COMPARATIVE PERFORMANCE ANALYSIS OF PUBLIC OWNED AND PRIVATE OWNED COMMERCIAL BANKS IN Ethiopia

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ABSTRACT

The main objective of this paper is to evaluate the performance of public owned and private owned commercial banks in Ethiopia from the period 2001 to 2013. Secondary data which is collected from the annual reports of two public owned and six private owned commercial banks and National Bank of Ethiopia is used in the study. The performance of the two groups of banks evaluated and compared from the perspective of Return on Asset, Return on Equity, Net Interest Margin, Net Profit Margin, Deposit Mobilization and Loan Disbursement. Ratio and graph are employed to analyse the data. The results of the study indicated that private owned commercial banks are performing well in many of the metrics of the performance evaluation such as ROA, NIM, deposit performance and loan performance relative to the public owned banks while public owned banks are doing better than private owned commercial banks in terms of ROE.

Key Words: Commercial banks, comparative analysis, Ethiopia, ownership structure, performance.

INTRODUCTION

Despite the increasing of banks in number, expansion of the banking services and changes of various reforms in the Ethiopian banking environment since the existing ruling party came in to power, considerably fewer studies had been conducted to analyse the performance of commercial banks. Moreover, majority of existing studies are linked with investigating the determinants of profitability, confined to limited variables and time periods. None of these studies attempted to evaluate and compare the performance of Ethiopian commercial banks using a certain parameters individually and in a group.

In view of the above facts, this paper is attempted to evaluate the performance of Ethiopian commercial banks in various aspects namely, ROA, ROE, NIM, Net Profit Margin, deposit mobilization and loan and advances disbursement by grouping commercial banks into two groups namely, public owned and private owned commercial banks.

OBJECTIVES

- To evaluate the performance of public owned banks with private owned banks
- To compare the performance of public owned banks with private owned banks

REVIEW OF LITERATURE

Cheenu Goel and Chitwan Bhutani Rekhi (2013) carried out a study entitled “A Comparative Study on the Performance of Selected Public Sector and Private Sector Banks in India”. The researchers conducted a detail profitability analysis of three public sector and three private sector banks from the year 2009 to

2012 in their study. Ratios and coefficient correlation are used for data analysis. Demand deposit to total deposit ratio, saving deposit to total deposit ratio, net interest margin, credit/loan to deposit ratio, debt to equity ratio, return on assets, return on equity, capital adequacy ratio, operating margin ratio and net profit margin ratio were used as a parameters to compare the performance of the selected public sectors banks with private sector banks. From the empirical findings of the study, it is observed that private banks outperform over the public sector banks in terms of demand deposit to total deposit ratio, ROA, operating profit margin, net profit margin and financing their asset with their own sources of finance while public sector banks registered good performance over private banks on return on equity. However, in saving to deposit ratio and credit or loan to deposit ratio a mixed result is observed on the two groups of banks. Finally, they concluded that private sector banks are more profitable than private sector banks in India.

In India **Garima Chaudhary (2014)** contributed a scholarly article regarding the performance comparison of private sector banks with the public sector banks using the data from 2007 to 2011. Ratio and graphs are employed to analyse the data. The researcher used the following parameters namely: branch and ATM network, productivity, capital adequacy ratio, asset quality, growth of balance sheet size and total income, efficiency of management, earning and liquidity as a basis of comparison. The result of the study signifies that the private sector banks have expanded their branch and ATM networking at a faster rate than public sector banks and since the private sector banks capital adequacy ratio is above the minimum requirement, they have put in a comfortable position to absorb any losses and shocks relative to public sector banks. In addition to this, the finding revealed that private sector banks performing well in terms of managing operating expenses, earning and liquidity. However, the public sector banks asset base/balance sheet size and income grew at a faster rate than private sector banks and also many fluctuations regarding the growth of balance sheet size and total income is observed in private sector banks.

