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Profitability Analysis of Selected New Private Sector Banks in India: Who is better?

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Abstract

New private sector banks developed the concept of direct selling agents who reached out to customers with credit products, taking loans to the customer's doorstep. Not only did the private sector banks expand in this manner, their example forced public sector banks to also adopt similar strategies. Financial ratio analysis is a technique for evaluating the financial strengths and weaknesses of business entity. These ratios allow investors to look at the company in an objective way, for most of the profitability ratios having a higher value relative to competitor's ratio or the same ratio form a previous period is indicative that the company is doing well. So the present study has been undertaken to analyze the profitability of selected new private sector banks in India and to know who is better

INTRODUCTION

The banks, which came in operation after 1991, with the introduction of economic reforms and financial sector reforms are called "new private-sector banks". Banking regulation act was then amended in 1993, which permitted the entry of new private-sector banks in the Indian banking sector. However, there were certain criteria set for the establishment of the new private-sector banks, some of those criteria set for the establishment of the new private-sector banks, some of those criteria are. The bank should have a minimum net worth of Rs.200 crores.

1. The promoters holding should be a minimum of 25% of the paid-up capital.
2. Within 3 years of the starting of the operations, the bank should offer shares to public and their net worth must increased to 300 crores.

Financial ratio analysis is a useful tool for users of financial statement.

I. It simplifies the financial statements.
II. It helps in comparing firms of different size with each other
III. It highlights important information in simple form quickly. A user can judge a company by just looking at few

numbers instead of reading the whole financial statement.

PROFITABILITY RATIO

INTRODUCTION

Every firm is most concerned with its profitability. One of the most frequently used tools of financial ratio analysis is profitability ratios which are used to determine the company's bottom line and its return to its investors .Profitability ratios are typically based on net earnings, but variations will occasionally use cash flow or operating earnings . Profitability is a measure of efficiency and control. Profitability ratios are employed by management in order to assess how efficiently they carry on business operation. Profitability is the main base for liquidity as well as solvency. Creditors, banks and financial institutions are interested in profitability ratios

OBJECTIVE OF THE STUDY

1) To study the profitability position of some selected new private sector banks they are AXIS Bank, HDFC Bank, YES Bank and KOTAK MAHINDRA Bank.
2) To compare and highlight the overall profitability of banks by following ratiosuch as Operating profit ratio, Gross profit margin ratio, Net profit margin ratio, Adjusted cash margin ratio, Reported return on net worth. Return on long term funds.

SCOPE OF THE STUDY

Profitability ratios measure a company's ability to generate earnings relative to sales, assets and equity. These ratios assess the ability of a company to generate earnings, profits and cash flows relative to some metric, often the amount of money invested. They highlight how effectively the profitability of a company is being managed. The study covers a period of 3 years from 2011- 2013 .The present study helps to know the profitability position of new private sector banks in India; it provides invaluable evidence concerning the earnings potential of a bank and the effectiveness of management.

DATA COLLECTON

Data is gathered from secondary sources such as Bank's websites, research papers etc.

TOOLS OF DATA ANALYSIS

Statistical tools are used such as Mean, Standard Deviation, Coefficient of Variation and Chi-square tests have been used for data analysis.

Mean:

$$\bar{X} = \frac{\Sigma X}{N}$$

Standard Deviation:

$$s = \sqrt{\frac{\sum (x - \bar{x})^2}{n - 1}}$$

$$\text{Coefficient of Variation} = \frac{SD}{MEAN} \times 100$$

Chi square:

$$X^2 = \Sigma \frac{(O - E)^2}{E}$$

Where:

X^2 is the value for chi square.

Σ is the sum.

O is the observed frequency

E is the expected frequency.

Degree of Freedom = (R-1) (C-1)

LIMITATION OF THE STUDY

The study is related to a period of 3 years.

As the data are only secondary, i.e., they are collected from the published annual reports and bank websites.

Only profitability ratio is taken for the study.

OPERATING MARGIN RATIO

Operating margin or **operating profit margin** measures what proportion of a company's revenue is left over, after deducting direct costs and overhead and before taxes and other indirect costs such as interest. **Operating margin formula** is:

$$\text{Operating Margin} = \frac{\text{Operating Income}}{\text{Net Sales}}$$

Operating margin is used to measure company's pricing strategy and operating efficiency. It gives an idea of how much a company makes (before interest and taxes) on each dollar of sales. Operating margin ratio shows whether the fixed costs are too high for the production or sales volume. A high or increasing operating margin is preferred because if the operating margin is increasing, the company is earning more per dollar of sales. Operating margin can be used to compare a company with its competitors and with its past performance. It is best to analyze the changes of operating margin over time and to compare company's figure to those of its competitors. Operating margin shows the profitability of sales resulting from regular business. Operating income results from ordinary business operations and excludes other revenue or losses, extraordinary items, interest on long term liabilities and income taxes.

