Journal of Business Administration and Education
ISSN 2201-2958
Volume 1 (2012), Number 1, 1-14

# A Comparison of Financial Performance in the Banking Sector: Some Evidence from Pakistani Commercial Banks

**Faisal Abbas (Corresponding author)**
*Imperial college of business studies Lahore, Pakistan*
**Muhammad Tahir**
*Imperial college of business studies Lahore, Pakistan*
**Mutee-ur-Rahman**
*Lecturer University of Sargodha, Sargodha, Pakistan*

## Abstract

The purpose of this study is to check the financial performance of the commercial banks of Pakistan by covering the period of five years from 2007 to 2011. The reasons for choosing this period is repaid growth of the banking sector of Pakistan and revolutionary change in financial performance of banks. There are more than twenty scheduled banks in Pakistan and out of those we have selected top five scheduled banks on the basis of their networks consist of more than 4000 branches. There are so many past studies in which the researchers used different financial ratio to check the financial performance of the Commercial banks such like Return on assets (ROA), Return on Equity (ROE), Return on Capital (ROC) and by using some other operating and efficiency ratios. But in this study, we used another indicator for assessment of financial performance that is Return on Operating Fixed Assets (ROFA). Return on Fixed Assets indicates that how the banks are using their Operating Fixed Assets and what is the contribution of the Operating Fixed Assets in the performance of the banks. This study shows that banks having more Total Assets, Total equity and Total operating fixed assets have better financial performance or not. Its does not means that the banks having higher total assets, higher total operating

fixed assets and higher equity have better performance.

## **Introduction:**

Banking in Pakistan is carried on as per the banking Companies Ordinance 1962. In Pakistan the whole banking sector is managed and controlled by State Bank of Pakistan which is also called Central Bank of Pakistan. Banks are called financial institutes and they are performing financial activities. The central bank of Pakistan also regulates the different issues of the Commercial banks. The Central Bank formulates and regulates the monetary policy to control the inflation and deflation in the country. It also provides clearing house facility to all the scheduled banks of the country. Banks basically perform depositing and lending operations in an economy. The stable banking sector is the basic need of the every economy. There are more than twenty schedule banks and all of these are busy now a day to contribute their share in development of the economy. In order to achieve the financial resource businessmen need help to promote their business activities which are difficult to tackle but it can become easy to mange with the help of commercial banks. In every sector of the country, finance is the basic requirement and that is the main source for promoting the business. In Pakistan almost all types of banks are doing working. Now a day banks are not only confined to perform services within the geographical limits but globally. These banks are almost performing all types of services such as like providing different types of loans such as Cash Credit, Bank Overdraft facility, ATM Card facility, Running finance facility, fixed deposit facility, Profit and loss saving account facility, funds transferring facility, Car loans facility and housing finance etc. The banks normally earn profit from lending of money. There are different parameters from which we can evaluate the financial performance of the banks. The financial performance of the banks can be checked through analysis of the different indicators such like total assets, total shareholder equity by comparing with profit of the banks. The profitability indicates the financial performance of the banks. The bank having high profit rate is performing well.

