken by top – level management and affects the organization in the long term. On the other hand, operational decision is related to day to day working of the organization. Such decisions are taken by middle and lower level manager.

As stated earlier, the above decisions can only be undertaken when financial analysis is done through financial statements. Financial statement comprises of balance sheet also known as position statement, trading and profit/ loss account also known as income statement, and cash flow statement. Balance sheet provides the information of assets, liabilities and capital, which an organization holds. The balance sheet is based on the accounting equation:

Assets = Liabilities + Shareholders' Equity.

Trading and Profit/ Loss Account are the most popular statement, which includes revenue generated during the period, expenses incurred and income earned during the year. The Income statement is based on the underlying equation:

Income = Revenue – Expenses.

Cash Flow Statement is the third most important statement provided by the organization which also plays an important role in decision making. Cash Flow Statement involves three major heads:

- Cash Flow from Operating Activities deals with income generated from day to day activities.
- Cash Flow from Investing Activities deals with the purchase and sale of investments like plant, machinery, equity, debt etc.
- Cash Flow from Financing Activity deals with collection and repayment of Capital.

To examine the financial health of an organization, it is vital to understand and analyse all the three financial statement. There are two groups in an organization who are interested in the information: internal users and external users.

### Company Profile

The study is based on one of the oldest nationalized banks in India, namely Allahabad Bank. On 24th April 1865 Allahabad Bank was set by a European Group in Allahabad having a subscribed capital of Rs. 3 lakh.

Allahabad Bank provides diversified range of product and services to their customers which includes Personal Banking, Social Banking, MSME Banking, Retail Credit Products, Corporate Banking, International Banking and Other Services like Insurance Repository Services, Insurance and Mutual Fund Scheme for depositors maintaining a Saving Account and Current Account or Term Deposit Account

## LITERATURE REVIEW

**In September 2013, Adrian Costein and Florian Neager** emphasized on bridging the banking sector with the real economy from a financial stability perspective. Their study included three tools, namely: probability of default model for the development and calibration, macroeconomic credit risk module and measuring the risk to financial stability. They tested the tool on the Romanian economy and concluded that the banking sector is in good shape and the up trending level of provisions can be easily used in a systematic manner.

**Cheenu and Chitwan (2013)** did a comparative study on the performance of Indian banks. They undertook public sector as well as private sector bank and found that new banks are more efficient than old banks and public sector banks are is showing less profitability as compared to a private sector bank.

**Dr.K.Srinivas and L.Saroja (2013)** conducted a comparative study to analyse the financial performance of HDFC Bank and ICICI bank. From the study it was concluded that both the banks are giving healthy competition to each other and are successful private sector banks. No major difference was found in their financial conditions, but HDFC still is better than ICICI bank as far as services is concerned. Deepti Tripathi and Kishore Meghani (2014) did a comparative study of the financial performance of Axis bank and Kotak Mahindra Bank. Hence it can be observed that, the study was done on private sector banks. Through CAMEL Model and t–test, it was also found that there is no major difference in the financial performance of both the bank. But it was seen that Axis Bank is performing better than Kotak Mahindra Bank.

**Gilbert and Charles (2014)** conducted study based on profitability, competence, liquidity, asset value, and risk measure and investor analysis model called as PELARI for analyzing the financial performance. It was found that the focus of ADB's is decreasing and it was noticed that the loans and advances for service sector was more as compared to agriculture sector which is 38% and 29 % respectively in 2012. It was also observed that bank liquidity is decreasing year by year and the Ghana banking survey (2011) confirmed that banks are illiquid.

**Ms. Rajni (Oct.2015),** compared the financial performance of the State Bank of India, PNB and Bank of Baroda using three sets of ratio, namely return on asset, total asset, operating efficiency ratio and also considered nonperforming assets. She concluded that SBI is more efficient in case of total assets, deposits and advances as compared to PNB and BOB.

### OBJECTIVES

(i) To analyse the concept of financial analysis.
(ii) To analyse the profitability position of the Allahabad Bank.
(iii) To analyse the Balance sheet position of the Allahabad Bank.

### RESEARCH METHODOLOGY

To achieve the required objectives, information's are collected through primary data like observation, direct interview, personal interview, group discussion & secondary data like budget, statistical report, annual report, financial statement, balance sheet profit & loss account and their schedules and also secondary data like field study.

All the information, which a collected through the annual report of Allahabad Bank and Interview of the employees of the concern, which will be relevant to the objectives so that the objectives can be easily fulfilled.

