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Analysis of Financial Performance of Non-Banking Financial Companies in India

KEYWORDS: NBFC, profitability, liquidity, leverage, Interest Coverage, Risk Indicator ratios

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ABSTRACT *The Non-Banking Financial Companies (NBFCs) have been considered as the one of the segments of the Indian financial system. In the 1980's this sector had a mushrooming of institutions and the profile of the industry has undergone many changes over the years. NBFCs are successful in rendering a wide range of services. Initially intended to cater to the needs of savers and investors, NBFCs later on developed into institutions that can provide services similar to bank. In this paper an attempt has been made to empirically analyse the performance of the NBFCs (Auto financing and Other Asset financing) in India across the period of 2007-2012. This study examines the profitability, efficiency and turnover aspects of the selected NBFCs. The findings indicate that the NBFCs differ significantly in terms of Profitability and Leverage indicators from one another.*

INTRODUCTION

The NBFCs flourished in India in decade of 1980s against the back drop of highly regulated banking sector. Beginning from 1997 the implementation of prudential norms and the strict supervision by the RBI has led to the orderly growth of the firms in this sector. Capital adequacy norms and assets classification norms which applied to banks are also made applicable to NBFCs. A performance review of NBFCs indicates that a number of NBFCs has come down gradually over the years. In the perspective of changed regulatory structure of NBFCs, it is pertinent to undertake a research study of the overall performance of select NBFCs.

NBFCs form a broad category of financial institutions other than commercial banks. NFBCs operate largely in vehicle financing, hire purchase, lease, personal loans, working capital loans, consumer loans, housing loans, loans against shares, investments, distribution of financial products, etc. In India considerable growth has taken place in the Non-banking financial sector in last two decades. Over the years, NBFCs have become a crucial part of the Indian financial system and they form around 11% of the assets of the total financial system. NBFCs have emerged as an important intermediary for financing and have provided strong competition to banks and financial institutions.

REVIEW OF LITERATURE

A brief summary of the previous research works relating to NBFCs are presented here.

Subramanian and Papola (1979) studied the influences of financial policy variables, assuming that profitability is major determinant of growth. The study has been made from a sample of 27 companies quoted in the stock exchange in India chemical industry during the period 1960-1969. The authors have observed that is a strong positive relationship between profitability and growth in the chemical industry. Kantwala (1997) analysed the performance of NBFCs in India. He has found a significant difference in the profitability ratio, leverage ratio, liquidity ratio of various categories of NBFCs in India during the year 1985-1995. Topy (2008) analysed the financial performance of Nigerian quoted manufacturing companies. He has found a statistically significant relationship between measure of liquidity and selected measure of profitability, efficiency and indebtedness in Nigerian quoted manufacturing companies. The impact of one percent increase in average liquidity measure produced a more significant increase in average profitability (21.9%) efficiency (16.1%) and ineptness' (16.6%). Singh and Ramniwas (2011) studied the growth and financial performance of the NBFCs in India. They have concluded that the NBFCs segment of finance was less regulated over a period of time. Vadde (2011) analysed the performance of NBFCs in India during the year 2008-2009 they have found a significant decrease in the operating profit along with diminishing profitability during 2008-2009. Paul (2011) analysed the financial performance of the selected NBFCs during the period 2004 to 2009. In his study five listed NBFCs have been taken as a sample for analysing the financial performance of the NBFCs. He concluded that the selected companies are significantly different in terms of their financial performance from one another.

Based on the studies discussed here, the present study attempts to analyses the financial performance of the NBFCs in India.

OBJECTIVE OF THE STUDY

In India considerable growth has taken place in the Non-banking financial sector in last two decades. Since the activities of NBFCs have undergone the qualitative change in the recent years, there is a need to look at the salient issues like liquidity, profitability, interest margins etc. This study analyses the performance of the NBFCs (Auto financing and Other Asset financing) during the year 2007-2012. The primary objective of the study is to evaluate the overall financial performance of NBFCs.

METHODOLOGY

For the purpose of this study the data relating to NBFCs were collected from the "PROWESS" database of from centre for monitoring Indian economy (CMIE) and "CAPITALINE" database. The study covers a period of six financial years starting from 2007 to 2012. Out of 14 NBFCs (Auto financing and Other Asset financing) listed in National Stock Exchange [NSE], 4 companies were excluded

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because of non-availability of data in the "PROWESS" database. The final sample consisted of 10 companies.

TOOLS USED FOR ANALYSIS OF DATA

For the purpose of analysis of data, different statistical tools like arithmetic mean, standard deviation, and ANOVA were used. Financial ratios were used in the study to examine the profitability, efficiency and turnover aspects. The selected financial ratios were divided into 4 broad groups: viz. Profitability ratios, Leverage ratios, Liquidity ratio, Interest Coverage Ratio and Indicator ratios

HYPOTHESIS

The following hypothesis has been framed to test the differences in the ratios between the NBFCs during the study period

H0- There is no significant difference between the selected NBFCs in terms of selected Profitability Ratio, Leverage Ratio, Liquidity Ratio, Interest Coverage Ratio and the Risk Indicator Ratio