**The Literature Review:**

The concept of financial performance of the banks based on the financial ratio is applied by different researcher and the following is the summary of past studies and their results about the performance of the banks. In his study, (Tarawneh, 2006) divided the commercial banks in Oman in cohesive categories depending on their financial characteristics revealed by financial ratios. Using simple regression analysis, the following were determined: the effect of asset management, operational efficiency, and bank size on the financial performance of five Omani commercial banks with more than 20 branches. The results indicated that bank with higher total capital, deposits, credits, or total assets do not always represent a better profitability performance.(Al-Tamimi, 2009) determined some significant factors influencing performance of the UAE Islamic and Conventional National banks from 1996-2008. Using regression analysis, specifically ROE and ROA as dependent Variable, the researcher concluded that liquidity and concentration were the most significant determinants of conventional national banks. Conversely, number of branches and cost were the most influential factors of Islamic banks' performance.In his research, (Sufian, 2009) investigated the determinants of banks profitability in a developing economy, case study Malaysian Financial sector during the period 2000-2004. The results showed that higher credit risk and higher loan concentration Malaysian banks face lower profitability level. On the contrary, Malaysian banks with higher level of capitalization, higher income from non-interest sources, and higher operational expenses face higher profitability level.(Okpara, 2009) determined the major factors that influence the banking system in Nigeria. Using factor analysis techniques, the author concluded that undue interference from board members, political crises, Undercapitalization, and fraudulent practices are considered the most critical factors that impact the performance of banking system in Negeria.Simply stated, much of the current bank performance literature describes the objective of financial organizations as that of earning acceptable returns and minimizing the risk taken to earn this return (Hempel G.Coleman, 1986). There is a generally accepted relationship between risk and return, that is, the higher the risk the higher the expected return. Therefore, traditional measures of bank performance has measured both risks and returns.(Spathis, and Doumpos, 2002) Investigated the effectiveness of Greek banks based their assets size. They used in their study a multi criteria methodology to classify Greek banks according to the return and operation factors, and to show the differences of the bank's profitability and efficiency between small and large banks. (Elizabeth Duncan, and Elliott, 2004) showed that all financial performance measures as interest margin, return on assets, and capital adequacy are positively correlated with customer service quality scores. In a study conducted in Kuwait (Edris, 1997) to determine the importance of selection factors used by Kuwait business consumers in choosing domestic and foreign banks. Findings of this study show that the highest ranking determinant factors of selection a bank in Kuwait by business firms were size of bank assets, personnel efficiency, banking experience, friendliness of staff, reputation, and availability of branches abroad. Miller and Noulas (1997) Observed the factors that affected the profitability of the banks in USA for the period of 1985 to 1990 in which the size of the banks was found to be a negatively related with profitability. The negative relationship of the size indicates the diseconomies of scale. Kosmidou (2008) stated the significant relationship of size and capital adequacy ratio, while the size is positively related with performance measures. Chirwa (2003) examine the negative relationship of capital to assets ratio with return on capital discus in previous studies. (Rangan and Grabowski, 1988) use data envelopment analysis to analyze technical efficiency in US banking into pure technical and scale efficiency. Ghulam Ali Bhatti & Haroon Hussain(2010) Examine the relationship between market structure and performance in the banking sector using data from Pakistani commercial banks by using regression analysis, they have found a positive relationship of concentration ratio(CR) with profitability. Ali, Akhtar and Ahmed (2011) reported the significant role of capital adequacy ratio, operating efficiency, asset management and GDP that are influencing the profitability of commercial banks in Pakistan while the impact on bank-specific and macro-economic factors on profitability. (Arzu Tektas, and Gunay, 2005) discussed the asset and liability management in financial crisis. They argued that an efficient asset-liability management requires maximizing banks profit as well as controlling and lowering various risks, and their study showed how shifts in market perceptions can create trouble during crisis.

**Study Methodology:**

Generally, most of the past studies made on financial performance of commercial banks based on different financial variables such like Return on Assets (ROA), Return on Equity (ROE) and Return on Capital (ROC) and this research is made for the same purpose. There are almost more than twenty scheduled banks in Pakistan with wide network of branches. But for particular study of financial performance comparison, only five top banks are selected and the additional dependant variable Return on Operating Fixed Assets is used. Financial performance is the dependent variable, and measured by Return on Asset (ROA), Return on Equity (ROE), Return on Operating Fixed Assets (ROFA), Growth and Average of the Assets and Equity.

**Data Collection:**

Data was collected from secondary means such like from the annual reports of the banks by analyzing the consolidated balance sheets and profit and loss accounts of the banks for five years 2007 to 2011. In addition, another source of data was from Journal of The Institute of Bankers Pakistan, through references to the library and the review of different articles, papers, and relevant past studies.

**Objectives of the study:**

The prime Objective of the study was to analyze the financial performance of the commercial banks of Pakistan for the period of five years from 2007 to 2011 by using financial ratios. The second Objective of this study was to analyze that how the banks were using their assets for their achievements.

**Sampling Design:**

The sample for this study was all branches of top five commercial banks of

Pakistan. The banking sector of the Pakistan is one of the major service sectors in Pakistan. There are different categories of banks in Pakistan but we have selected Commercial banks for this study.