Mean, Standard Deviation and Coefficient of Variance

TABLE -1

YEAR	AXIS	HDFC	YES	KOTAK
MARCH 2011	13.6	19.5	25.31	15.33
MARCH 2012	10.69	15.57	21.45	12.85
MARCH 2013	11.41	14.9	11.28	14.03
MEAN	**11.9**	**16.65**	**19.34**	**14.07**
SD	**1.237**	**2.029**	**5.917**	**1.0128**
CV	**10.394**	**12.186**	**30.594**	**7.198**

INTERPRETATION:

Table-1 exhibits that bank wise mean standard deviation & coefficient of variation of operating margin of selected new private sector banks. YES has highest mean value & AXIS has lowest value when compare to other banks. Standard deviation of operating margin to sales of YES has 5.917 % with highest coefficient of variation and AXIS has low standard deviation of 1.237 % and low coefficient of variation of 12.186%, YES is having A high or increasing operating margin which is preferred because if the operating margin is increasing, the company is earning more per dollar of sales.

Hypothesis:

H0: $\mu1 = \mu2 = \mu3 = \mu4$ (There is no significant relationship between operating margin among different new private sector banks in India)

H1: $\mu1 \neq \mu2 \neq \mu3 \neq \mu4$ (There is a significant relationship between operating margin among different new private sector banks in India)

Profitability	Degrees of Freedom	Calculated value (Chi Square)	Tabular value at 5% level of significance	H0 : Null Hypothesis Accepted/Rejected
Operating Margin	6	32.72	12.592	Rejected

Since the calculated value of Chi-square (32.72) is more than the table value (12.592) as shown in table, Null hypothesis is rejected. It is therefore, concluded that there is a significant relationship between the Operating Margin among (AXIS, HDFC, YES, KOTAK) new private sectors banks in India.

GROSS MARGIN RATIO:

Gross profit margin is a key financial indicator used to asses the profitability of a company's core activity, excluding fixed cost. Gross Profit Margin formula is:

$$\text{Gross Profit Margin} = \frac{\text{Net Sales - Cost}}{\text{Net S}}$$

Gross profit margin measures company's manufacturing and distribution efficiency during the production process. It is a measurement of how much from each dollar of a company's revenue is available to cover overhead, other expenses and profits.

The ideal level of gross profit margin depends on the industries, how long the business has been established and other factors. Although, a high gross profit margin indicates that the company can make a reasonable profit, as long as it keeps the overhead cost in control. A low margin indicates that the business is unable to control its production cost.

Gross profit margin can be used to compare a company with its competitors. More efficient firms will usually see a higher margin. Also, it provides clues about company's pricing, cost structure and production efficiency. Therefore, gross profit margin can be used to compare company's activity over time.

For most of the businesses, gross profit margin is affected by seasonality. Generally, in the good months, this margin is higher than in the slower months, when the company may use sales and other marketing tools to attract more customers.

Gross profit margin is related to operating margin, which asses the profitability after including fixed cost and net profit margin, which asses the profitability after including fixed cost, interest expenses and taxes.

Mean, Standard Deviation and Coefficient of Variance

TABLE-2

YEAR	AXIS	HDFC	YES	KOTAK
MARCH 2011	11.76	17.01	24.56	12.99
MARCH 2012	9.14	13.58	20.88	10.96
MARCH 2013	10.12	13.04	10.66	12.38
MEAN	**10.34**	**14.54**	**18.7**	**12.11**
SD	**1.080**	**1.757**	**5.879**	**0.850**
CV	**10.44**	**12.08**	**31.43**	**7.018**

INTERPRETATION:

Table-2 exhibits that bank wise mean standard deviation & coefficient of variation of Gross profit margin of selected new private sector banks. YES has highest mean value & AXIS has lowest value when compare to other banks. Standard deviation of Gross profit margin to net sales of YES has 5.879 % with highest coefficient of variation 31.43% and KOTAK has low standard deviation of 0.850 % and low coefficient of variation of 7.018%.The Gross profit margin of YES is high as compare to other banks only in 2013 it decreased. High gross profit margin of YES indicates that the company can make a reasonable profit, as long as it keeps the overhead cost in control.