Sneha S. Shukla (2015) attempted to analyse financial strength of Indian public and private sector banks using a CAMEL approach. The study was made based on secondary data which was collected from three public owned banks namely bank of Baroda, PNB bank and IDBI bank; and three private sector banks such as Axis, ICICI and HDFC banks for the period from 2010 - 13. The study concluded that HDFC Bank took the first place in terms of capital adequacy, asset quality, management quality and earnings quality. In the context of liquidity ICICI Bank stood at the first place. Finally, the researcher concluded that the overall performance table shows that private banks do better than public sector banks.

Kajal Chaudhay and Monika Sharma (2011) in their article entitled “performance of Indian public sector banks and private sector banks: A comparative study” attempted to evaluate and compare the asset qualities of the two categories of banks. Trend analysis and ratio were employed for analysis. Based on the findings of their study, they recommended that public banks must pay on their functioning to compete with private sector banks. Moreover, public sector banks should be well versed in proper selection of their customers who have taken loan from them.

METHODOLOGY

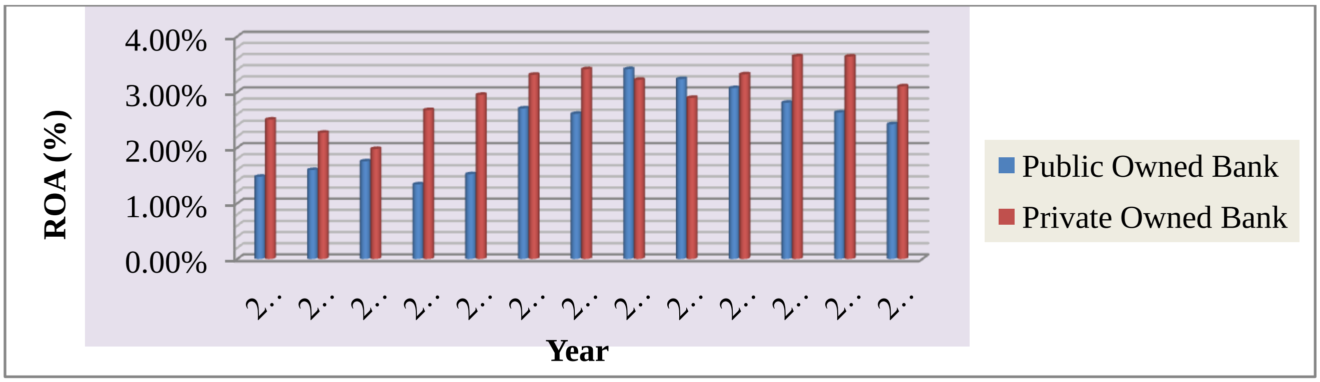
In the study, data collected from eight commercial banks namely; CBE, CBB, DB, AIB, BOA, WB, UB and NIB bank. Non-probability purposive sampling technique is employed to select the banks. Thirteen years financial data have been considered in the study. The study is based on secondary data which is collected from the annual report of the studied banks, National Bank of Ethiopia and journals. For the purpose of analysis the ratio and graphical analysis techniques are used.

RESULTS AND DISCUSSIONS

RETURN ON ASSET (ROA)

V.K. Bhalla (2006), in his book, explains ROA as a ratio which is used to measure the company's efficiency in the use of its assets to generate profit. It means that a more efficient company will generate a higher level of profit from a given level of total asset than its less efficient competitor. Return on assets is one of the standardized measures of profitability of businesses and is computed by dividing net income after tax by average assets and multiplied by 100. The graph 1 shows the comparative analysis of public owned and private owned commercial banks.

