IMPACT OF FINANCIAL PERFORMANCE ON PROFITABILITY

-A STUDY ON ICICI BANK

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ABSTRACT

Financial Performance is the term which indicates the operational efficiency of every company/Institution. The performance of any institution includes the inflow of funds and better utilization and performance of the funds. Performance can be evaluated through measurement of the efficiency of funds by applying various techniques like comparative statements or ratio analysis etc. Every company or institution compares the efficiency of its own performance from year to year, so that improvement in efficiency can be assessed. The performance evaluation differs according to the nature of the Institution. When the financial performance of a Bank is compared with its previous year, it includes the elements such as deposit mobilization, advances, asset mobilization etc. The study of the financial performance definitely has its impact on the flow of the profits. In the present study, the financial performance of ICICI Bank and its impact on profitability position is focused.

Key Words: Financial Performance, Measurement , operational efficiency, Profitability, inflow of funds, Utilization of funds.

INTRODUCTION

Financial Performance is the term which indicates the operational efficiency of every company/Institution. The performance of any institution includes the inflow of funds and better utilization and performance of the funds. Performance can be evaluated through measurement of the efficiency of funds by applying various techniques like comparative statements or ratio analysis etc. Every company or institution compares the efficiency of its own performance from year to year, so that improvement in efficiency can be assessed. The performance evaluation differs according to the nature of the Institution. When the financial performance of a Bank is compared with its previous year, it includes the elements such as deposit mobilization, advances, asset mobilization etc.

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The banking industry plays a prominent role in the development of an economy. It supplies the funds that supports and enhances growth in all the industries. Growth of the banking sector is measured by the increase in the number of branches, deposits, credit, etc. Analysis of banking sector helps to study the direction in which the country's economy is moving.

ICICI Bank was originally promoted in 1994 by ICICI Limited, an Indian financial institution, and was its wholly-owned subsidiary. ICICI's shareholding in ICICI Bank was reduced to 46% through a public offering of shares in India in fiscal 1998, an equity offering in the form of ADRs listed on the NYSE in fiscal 2000, ICICI Bank's acquisition of Bank of Madura Limited in an all-stock amalgamation in fiscal 2001, and secondary market sales by ICICI to institutional investors in fiscal 2001 and fiscal 2002. ICICI was formed in 1955 at the initiative of the World Bank, the Government of India, and representatives of Indian industry. The principal objective was to create a development financial institution for providing medium-term and long-term project financing to Indian businesses.

In the 1990s, ICICI transformed its business from a development financial institution offering only project finance to a diversified financial services group offering a wide variety of products and services, both directly and through a number of subsidiaries and affiliates like ICICI Bank. In 1999, ICICI become the first Indian company and the first bank or financial institution from non-Japan Asia to be listed on the NYSE.

After consideration of various corporate structuring alternatives in the context of the emerging competitive scenario in the Indian banking industry, and the move towards universal banking, the managements of ICICI and ICICI Bank formed the view that the merger of ICICI with ICICI Bank would be the optimal strategic alternative for both entities, and would create the optimal legal structure for the ICICI group's universal banking strategy. The merger would enhance value for ICICI shareholders through the merged entity's access to low-cost deposits, greater opportunities for earning fee-based income and the ability to participate in the payments system and provide transaction-banking services. The merger would enhance value for ICICI Bank shareholders through a large capital base and scale of operations, seamless access to ICICI's strong corporate relationships built up over five decades, entry into new business segments, higher market share in various business segments, particularly fee-based services, and access to the vast talent pool of ICICI and its subsidiaries.

In October 2001, the Boards of Directors of ICICI and ICICI Bank approved the merger of ICICI and two of its wholly-owned retail finance subsidiaries, ICICI Personal Financial Services Limited and ICICI Capital Services Limited, with ICICI Bank. The merger was approved by shareholders of ICICI and ICICI Bank in January 2002, by the High Court of Gujarat at Ahmedabad in March 2002, and by the High Court of Judicature at Mumbai and the Reserve Bank of India in April 2002. Consequent to the merger, the ICICI group's financing and banking operations, both wholesale and retail, have been integrated in a single entity.