## Hypothesis:

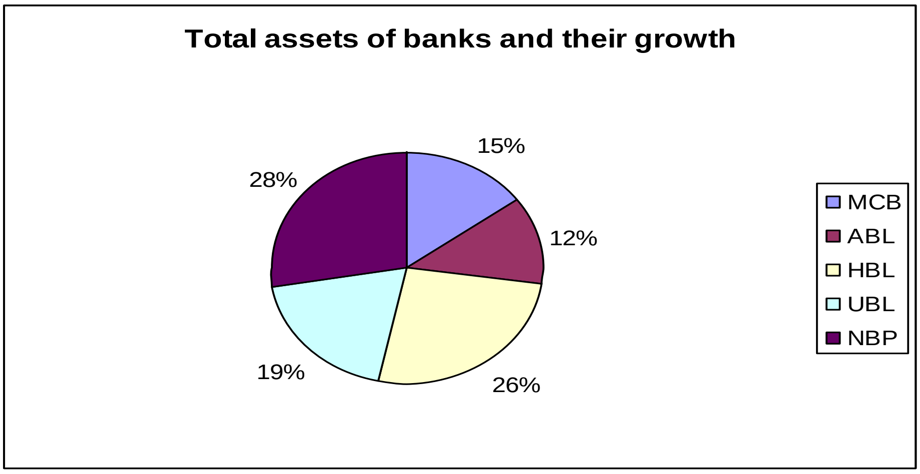
- The banks having higher average of total assets, higher average of operating fixed assets and higher average of total equity have higher growth rate
- The banks having higher total assets, higher operating fixed assets and higher total equity have higher returns

## Results and Discussion

**Table 1: Total assets of the banks and their growth (Values in millions)**

| years / Banks | *2007* | *2008* | *2009* | *2010* | *2011* | *Growth Rate* | *Average* |
|---|---|---|---|---|---|---|---|
| **MCB** | 410486 | 443616 | 509224 | 567553 | 653233 | 59.136487 | 516822.4 |
| **ABL** | 320109 | 366695 | 418374 | 449931 | 515699 | 61.1010625 | 414161.6 |
| **HBL** | 691991 | 749806 | 863778 | 924699 | 1139554 | 64.6775753 | 873965.6 |
| **UBL** | 546796 | 620707 | 640450 | 725390 | 753617 | 37.8241611 | 657392 |
| **NBP** | 764609 | 817758 | 944233 | 1038018 | 1153480 | 50.858805 | 943619.6 |

Source: (Compiled from audited financial statements of banks for 2007-2011)

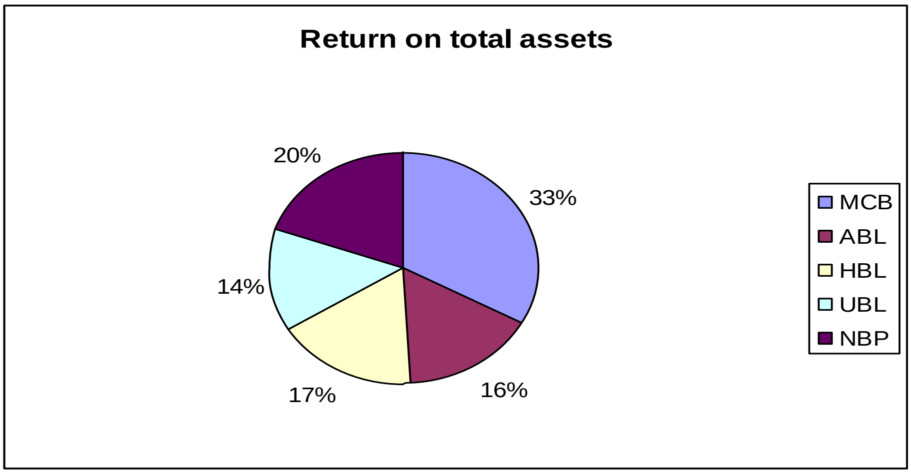



The growth of the banks is calculated on by taking the 2007 as a base year. By assigning the ranks to the banks on the basis of average total assets is as under; The average total assets of NBP is at number one, HBL is at number two, UBL is at number three, MCB is at number four and ABL is at number five. One of the important factors is that all the banks have positive growth rate. By testing the first hypotheses, banks having higher average of total assets were not found to be having higher growth rate because, the NBP having higher average of total assets but not having higher growth rate. On the other hand UBL having third highest average of total assets but the growth rate of UBL is lowest among all the banks.