Graph 1: Comparative analysis of return on asset (ROA) of public owned and private owned commercial banks in Ethiopia from the period 2001-2013



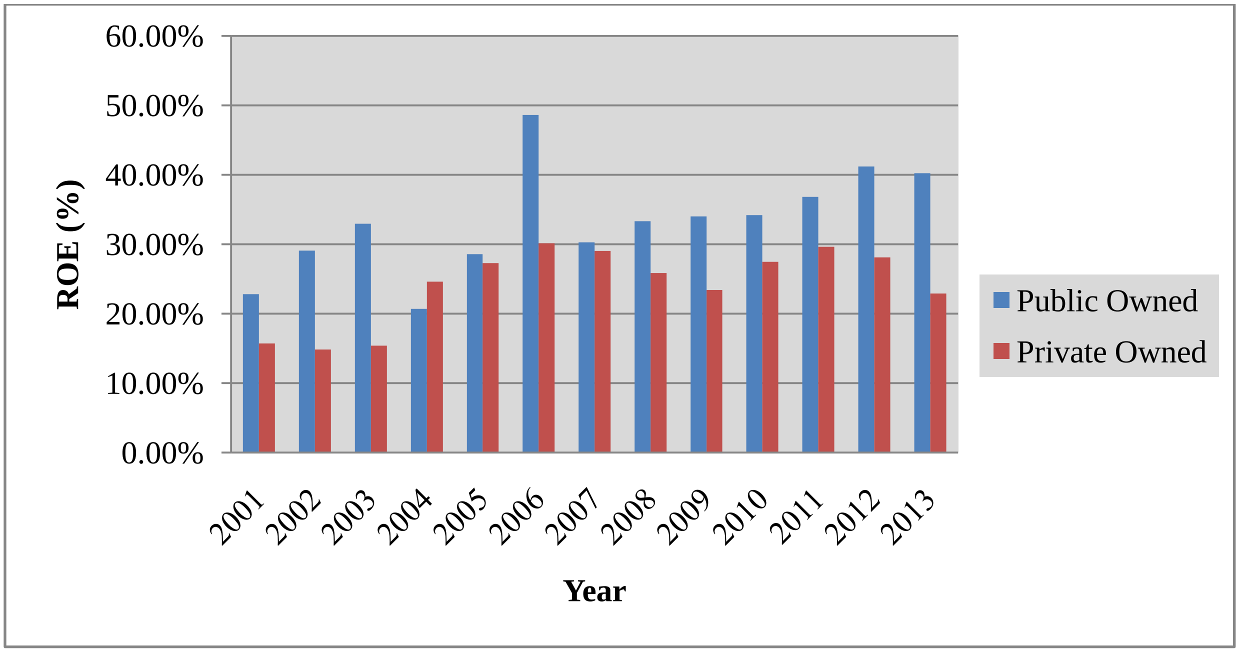
Sources: Selected commercial banks annual report and National bank of Ethiopia

Graph 1 showed that the comparative analysis of the two categories of banks. As it is observed from the above graph; public owned banks ROA varies in between 1.34% to 3.41% and private banks from 1.98% to 3.64%. Public sector banks have attained the highest and the lowest ROA in 2004 and 2008 respectively while private owned commercial banks registered the maximum ROA in two successive years 2011 and 2012 and the minimum in 2003. On average, the ROA performance of public sector banks is 2.35% and private sector banks is 2.99%. This implies that private owned commercial banks utilizes banks assets more efficiently than public owned banks to generate income to their shareholders. Therefore, the researchers concluded that private owned commercial banks do better than public owned banks in terms of return on assets in all times of under study except in 2008 and 2009 and this agreed with the result of Goel and Rekhi (2013). This may be attributed to the low income generated by CBB.

RETURN ON EQUITY (ROE)

ROE is also a ratio that refers to how much profit a company earned relative to the total amount of shareholder equity invested in the bank. In other words, it is used to measure how effectively the resources provided by the shareholders are being utilized to generate income (V.K. Bhalla, 2006). It is calculated to evaluate the performance of the bank from the perspective of shareholders' equity. Thus, the higher the ROE the better the bank is performing in terms of profit generation from the perspective of sharehoders' equity.