Hypothesis:

H0: $\mu1 = \mu2 = \mu3 = \mu4$ (There is no significant relationship between Gross Profit margin among different new private sector banks in India)

H1: $\mu1 \neq \mu2 \neq \mu3 \neq \mu4$ (There is a significant relationship between Gross Profit margin among different new private sector banks in India)

Profitability	Degrees of Freedom	Calculated value (Chi Square)	Tabular value at 5% level of significance	H0 : Null Hypothesis Accepted/Rejected
Operating Margin	6	3.377	12.592	Accepted

Since the calculated value of Chi-square (3.377) is less than the table value (12.592) as shown in table, Null hypothesis is accepted. It is therefore, concluded that there is no significant relationship between the Gross Profit Margin among (AXIS, HDFC, YES, KOTAK) new private sectors banks in India.

NET PROFIT MARGIN RATIO:

Net profit margin is a key financial indicator used to asses the profitability of a company. Net profit margin formula is:

$$\text{Net Profit Margin} = \frac{\text{Net profit (after ta}}{\text{Net Sales}}$$

Net profit margin measures how much of each dollar earned by the company is translated into profits. A low profit margin indicates a low margin of safety: higher risk that a decline in sales will erase profits and result in a net loss.

Net profit margin provides clues to the company's pricing policies, cost structure and production efficiency. Different strategies and product mix cause the net profit margin to vary among different companies.

Net profit margin is an indicator of how efficient a company is and how well it controls its costs. The higher the margin is, the more effective the company is in converting revenue into actual profit.

Net profit margin is mostly used to compare company's results over time. To compare net profit margin, even between companies in the same industry, might have little meaning. For example, if a company recently took a long-term loan to increase its production capacity, the net profit margin will significantly be reduced. That does not mean, necessarily, that the company is less efficient than other competitors.

Mean, Standard Deviation and Coefficient of Variance

TABLE-3

YEAR	AXIS	HDFC	YES	KOTAK
MARCH 2011	17.12	16.18	15.56	16.46
MARCH 2012	15.47	15.88	13.66	15.15
MARCH 2013	15.35	16.04	13.61	14.78
MEAN	15.98	16.01	14.27	15.46
SD	0.807	0.122	0.579	0.519
CV	0.05	0.762	4.057	3.357

INTERPRETATION:

Table-3 exhibits that bank wise mean standard deviation & coefficient of variation of Net profit margin of selected new private sector banks. HDFC has highest mean value & YES has lowest value when compare to other banks. Standard deviation of Net profit margin to net sales of YES has 0.579% with highest coefficient of variation 4.057%, HDFC has low standard deviation of 0.122 and AXIS has 0.050% low coefficient of variation .The Net profit margin of HDFC is high as compare to other banks. High Net profit margin of HDFC is indicator of how efficient a company is and how well it controls its costs. The higher the margin is, the more effective the company is in converting revenue into actual profit.

Hypothesis:

H0: $\mu1 = \mu2 = \mu3 = \mu4$ (There is no significant relationship between Net Profit margin among different new private sector banks in India)

H1: $\mu1 \neq \mu2 \neq \mu3 \neq \mu4$ (There is a significant relationship between Net Profit margin among different new private sector banks in India)

Profitability	Degrees of Freedom	Calculated value (Chi Square)	Tabular value at 5% level of significance	H0 : Null Hypothesis Accepted/Rejected
Operating Margin	6	0.0814	12.592	Accepted

Since the calculated value of Chi-square (0.0814) is less than the table value (12.592) as shown in table, Null hypothesis is accepted. It is therefore, concluded that there is no significant relationship between the Net Profit Margin among (AXIS, HDFC, YES, KOTAK) new private sectors banks in India.

ADJUSTED CASH MARGIN:

Adjusted cash margin also known as operating cash flow margin, the cash flow margin measures how well a company's daily operations can transform sales of their products and services into cash. A key profitability ratio, relating cash flow from operations to net sales provides powerful view into the inner workings of a company using two crucial measures of company

performance. The cash flow margin ratio measures the ability of a firm to translate sales into cash.