ICICI Bank disseminates information on its operations and initiatives on a regular basis. The ICICI Bank website serves as a key investor awareness facility, allowing stakeholders to access information on ICICI Bank at their convenience. ICICI Bank's dedicated investor relations personnel play a proactive role in disseminating information to both analysts and investors and respond to specific queries.

REVIEW OF LITERATURE:

- Baral (2005), study the performance of joint ventures banks in Nepal by applying the CAMEL Model. The study was mainly based on secondary data drawn from the annual reports published by joint venture banks. The report analyzed the financial health of joint ventures banks in the CAMEL parameters. The findings of the study revealed that the financial health of joint ventures is more effective than that of commercial banks. Moreover, the components of CAMEL showed that the financial health of joint venture banks was not difficult to manage the possible impact to their balance sheet on a large scale basis without any constraints inflicted to the financial health.
- Wirnkar and Tanko (2008), analyzed the adequacy of CAMEL in evaluating the performance of bank. This empirical research was implemented to find out the ampleness of CAMEL in examining the overall performance of bank, to find out the importance of each component in CAMEL and finally to look out for best ratios that bank regulators can adopt in assessing the efficiency of banks. The analysis was performed from a sample of eleven commercial banks operating in Nigeria. The study covered data from annual reports over a period of nine years (1997-2005). The analysis disclosed the inability of each component in CAMEL to congregate the full performance of a bank. Moreover the best ratios in each CAMEL parameter were determined.
- Bansal (2010) studied the impact of liberalization on productivity and profitability of public sector banks in India. The study has been conducted on the basis of primary as well as secondary data for the period 1996-07. The study concluded that the ability of banks to face competition was dependent on their determined efforts at technological upgradation and improvement in operational and managerial efficiency, improvement in customer service, internal control and augmenting productivity and profitability. The study found that public sector banks have to pay great attention to strategic management, strategic planning and to greater specialization in the technical aspect of lending and credit evaluation. It was recommended that public sector banks should strengthen their project appraisal capabilities. In order to raise their productivity and profitability, public sector banks should spell turnover strategies, income-oriented and cost oriented strategies from time to time.
- A Study of Financial performance of ICICI Bank by Dr .Krishna Banana , V.Veeranjaneya Kumar and Acharya Polisetty from Acharya Nagarjuna University concluded that, the study of financial performance and trend helps to understand the progress of the bank. The study identified that there is a significant difference in performance of the bank from 2015 onwards. The productivity of the bank presented down trend. The proportion of performing assets is also decreasing year by year. The performance of the bank is progressive till 2015, later the bank suffering from huge variations in different ratios.

STATEMENT OF THE PROBLEM

Performance and efficiency of commercial banks are the key elements of competence and efficiency of national financial system. The broad objective of the banking sector reforms in India has been to increase efficiency and profitability of the banks. Prior to banking reforms, the industry was a near monopoly dominated by public sector banks. However, the banking reforms created an opportunity to increase number of private and foreign banks in the market. Operational efficiency is an indicator, which will help not only the public but to the management, regulators, and supervisors to understand and judge the relative efficiency of the players competing in the banking sector. Therefore, this study attempts to apply different ratios on ICICI Bank in order to study its efficiency and solvency position.

OBJECTIVES OF THE STUDY

1. To study the financial performance of ICICI Bank.

2. To study the impact of financial performance on profitability of the Bank

RESEARCH METHODOLOGY:

Data Collection: The data were collected through annual reports of ICICI and other secondary sources such as internet, magazines, websites, books, and journals.

Period of study: This study covers a period of 5 years, i.e., from 2014-15 to 2018-19.

ICICI -AN OVERVIEW OF DEVELOPMENTS

The key regulatory developments impacting banks during fiscal 2019 were as follows:

• In March 2019, RBI deferred the implementation of Ind AS till further notice as the legislative amendments recommended by it were still under the consideration of the Government of India.