Graph 2: Comparative analysis of return on equity (ROE) of public owned and private owned commercial banks in Ethiopia from the period 2001-2013



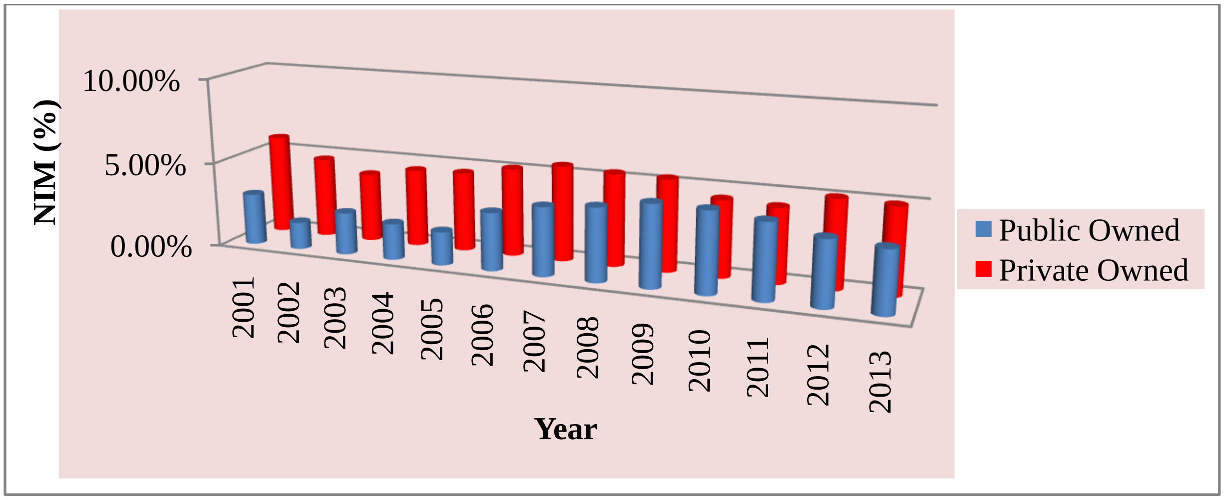
Sources: Selected commercial banks annual report and National bank of Ethiopia

As shown in graph 2, the comparative analysis of ROE of public and private owned banks. In terms of ROE, public owned banks performed well relative to private owned banks. Public owned banks attained the maximum (48.62%) in the year 2006 and the minimum in 2004 (20.69%). Private owned banks also registered the highest ROE in the same period as public owned banks in 2006 (30.13%) but the lowest (14.83%) is registered in 2002. On average public owned banks enjoyed 33.28% ROE while private owned banks attained 24.18%. Therefore; public owned commercial banks generate more net income after tax than private owned commercial banks from the equity of the bank and this also in consistent with the result obtained by Goel and Rekhi (2013) in India.

NET INTEREST MARGIN (NIM)

NIM is also one of the parameters used to measure the performance of banks in the banking environment. It is computed by dividing the net interest income by the average earning assets of banks. Net interest income is the difference between interest income and interest expense.

Graph 3: Comparative analysis of return on equity (ROE) of public owned and private owned commercial banks in Ethiopia from the period 2001-2013



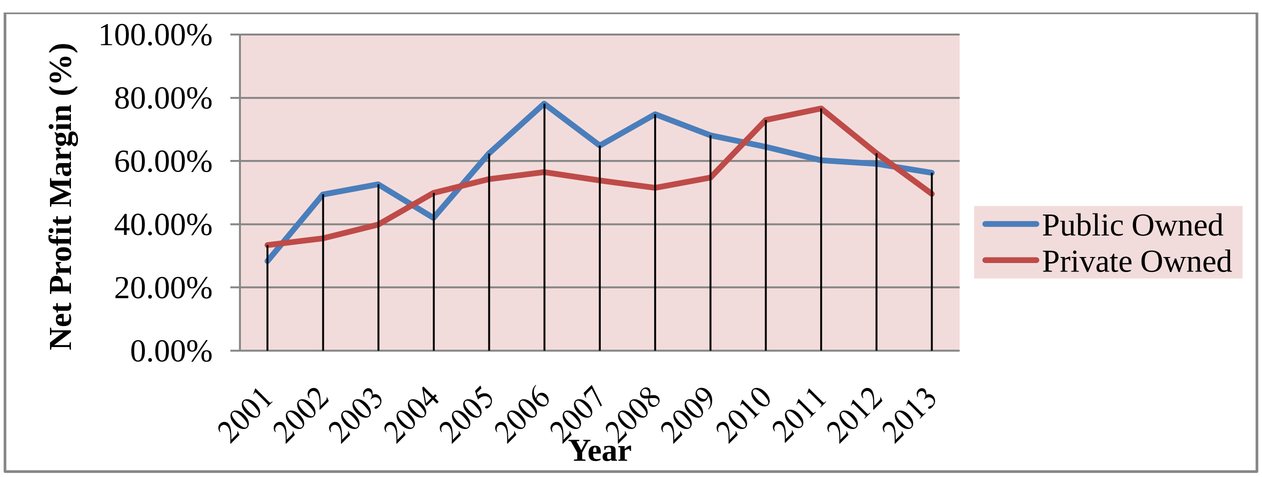
Sources: Selected commercial banks annual report and National bank of Ethiopia