**Table 2: RETURN ON TOTAL ASSETS (Values in millions)**

| years / Banks | *2007* | *2008* | *2009* | *2010* | *2011* | *Average* |
|---|---|---|---|---|---|---|
| **MCB** | 3.719006 | 3.465835 | 3.042865 | 2.972938 | 2.973671 | 3.23486319 |
| **ABL** | 1.273316 | 1.133367 | 1.702305 | 1.82828 | 1.966263 | 1.5807063 |
| **HBL** | 1.457244 | 1.448908 | 1.551325 | 1.842113 | 1.959802 | 1.65187836 |
| **UBL** | 1.689299 | 1.360545 | 1.481458 | 1.090034 | 1.406417 | 1.4055506 |
| **NBP** | 2.537898 | 1.89029 | 1.928761 | 1.708834 | 1.535267 | 1.92021014 |

Source: (Compiled from audited financial statements of banks for 2007-2011)

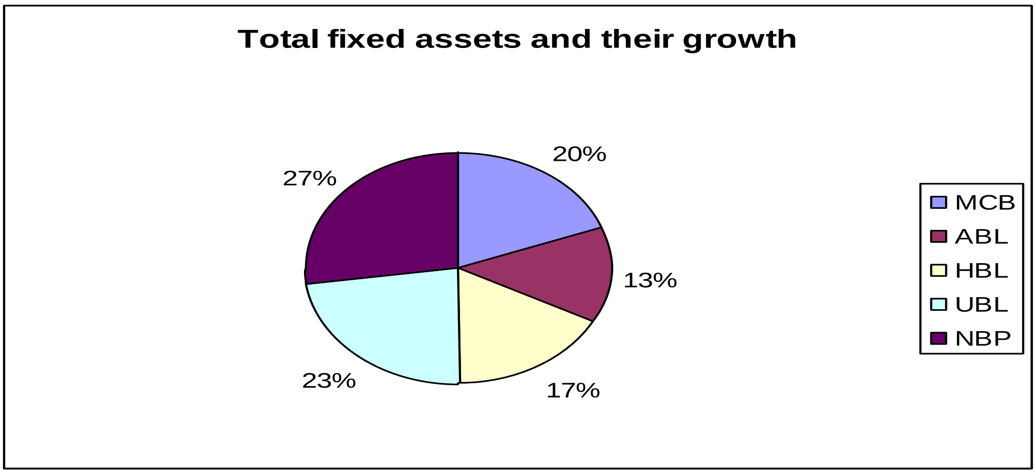



As above, the return on assets ratios are given for the period of 2007-11 for each selected commercial bank of Pakistan. The ranks of banks on the basis of ratios, MCB is number one with average of 3.23%, NBP is at number two, HBL is at number three, ABL is at number four with 1.58% and UBL is at number five with average return rate 1.4%.By testing the second hypothesis, MCB having the higher rate of return on total assets without having the higher average of total assets so this hypothesis is rejected. We can make our senses clear by observing the return of NBP which have highest average of total assets without having the highest return rate on total assets.

**Table 3: TOTAL FIXED ASSETS AND THEIR GROWTH (Values in millions)**

| years / Banks | *2007* | *2008* | *2009* | *2010* | *2011* | *Growth Rate* | *Average* |
|---|---|---|---|---|---|---|---|
| **MCB** | 16024 | 17264 | 18015 | 20947 | 22008 | 37.343984 | 18851.6 |
| **ABL** | 7549 | 11134 | 12447 | 15360 | 18087 | 139.594648 | 12915.4 |
| **HBL** | 13780 | 14751 | 16766 | 16155 | 19168 | 39.1001451 | 16124 |
| **UBL** | 19040 | 19927 | 23734 | 24685 | 24958 | 31.0819328 | 22468.8 |
| **NBP** | 25979 | 24218 | 25147 | 27621 | 28127 | 8.26821664 | 26218.4 |

Source: (Compiled from audited financial statements of banks for 2007-2011)