• RBI deferred the implementation of the last tranche of 0.625% of Capital Conservation Buffer (CCB) from March 31, 2019 to March 31, 2020. Accordingly, the minimum capital conservation ratios as earlier applicable from March 31, 2018 would apply from March 31, 2019 till the CCB attains the level of 2.5% of risk weighted assets (RWA) as on March 31, 2020. The pre-specified trigger for loss absorption through conversion/write-down of Additional Tier 1 instruments shall remain at 5.5% of RWAs and would increase to 6.125% of RWAs on March 31, 2020.

• In September 2018, RBI permitted banks to reckon an additional 2.0% of their net demand and time liabilities (NDTL), under Facility to Avail Liquidity for Liquidity Coverage Ratio (FALLCR) within the management's discussion & analysis ,mandatory statutory liquidity requirement (SLR), as level one high quality liquid assets (HQLA) for the purpose of computing their liquidity coverage ratio (LCR). This was applicable from October 1, 2018 resulting in a total of 15.0% of

NDTL comprising statutory liquidity ratio securities available for banks to be recognized as level one HQLA. In April 2019, RBI permitted a further 2.0% of NDTL to be reckoned as level one HQLA in a phased manner.

• With a view to align the SLR with the LCR requirement, RBI decided to reduce the SLR by 25 basis points every quarter until the SLR reaches 18.0% of NDTL. The first reduction of 25 basis points from 19.50% to 19.25% was effective from January 1, 2019.

• With a view to facilitate meaningful restructuring of micro, small and medium enterprises' (MSME) accounts that are stressed, RBI permitted a one-time restructuring of existing loans to MSMEs that are in default but 'standard' as on January 1, 2019, without an asset classification downgrade. To be eligible for the scheme, the aggregate exposure, including non-fund-based facilities of banks and NBFCs, to a borrower should not exceed ` 250.0 million as on January 1, 2019. The restructuring will have to be implemented by March 31, 2020. A provision of 5.0%, in addition to the provisions already held, shall be made in respect of accounts restructured under this scheme.

• With a view to facilitate flow of credit to well-rated NBFCs, in February 2019 RBI revised the risk weights on exposures to non-deposit taking systemically important NBFCs. From a uniform risk weight of 100%, RBI allowed rated exposures of banks to these NBFCs to be risk-weighted as per the rating assigned by the accredited rating agencies, in a manner similar to that for corporates. The rated exposures of banks to all NBFCs excluding Core Investment Companies (CICs), will now be risk-weighted in a manner similar to that for corporates. Exposures to CICs continue to be risk-weighted at 100%.

• In February 2019, RBI revised the definition of bulk deposits (i.e. deposits where banks have the discretion to offer differential rate of interest) from single deposit of ` 10.0 million and above to single deposit of ` 20.0 million and above. Banks are henceforth required to maintain their bulk deposit interest rate cards in the core banking system for supervisory review.

• In April 2019, the Supreme Court declared the RBI circular on revised framework for resolution of stressed assets dated February 12, 2018 as unconstitutional. RBI is in the process of issuing revised guidelines.

• In November 2018, the Securities and Exchange Board of India released a framework that requires a company rated AA and above and with an outstanding long term borrowing of ` 1.00 billion and above at March 31 in any given year, to necessarily raise 25.0% of its incremental borrowings for the following year through the bond market. This is effective from April 1, 2019.

The Bank believes that the Indian economy has significant long-term potential, based on its demographic profile, consumption growth and vast potential for investment. These factors would drive the long-term growth of the Indian financial sector. The banking sector is expected to benefit from the growing formalization of the economy, the recently introduced insolvency resolution regime and the rapid adoption of technology in banking.

FINANCIAL PERFORMANCE OF ICICI

An attempt is made here to study the financial performance during 2015-16 to 2018-19. Coverage ratio, Performing Assets ratio, Business Per Employee, Profit Per Employee, Credit Deposit ratio, Return on Assets and Income spread to total Assets ratio are selected for the analysis during the study period.