### 1. ANALYSIS OF RATIOS OF ALLAHABAD BANK

#### NET PROFIT RATIO (NPR)

**Overview:**

The Net Profit ratio is the most important ratio, which is considered while analyzing the financial statement. The ratio shows the relationship between the net profit after tax and net sales of the organization. The net profit after tax is divided by net sales to find out the net profit ratio. The calculation of Net Profit is done by deducting gross profit with operating expenses and income tax. The Net Profit Ratio is stated in terms of percentage. The ratio is also known as Net Profit Margin.

**Formula:**

$$\text{Net profit (NP) margin} = \frac{\text{Net profit after tax}}{\text{Net sales}} \times 100$$

**Table No. : 1**

**Statement of Net Profit to Net Sales**

**(In Rs. Crore)**

| Year | Net Profit (Rs.) | Net Sales (Rs.) | Ratio (%) |
|---|---|---|---|
| 2013–2014 | 1180.75 | 18775.60 | 6.28 |
| 2014–2015 | 1631.14 | 19749.06 | 3.30 |

**Interpretation:**

The Net Profit Ratio of the Allahabad Bank showed the decreasing trend in 2015 which was 3.2% as compared to the year ended 31st March 2014 which was 6.8%. It shows that bank needs to work on its policies so that efficient management takes place and cost is reduced and bank earn larger profit.

#### NET INTEREST MARGIN RATIO (NIM)

**Overview:**

Net Interest Margin is a ratio similar to Gross Profit Margin ratio considered in non– financial organization. It is calculated when Interest earned by the organization is subtracted by Interest expended and then it is divided by the total assets. It is presented in percentage format. The higher the ratio better is the investment strategy. On contrary, if the ratio is less, it will show that the investment is costing higher than its return. Through this ratio, it can analysed that whether the investments are really making money or not so that the interest expended can be vindicated or to decrease interest expense the company is paying off its debt.

**Formula:**

$$\text{Net Interest Margin} = \frac{\text{Investment Returns} - \text{Interest Expenses}}{\text{Average Earning Assets}} \times 100$$

**Table No.: 2**

**Statement of Net Interest Margin**

**(In Rs. Crore)**

| Year | Net Interest Income (Rs.) | Total Assets (Rs.) | Ratio (%) |
|---|---|---|---|
| 2013–2014 | 5341.04 | 220951.94 | 2.42 |
| 2014–2015 | 6211.72 | 227679.66 | 2.73 |

**Interpretation:**

From the above graph, it can be observed that the percentage of the Net Interest Margin has increased from 2.42% to 2.73% in 2015, which shows that the bank has experienced more demand for loan, mutual funds and trust.

#### OPERATING EXPENSE RATIO (OER)

**Overview:**

The Operating Expense Ratio is the ratio which calculates the amount which is required for the working of the organization in comparison to the income earned by it. The ratio is calculated in the percentage format by dividing operating expense with income generated. The ratio depicts the financial efficiency and efficiency of the management. Lower percentage is more profitable for the organization.

**Formula:**

$$\text{Operating Expense Ratio} = \frac{\text{Operating Expenses}}{\text{Total Income}} \times 100$$

**Table No.: 3**

**Statement of Operating Expense Ratio**

**(In Rs. Crore)**

| Year | Operating Expense (Rs.) | Total Income (Rs.) | Ratio (%) |
|---|---|---|---|
| 2013–2014 | 1239.20 | 21049.80 | 5.89 |
| 2014–2015 | 1431.47 | 21873.64 | 6.54 |

**Interpretation:**

It is observed that the Operating Expense Ratio has increased from as compared to previous i.e., from 5.89% to 6.54% which shows the unfavorable condition for the bank and also depicts that there is decrease in efficiency.

#### CURRENT ASSET TURNOVER RATIO

**Overview:**

The Current Assets Turnover Ratio shows that the current assets are transformed into sales. Higher the current asset turnover better is the ability of the business to achieve highest sales with lowest investment in current assets, which indicates that higher the current ratio better is the situation. It is calculated by dividing the net sales by its current assets. The value varies from business to business and from industry to industry and there is no normative value. However, if the current assets turnover is high as compared to its competitors, it would indicate that current assets in used at higher rate of intensity. It also indicated that the company is consistently improving its policies in cash, accounts receivable, inventory and further current assets.