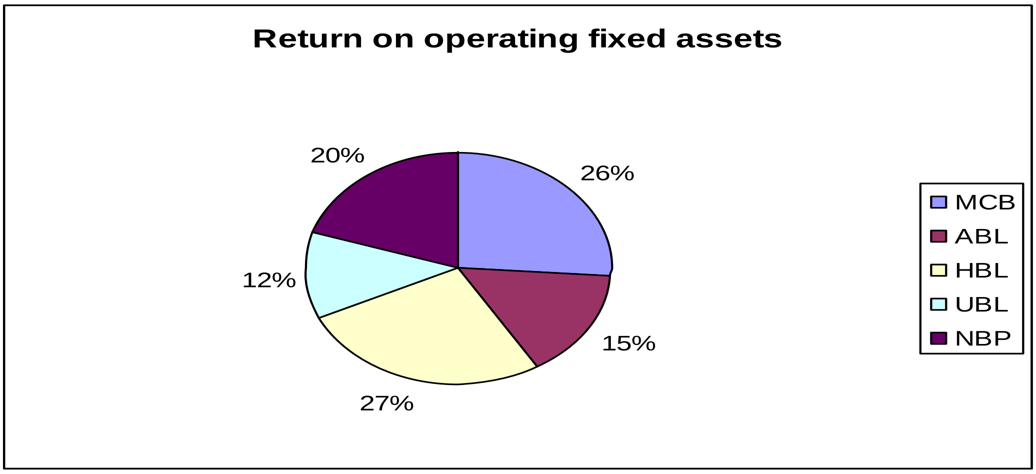



The growth of banks is calculated on by taking 2007 as a base year with comparison of 2011. By assigning the ranks of the banks on the basis of average total operating fixed assets is as under; NBP is at number one with Rs. 26218.4 million, UCB is at number two with average of Rs.22468.8 million, MBL is at number three with average of Rs. 18851.6 million, HBL is at number four with Rs. 16124 million and ABL is at number five. By testing the first hypothesis, the NBP having higher average of total operating fixed assets is having lowest growth rate so that why this hypotheses is also rejected. We can make our senses more clearly by taking the example of ABL which have lowest average of total operating fixed assets with highest growth rate among all the banks.

**Table 4: RETURN ON OPERATING FIXED ASSETS (Values in millions)**

| years / Banks | *2007* | *2008* | *2009* | *2010* | *2011* | *Average* |
|---|---|---|---|---|---|---|
| **MCB** | 95.2696 | 89.05816 | 86.01166 | 80.55091 | 88.26336 | 87.8307362 |
| **ABL** | 53.99391 | 37.32711 | 57.21861 | 53.55469 | 56.06237 | 51.6313345 |
| **HBL** | 73.17852 | 73.64924 | 79.92366 | 105.441 | 116.5119 | 89.7408707 |
| **UBL** | 48.51366 | 42.37969 | 39.97641 | 32.0316 | 42.46735 | 41.073742 |
| **NBP** | 74.69495 | 63.82856 | 72.42216 | 64.21925 | 62.96086 | 67.6251541 |

Source: (Compiled from audited financial statements of banks for 2007-2011)

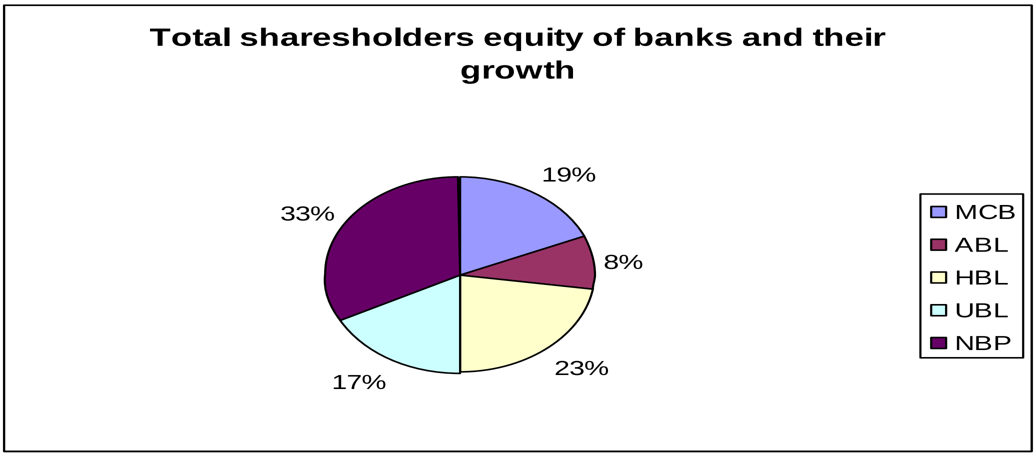



By testing the second hypothesis on return of operating fixed assets, HBL is at top but not having the highest average of operating fixed assets. On the other hand, NBP having the high average of operating fixed assets but not having the highest rate of return. ABL have the lowest average of operating fixed assets but not the rate of return on operating fixed assets.