COVERAGE RATIO: Coverage ratio is a measure of owner's contribution to total assets. It is useful to measure to study the relationship between the owners' equity and total assets.

$$\text{Coverage ratio} = \frac{Net\ Worth - Net\ NPA}{Total\ Assets} \times 100$$

DEBT EQUITY RATIO: The debt-to-equity ratio (D/E) is a financial ratio indicating the relative proportion of shareholder's equity and debt used to finance a company's assets. The two components are often taken from the firm's balance sheet or statement of financial position, but the ratio may also be calculated using market value for both, if the company's debt and equity are publicly traded, or using a combination of book value for debt and market value for equity financially. A high debt/equity ratio generally means that a company has been aggressive in financing its growth with debt. This can result in volatile earnings as a result of the additional interest expense. This can result in volatile earnings as a result of the additional interest expense. A low debt/equity ratio usually means that a company has been friendly in financing its growth with debt and more aggressive in financing its growth with equity.

$$\text{Debt Equity} = \frac{\text{Total Liabilities}}{\text{Shareholders Equity}} \times 100$$

CREDIT DEPOSIT RATIO: The loan-to-deposit ratio (LTD) is a commonly used statistic for assessing a bank's liquidity by dividing the bank's total loans by its total deposits. This number is expressed as a percentage. If the ratio is too high, it means that the bank may not have enough liquidity to cover any unforeseen fund requirements, and conversely, if the ratio is too low, the bank may not be earning as much as it could be.

$$\text{Credit deposit ratio} = \frac{Total\ Advances}{Total\ Deposits} \text{ X } 100$$

CAPITAL ADEQUACY RATIO: is the ratio of a bank's capital in relation to its risk-weighted assets and current liabilities. It is decided by central banks and bank regulators to prevent commercial banks from taking excess leverage and becoming insolvent in the process.

$$\text{Capital Adequacy ratio} = \frac{\text{Capital Funds}}{\text{Risk Weighted Assets}} \times 100$$

TABLE NO:1 THE PERFORMANCE OF ICICI THROUGH RATIOS

RATIOS	2014-15	2015-16	2016-17	2017-18	2018-19
Provision Coverage Ratio	58.6%	50.6%	40.2%	47.7%	70.6%
Debt Equity Ratio	4.10%	4.23	4.39	4.53	4.50
Credit Deposit Ratio	107.17%	103.28%	94.73	91.34	88.93
Capital Adequacy Ratio	19.54	18.52	18.74	17.70	17.02

Source: Annual Reports of ICICI

The Provision Coverage ratio is high in the year 2018-19 , that means that the performance of the bank is good in the year 2018-19,Debt Equity ratio is also high in 2017-18 and 2018-19, it shows that the effectiveness of the bank to provide advances is high, Credit Deposit ratio is in decreasing mode in 2017-18 and 2018-19 which infers that the operational efficiency of the bank is good. Capital adequacy ratio is high in almost all the years which shows that the ratio higher the capacity to with stand with financial down turns.

TABLE-2 – PERFORMANCE OF ICICI THROUGH OPERATIONS

(Rs.in billion)

ITEMS	2014-15	2015-16	2016-17	2017-18	2018-19
Total Deposits	495.20	588.70	749.83	889.58	962.70
Total Advances	3875.22	4352.64	4642.32	5123.95	5806.47
Total Assets	6461.29	7206.95	7717.91	8791.89	9644.59

Source: Annual Report of ICICI

Net operating Profit	180.27	198.03	179.10	189.39	220.72

When the operational performance of ICICI is observed it is clear that in the years 2017-18 and 2018-19 deposits are more, advances are more, assets are high, profit is also high. Therefore, it is clearly proved that there is impact of financial performance on the profitability of the bank.

CONCLUSION

The study of financial performance and trends helps to understand the progress of the bank. The study identified that there is a significant difference in performance of the bank from 2015 onwards. ICICI bank has good performance in providing advances, accepting deposits, maintaining operating profits and maintain assets etc. in the years 2017-18 and 2018-19.The bank should maintain the same level of increased profits through its increasing operations.

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