**Formula:**

Current Asset Turnover Ratio = Annual Sales / Current Assets

**Table No. : 4 Statement of Current Asset Turnover Ratio:**

**(In Rs. Crore)**

| Year | Annual Sales(Rs.) | Current Assets (Rs.) | Times |
|---|---|---|---|
| 2013–2014 | 18775.60 | 17157.49 | 1.094 |
| 2014–2015 | 19749.06 | 19335.49 | 1.021 |

**Interpretation**

In the above graph, it can be observed the current asset turnover ratio has been a decrease in percentage from 1.094% in the year 2014 to 1.021% in the year 2015 which means that the organization has sold products with more investment in current assets

**CURRENT LIABILITIES TURNOVER RATIO**

**Overview:**

The ratio shows that the firm's capability to settle down its debt in the accounting period which is only possible when the organization works towards transforming efforts into sales. The ratio depicts the relationship involving sales and current liabilities. Higher the ratio better is the scenario of the organization in meeting its current liabilities.

**Formula:**

Current Liabilities Turnover Ratio = Annual Sales / Current Liabilities

**Table No. : 5**

**Statement of Current Liabilities Turnover Ratio:**

**(In Rs. Crore)**

| Year | Annual Sales(Rs.) | Current Liabilities (Rs.) | Times |
|---|---|---|---|
| 2013–2014 | 18775.60 | 5659.97 | 3.15 |
| 2014–2015 | 19749.06 | 6713.73 | 2.94 |

**Interpretation**

In the above graph, it can be observed the current liability turnover ratio has decreased from 3.15times to 2.94times which means that the organization need to use its current liabilities precisely so that it can settle all its debts in the same accounting period.

**FIXED ASSET TURNOVER RATIO**

**Overview:**

The fixed asset turnover ratio is a ratio which is used to measure the operating performance of the organization. The ratio is measured by dividing net sales with fixed assets. This ratio depicts the how much capable a company is to create net sales from fixed assets, for example property, equipment, and plant. Greater the ratio better is the situation as it shows that the investments in fixed assets are utilized more effectively, so that revenue can be generated.

**Formula:**

Fixed Assets Turnover Ratio = Annual Sales / Fixed Assets

**Table No. : 6**

**Statement of Fixed Assets Turnover Ratio:**

**(In Rs. Crore)**

| Year | Annual Sales(Rs.) | Fixed Assets (Rs.) | Times |
|---|---|---|---|
| 2013–2014 | 18775.60 | 1316.33 | 14.29 |
| 2014–2015 | 19749.06 | 1413.33 | 13.97 |

**Interpretation**

In the above graph, it can be observed that the fixed assets turnover ratio has decreased from 14.297 times to 13.97 times from 2014 to 2015 which means there is an overinvestment in fixed assets and the investments on fixed assets incapable of transforming into sales.

**CONCLUSION**

The main purpose of the research paper was to understand the concept of financial analysis through a thorough analysis of income statement, balance sheet, cash flow statement and working capital.

- The bank earned interest 5.18% more than the previous year which illustrates that the operational activity is on pleasant track.
- The net profit ratio of the bank decreased from 6.8% in the year 2014 to 3.2% in 2015 showing that bank needs to work on its policies so that efficient management takes place and cost are reduced and bank earn a larger profit.
- A decline in net interest margin was also found which shows that the bank has experienced more demand for loan, mutual funds, and trust.
- An increase in operating expense ratio shows the unfavorable condition for the bank and also depicts that there is a decrease in efficiency.
- The roce has shown an increasing trend due to increase in earnings before interest and tax in the bank which means that the investments of the shareholders are efficiently utilized by the management.
- The cash and cash equivalent of the bank have increased by 36.49% in case of balances with banks money at call and short notice and 9.35% increase was observed in the case of cash balances with rbi.
- It was found that the bank is selling products by investing more in current assets which are ultimately leading to decrease in the percentage of ratio to 1.021% in the current year that i.e. 2015.
- The current liability turnover ratio indicated that there is a decrease in the ratio which means that the bank needs to use its current liabilities precisely so that it can settle all its debts in the same accounting period.
- An overinvestment in fixed asset is observed. Moreover, it is also found that the investment done on fixed assets are incapable of transforming into sales.

**Suggestions**

- For upgrading the financial performance, enlisted below are few suggestions for the analysis done:
- Being a Public Sector Bank, it is important to develop the motivational powers within the customer by providing the assurance that products and working of the bank is customer friendly.
- There is a need to enhance the momentum and competency of delivery services which is a need for any retail business like banking.

- It is necessary for the bank to develop the quality of delivery services which is related to accuracy of accounts management of customer also it is important for the bank to develop a cordial relationship with their customer.

- It is also important that the bank focus upon building confidence of its customer which will help to multiply the credit facilities also it will help to increase the investment advisory services for their valuable customer.

- To develop confidence within the customer the bank need to accept that customer is the king of the market and treat them like that.

- An old public sector bank like allahabad bank need to accept the ongoing changes in the india banking sector and face the challenges to maintain their share in the market.

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