**Table 5: TOTAL SHAREHOLDER'S EQUITY AND THEIR GROWTH (Values in millions)**

| years / Banks | *2007* | *2008* | *2009* | *2010* | *2011* | *Growth Rate* | *Average* |
|---|---|---|---|---|---|---|---|
| **MCB** | 55120 | 58436 | 69740 | 79204 | 88802 | 61.1066763 | 70260.4 |
| **ABL** | 19878 | 22356 | 29960 | 35975 | 43340 | 118.029983 | 30301.8 |
| **HBL** | 63237 | 66308 | 84369 | 96250 | 108351 | 71.3411452 | 83703 |
| **UBL** | 47891 | 49396 | 67318 | 75134 | 81129 | 69.403437 | 64173.6 |
| **NBP** | 117914 | 102459 | 119556 | 131999 | 135794 | 15.1635938 | 121544.4 |

Source: (Compiled from audited financial statements of banks for 2007-2011)

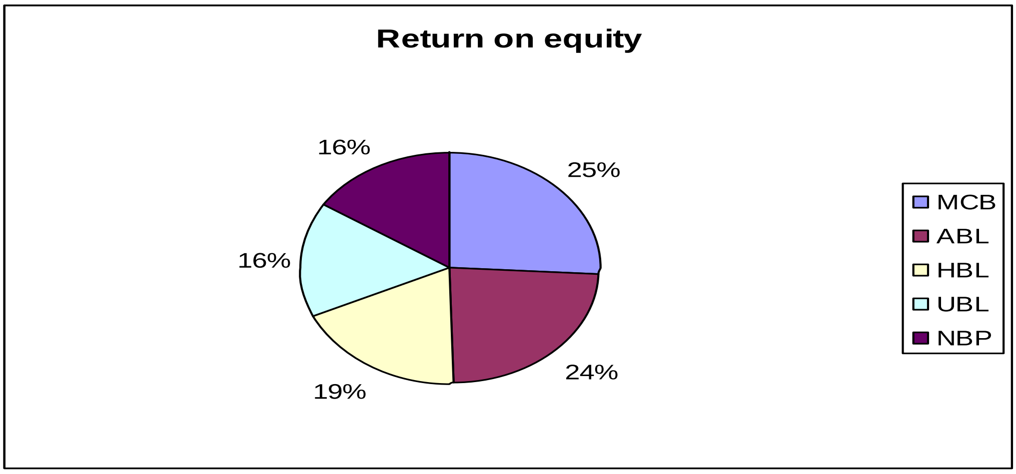



According to table 5 the average of equity for rank purpose is as under; NBP is at number one with highest average of equity 121544.4 million, HBL is at number two, MCB is at number three, UBL is at number four and ABL is at number five. By testing the first hypothesis, NBP is having highest average of total equity but having the lowest growth rate. On the other hand, UBL is having exceptionally highest growth rate but not having the highest average of total equity.

**Table 6: RETURN ON EQUITY (Values in millions)**

| years / Banks | *2007* | *2008* | *2009* | *2010* | *2011* | *Average* |
|---|---|---|---|---|---|---|
| **MCB** | 27.69594 | 26.31084 | 22.21824 | 21.30322 | 21.87451 | 23.8805471 |
| **ABL** | 20.50508 | 18.59009 | 23.7717 | 22.86588 | 23.3964 | 21.8258288 |
| **HBL** | 15.94636 | 16.38415 | 15.88261 | 17.69766 | 20.61172 | 17.3044992 |
| **UBL** | 19.28755 | 17.09653 | 14.0943 | 10.52386 | 13.06438 | 14.813324 |
| **NBP** | 16.45691 | 15.08701 | 15.23303 | 13.43798 | 13.04108 | 14.6512012 |

Source: (Compiled from audited financial statements of banks for 2007-2011)




By testing the second hypothesis, the return on equity of MCB is higher than all other banks, but not having the higher average of equity. On the other hand, NBP has higher average equity but the lowest rate of return on equity.