Graph 3 showed that the performance of the two groups of banks in terms of NIM. As it is shown above private banks attained a better performance than public owned commercial banks in terms of NIM. Public owned banks registered the highest (4.76%) and lowest (1.59%) net profit margin in 2009 and 2002 respectively while private owned banks obtained the maximum in 2001 (5.82) and the minimum in 2003 (4.03%). With respect to the average NIM, private owned commercial banks have 4.92% and public owned banks 3.38%. Therefore, private owned banks are outperforming relative to public owned commercial banks in Ethiopia.

NET PROFIT MARGIN

Net profit margin is the ratio of net income after tax to total interest income and shows the profitability percentage of banks. A higher net profit margin signifies more efficiency of the bank in converting its revenue into actual profit (Priya.S, 2014).

Graph 4: Comparative analysis of net profit margin of public owned and private owned commercial banks in Ethiopia from the period 2001-2013



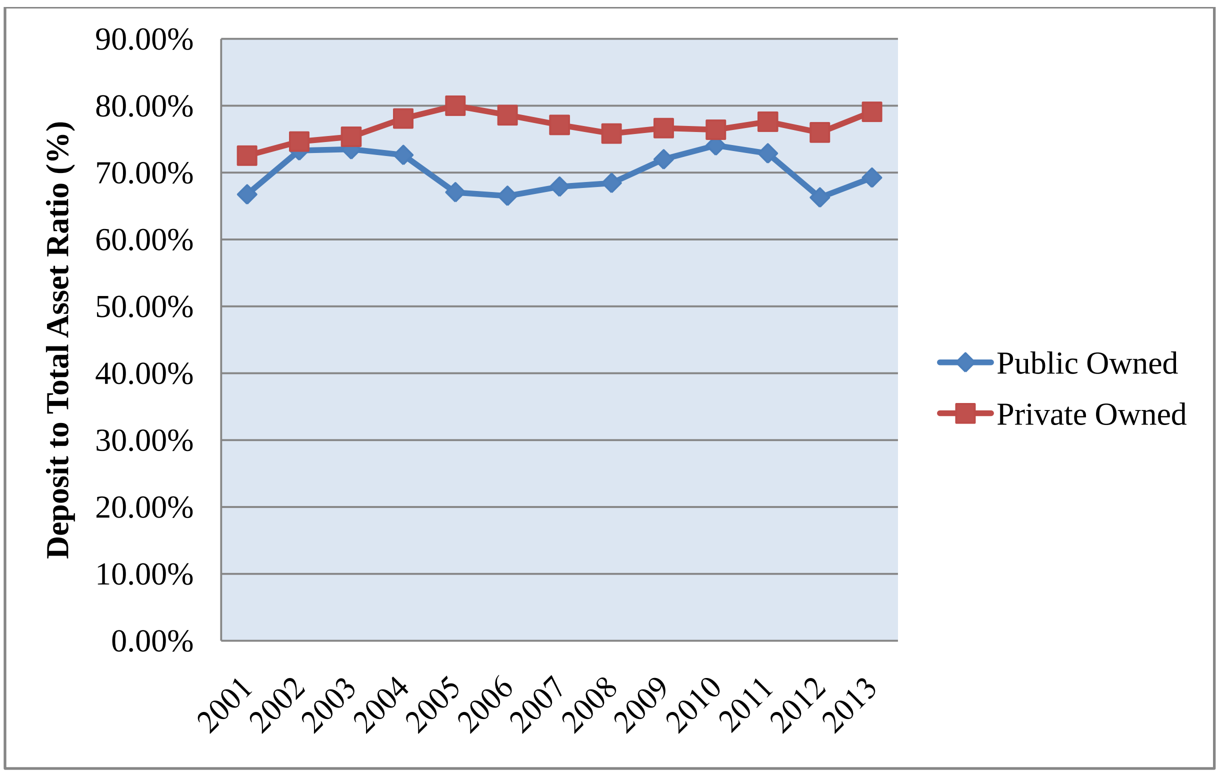
Sources: Selected commercial banks annual report and National bank of Ethiopia