FINDINGS

The average ratios of various categories of NBFC's are presented in Table: 1

Table: 1 Average Ratios of NBFC's

Ratios	MEAN	S.D
Profitability Ratios		
Gross Profit / Total Income	27	11
Profit Before Tax / Total Income	25	11
Net Profit / Total Income	17	8
Return on Net Worth	17	8
Total Income / Total Assets	17	4
Return on Assets	3	2
Return On Capital Employed	13	4
Return on Equity	3	2
Earnings Per Share	26	21
Price Earnings Ratio	15	12
Leverage Ratios		
Borrowings To Total Assets	81	10
Bank Borrowings to Total Assets	43	14
Networth to Total Assets	18	8
Bank Borrowings to Borrowings	53	17
Debt-Equity Ratio	5	2
Long-term Debt Equity Ratio	4	2
Interest Coverage Ratio	2	1
Liquidity Ratio		
Current Ratio	4.24	2.82
Risk Indicator Ratios		
Equity Multiplier Ratio	124.5	78.9
Equity Ratio	1.25	1.237

Sources : Computed

From Table-1, it reveals that the Overall average of Return on Net worth and Return on Capital Employed, Earnings Per share and Price Earnings Ratios shows a better Profitability Position of the NBFCs. The average Current ratio of NBFCs is 4.24. The Current Ratio of the NBFCs shows an increasing trend. NBFCs have good solvency as they have the current ratio of more than the 2:1 the standard yardstick. The Interest Coverage Ratio is low for the NBFCs. It shows the capacity to service the additional debts are low for the NBFCs. The average ratio of Debt Equity is 5 and for the Long-term Debt Equity are 4. The NBFCs has employed Long-term debts to the extent of 4 to 5 times that of Shareholder funds.

Table-2 One Way ANOVA results of various ratios among NBFC's

Sources of variation	Sum of Squares	df	Mean Square	F	Sig.
Gross Profit to Total Income					
Between Groups	0.481	9	0.053	**9.022***	.000
Within Groups	0.296	50	0.006		
Profit Before Taxes to Total Income					
Between Groups	0.449	9	0.050	**8.436***	.000
Within Groups	0.296	50	0.006		
Net Profit to Total Income					
Between Groups	0.205	9	0.023	**8.731***	.000
Within Groups	0.130	50	0.003		
Return on Networth					
Between Groups	0.193	9	0.021	**5.430***	.000
Within Groups	0.197	50	0.004		
Total Income to Total Assets					
Between Groups	0.065	9	0.007	**6.826***	.000
Within Groups	0.053	50	0.001		
Return on Assets					
Between Groups	0.010	9	0.001	**9.275***	.000
Within Groups	0.006	50	0.000		
Return on Capital Employed					
Between Groups	587.45	9	65.27	**20.705***	.000
Within Groups	157.62	50	3.15		
Return on Equity					
Between Groups	155.75	9	17.30	**4.111***	.001
Within Groups	210.50	50	4.210		
Earnings Per Share					
Between Groups	10980.34	9	1220.03	**4.150***	.000
Within Groups	14699.35	50	293.98		
Price Earnings Ratio					
Between Groups	2322.80	9	258.08	1.896	.074
Within Groups	6805.52	50	136.11		
Borrowings to Total Assets					
Between Groups	0.299	9	0.033	**4.900***	.000
Within Groups	0.339	50	0.007		
Bank Borrowings to Total Assets					
Between Groups	0.433	9	0.048	**3.167***	.004
Within Groups	0.759	50	0.015		
Networth to Total Assets					
Between Groups	0.250	9	0.028	**8.976***	.000
Within Groups	0.155	50	0.003		
Bank Borrowings to Borrowings					
Between Groups	0.616	9	0.068	**3.124***	.005
Within Groups	1.095	50	0.022		
Debt-Equity Ratio					
Between Groups	165.75	9	18.41	**15.411***	.000
Within Groups	59.75	50	1.19		
Long-term debt equity ratio					
Between Groups	122.45	9	13.60	**9.737***	.000
Within Groups	69.86	50	1.39		
Interest Coverage Ratio					
Between Groups	8.38	9	0.932	**4.565***	.000
Within Groups	10.20	50	0.204		
Current Ratio					
Between Groups	105.88	9	11.76	1.622	.135
Within Groups	362.69	50	7.25		
Equity Multiplier Ratio					
Between Groups	186414.78	9	20712.75	**5.725***	.000
Within Groups	180886.11	50	3617.72		

Sources : Computed

The ANOVA result given in table-2 reveals that the Price Earnings Ratio ($F= 1.896$, $p > 0.05$) and the Current Ratio ($F=1.622$, $p > 0.05$) between the selected NBFCs are not

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statistically significant at 0.05 level of significance. It shows that the Price Earnings Ratio and the Current Ratio have same composition for the NBFCs. It shows that the NBFCs are following the standard yardstick 2:1 for the Current Ratio. Hence, the null hypothesis that there is no significant difference among the selected NBFCs is rejected in terms of Price Earnings Ratio and the Current Ratio and accepted for all other ratios. This indicates that the selected NBFCs differ significantly in terms of Profitability and Leverage indicators from one another. This result is consistent with the findings of Kantwala (1997), and Paul (2011)

CONCLUSION

On the basis of the study, it can be concluded that there exists a significant difference in the profitability ratios, leverage ratios, liquidity ratios and risk indicator ratios of selected NBFCs. When all companies are taken together the significant difference does not exist for only two ratios i.e. Price Earning Ratio and Current Ratio. The ratios for all the selected NBFCs are differing significantly from one another. From this it is observed that the ratios of NBFCs are generally different from each other. The analysis of variance along with details about average ratios may become a useful guide to the NBFCs in their financial decisions making.

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