**Table 7: Ranks of Pakistani Commercial Banks based on Financial Performance**

| **Banks Indicator** | **NBP** | **MCB** | **HBL** | **UBL** | **ABL** |
|---|---|---|---|---|---|
| **Average Total Assets** | **1** | **4** | **2** | **3** | **5** |
| **ROA** | **2** | **1** | **3** | **5** | **4** |
| **Average Operating Fixed Assets** | **1** | **3** | **4** | **2** | **5** |
| **Return on Fixed Assets** | **3** | **2** | **1** | **5** | **4** |

| | | | | | |
|---|---|---|---|---|---|
| **Average Total Equity** | **1** | **3** | **2** | **4** | **5** |
| **ROE** | **5** | **1** | **3** | **4** | **2** |

## Conclusion:

The main idea of this study is to observe that whether the banks are using their assets and equity according to their investment or not. The findings of this study shows that the ranking of top five Pakistani commercial banks based on their total average assets, total operating fixed assets, total average equity and return on the respective variable. According to ranking, NBP is at number one, MCB is at second, HBL is at third, UBL is at fourth and ABL is at fifth number. The bank getting first rank frequently are considered top performer. Following this phenomenon, MCB is 2nd and HBL is 3rd. These results are according to the present situation of the market and matched with the situation in industry. Finally, this paper provides information to bank managers that how they can make their resources productive for the improvement of financial performance.This study is an important contribution in order to meet up the gap of financial performance literature. The finding of the present study can be used for further studies about financial performance. It is also useful for bank organizers, managers, financial analysists and decision makers to focus on the area which is not contributing towards the financial performance. This study is also providing the information for decision makers to put their efforts on those resources which can improve the financial performance.

## References

[1] Tarawneh, M, (2006),"A Comparison of Financial Performance in the Banking Sector: Some Evidence from Omani Commercial Banks", International Research Journal of Finance and Economics, Issue.3.

[2] Al-Tamimi, H, (2010),"Factors Influencing Performance of the UAE Islamic and Conventional National Banks", Global Journal of Business Research, vol. 4, no. 2,

pp.1-9

[3] Sufian, F, (2009), "Factors Influencing Bank Profitability In Developing Economy: Empirical Evidence from Malaysia" , Global Business Review, vol.10,No.2, pp.225-241.

[4] Okpara, G, (2009), "A Synthesis of the Critical Factors Affecting performance of the Nigerian Banking System", European Journal of Economics, Finance and Administrative Sciences, issue.

[5] Hempel G., Coleman, A., and Smon, D.(1986), Bank Management text and cases, Wiley, New York.

[6] Spathis, K., and Doumpos M., (2002), "assessing profitability factors in the Greek banking system: A multi criteria methodology" International transcation in Operational Research, Vol. 9, Sept.Issue, p.517

[7] Elizabeth D., Greg Elliot (2004), "Efficiency, customer service and financial performance among Australian financial institutions", International Journal of Bank Marketing, Vol.22, No.5, pp.319-342.

[8] Thabet A., Edris (1997), "Services considered important to business customer and determinants of banks selection in Kuwait: A segmentation analysis. International Journal of Bank marketing, Vol.15, No.4, pp. 126-133.

[9] Miller, S.M., & Noulas, A.G. (1997). Portfolio mix and large-bank profitability in the USA. Applied Economics, 24(4), 505---512

[10] Kosmidou, K (2008). The determinants of banks profit in Greece During the period of EU Financial integration. Managerial Finance, 34(3), 146-159.

[11] Chirwa, E.W. (2003). Determinants of commercial banks in Malawi: a cointergration approach. Applied Financial Economics, 13, 565-571

[12] Rangan, N., Grabowski, R. (1988), "The technical efficiency of Us Bnaks", Economic Letters, 28, pp. 169-175.

[13] Ghulam Ali Bhati & Haroon Hussain (2010), "Evidence on Structure conduct Performance Hypothesis in Pakistani Commerical Banks", International Journal of Business and Management.

[14] Ali, K., Akhtar, M.F., and Ahmed, H.Z. (2011). Bank-Specific and Macroeconomic

indicators of Profitability – Empirical Evidence from the commercial Banks of Pakistan. “International Journal of business and Social Science”, 2(6), 235-242.

[15] Arzu Tektas, and Gokhan Gunay,(2005), “Asset and Liability management in financial crisis” The Journal of Risk Finance, Vol. 6, No. 2, pp.135-149.