As it is observed on graph 4 the two groups of banks attained highly fluctuated net profit margin from the period 2001-2013. Public owned banks attained the highest (78.12%) and lowest (28.37%) net profit margin in 2006 and 2001 respectively while private owned banks obtained the maximum in 2011 (76.59) and the minimum in 2001 (33.40%). When we look at the average net profit margin, public owned commercial banks recorded 58.52% and private owned banks 53.15% which is lower than public owned banks by 5.37%. Therefore, public owned banks are in a better position than private owned banks in converting their revenue in to actual profit after the deduction of all expenses.

DEPOSIT MOBILIZATION

It is used to measure the degree of financing demands of liquidity using the cheapest source of fund, i.e., deposit; the researchers used the ratio of total deposit to total assets to compare the performance of public owned and private owned commercial banks.

Graph 5: Comparative analysis of deposit mobilization of public owned and private owned commercial banks in Ethiopia from the period 2001-2013



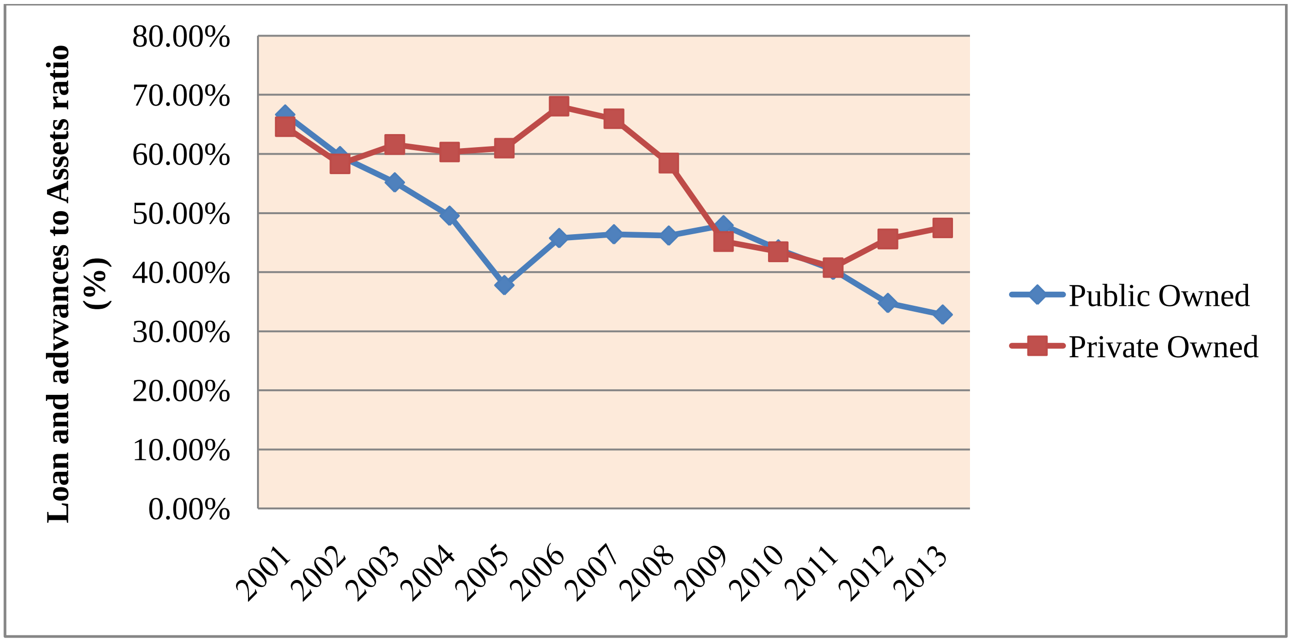
Sources: Selected commercial banks annual report and National bank of Ethiopia

As shown in graph 5 the ratio of total deposit to total asset is better in case of private owned banks than public owned in all times of the study period. Private owned banks enjoyed the highest deposit to asset ratio in 2005 (80.00%) and the lowest in 2001 (72.53%) where as public owned banks registered the highest in 2010 (74.05%) and the lowest in 2006 (66.52%). The overall average deposit to asset ratio indicates that private owned banks (76.77%) are outperforming players in the last thirteen years relative to public owned banks (70.04%). This implies that private banks are doing better in mobilizing deposits to finance their assets with the cheapest sources of funds than public owned banks.

LOAN AND ADVANCES DISBURSMENT

It is one of the principal sources of commercial banks income and expected to have an impact on banks profitability (Gul et al, 2011). High ratio is expected to enhance the profitability of commercial banks because it is the main sources of income for banks. The table below is used to analyse and compare the performance of public and private owned bank in Ethiopia.

Graph 6: Comparative analysis of loan and advances disbursement of public owned and private owned commercial banks in Ethiopia from the period 2001-2013



Sources: Selected commercial banks annual report and National bank of Ethiopia

Graph 6 is used to show the comparative analysis of loan and advances performance between public owned and private banks from the 2001-2013. The graph showed that there is a declining trend in loan and advances performance of public owned commercial banks in the most recent year since 2010. Even though private banks recording a declined trend on loan and advances performance for five successive years of operation from 2005 to 2011 in recent it starts to rise up. The maximum and minimum loan and advances public owned banks obtained in 2001 (66.69%) and 2013 (32.81%) respectively where as private banks perform the highest performance of loan and advances in 2006 (68.05%) and the lowest in 2011 (40.80%). The average loan and advances to total assets ratio also disclosed that private owned banks (55.45%) are doing better on loan disbursement relative to public owned banks (46.69%). From this the researchers concluded that private owned banks are in a better position in loan and advances disbursement to generate income for their shareholders. Since loan and advance is the main sources of income for banks, public owned banks revise their strategy and policies regarding loan advancement to borrowers. On the other hand, private owned banks should also be careful while they grant a loan and advances because the consequence of mere granting loan without detail analysis of loan takers is high. It increases the probability of not getting the principal and interest on the maturity date of the loan.

CONCLUSION AND RECOMMENDATION

The banking industry of Ethiopia has undergone through various financial reforms since the down fall of the Derg regime in 1991. Currently a total of 19 banks, of which 3 are public owned and 16 banks are private owned, are operating in a country. This study attempts to compare the performance of public owned and private owned commercial banks using a certain metrics namely, ROA, ROE, NIM, net profit margin, deposit performance and loan performance by using the data obtained from the audited financial statements of two public owned and 6 private owned commercial banks from the period 2001 and 2013. The findings of the study revealed that private owned banks outshine in many of the metrics of the performance evaluation such as ROA, NIM, deposit performance and loan performance over the public owned banks while public owned banks are doing better than private owned commercial banks in terms of ROE. However, the net profit margin result showed that there is a high fluctuation over the study period in both categories of banks. In some years public owned banks did better than private and in the other periods private owned banks are in a better position than public owned banks in terms of net profit margin. Finally we suggest that public owned commercial banks should improve their performance with regard to deposit mobilization and loan disbursement through revising their strategies and policies to enhance their income.

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