Adjusted cash margin = Cash Flow from Operations / Net sales

Mean, Standard Deviation and Coefficient of Variance

TABLE-4

YEAR	AXIS	HDFC	YES	KOTAK
MARCH 2011	18.58	18.23	16.31	18.43
MARCH 2012	16.72	17.55	14.25	16.79
MARCH 2013	16.39	17.60	14.15	16.22
MEAN	17.23	17.79	14.90	17.14
SD	0.964	0.309	0.995	0.936
CV	5.59	1.73	6.67	5.46

INTERPRETATION:

Table-4 exhibits that bank wise mean standard deviation & coefficient of variation of Gross profit margin of selected new private sector banks. HDFC has highest mean value & YES has lowest value when compare to other banks. Standard deviation of Adjusted cash margin to net sales of YES has 9.995% with highest coefficient of variation 6.67% , HDFC has low standard deviation of 0.309 and low coefficient of variation 1.73% .The Adjusted cash margin of HDFC is high as compare to other banks .

High Adjusted cash margin of HDFC is indicator of how well a company's daily operations can transform sales of their products and services into cash.

Hypothesis:

H0: $\mu1 = \mu2 = \mu3 = \mu4$ (There is no significant relationship between Adjusted Cash margin among different new private sector banks in India)

H1: $\mu1 \neq \mu2 \neq \mu3 \neq \mu4$ (There is a significant relationship between Adjusted Cash margin among different new private sector banks in India)

Profitability	Degrees of Freedom	Calculated value (Chi Square)	Tabular value at 5% level of significance	H0 : Null Hypothesis Accepted/Rejected
Operating Margin	6	47.28	12.592	Rejected

Since the calculated value of Chi-square (47.28) is more than the table value (12.592) as shown in table, Null hypothesis is rejected. It is therefore, concluded that there is a significant relationship between the Adjusted Cash Margin among (AXIS, HDFC, YES, KOTAK) new private sectors banks in India.

REPORTED RETURN ON NET WORTH:

The Return on Net Worth ratio ratio states the return that shareholders could receive on their investment in a company, if all the profit earned were to be passed through directly to them. Thus, the ratio is developed from the perspective of the shareholder, not the company, and is used to analyze investor returns. The ratio is useful as a measure of how well a company is utilizing the shareholder investment to create returns for them, and can be used for comparison purposes with competitors in the same industry.

Net worth ratio = Net after tax profits/shareholders capital + Retained earnings

Mean, Standard Deviation and Coefficient of Variance

TABLE-6

YEAR	AXIS	HDFC	YES	KOTAK
MARCH 2011	17.83	15.47	19.16	12.03
MARCH 2012	18.59	17.26	20.89	13.65
MARCH 2013	15.64	18.57	23.39	14.40
MEAN	17.35	17.1	21.147	13.36
SD	1.250	1.270	1.736	0.989
CV	7.20	7.42	8.20	7.40

INTERPRETATION:

TABLE-6 exhibits that bank wise mean standard deviation & coefficient of variation of Reported Return on net worth of selected new private sector banks. YES has highest mean value and KOTAK has lowest value when compare to other banks. YES has highest standard deviation (1.736) and coefficient of variation (8.20) YES is giving high returns to its shareholders compare to other banks.

Hypothesis:

H0: $\mu1 = \mu2 = \mu3 = \mu4$ (There is no significant relationship between Reported return on net worth ratio among different new private sector banks in India)

H1: $\mu1 \neq \mu2 \neq \mu3 \neq \mu4$ (There is a significant relationship between Reported return on net worth among different new private sector banks in India)

Profitability	Degrees of Freedom	Calculated value (Chi Square)	Tabular value at 5% level of significance	H0 : Null Hypothesis Accepted/Rejected
Operating Margin	6	0.740	12.592	Accepted

Since the calculated value of Chi-square (0.740) is less than the table value (12.592) as shown in table, Null hypothesis is accepted. It is therefore, concluded that there is no significant relationship between the Reported return on net worth ratio among

(AXIS, HDFC, YES, KOTAK) new private sectors banks in India.

RETURN ON LONG TERM FUNDS:

This ratio establishes the relationship between net profit and the long term fund. The term long term fund refers to total investment made in the business of long run.

Return on Long term fund % = Net profit / Long term fund

Mean, Standard Deviation and Coefficient of Variance

TABLE-7

YEAR	AXIS	HDFC	YES	KOTAK
MARCH 2011	72.25	59.91	102.46	48.25
MARCH 2012	88.84	75.20	131.35	66.29
MARCH 2013	75.72	80.09	137.76	72.07
MEAN	78.937	71.733	123.85	62.203
SD	7.14	8.595	15.35	10.14
CV	9.04	11.98	12.39	16.30

INTERPRETATION:

TABLE-6 exhibits that bank wise mean standard deviation & coefficient of variation of Return on long term funds of selected new private sector banks. YES has highest mean value and KOTAK has lowest value when compare to other banks. YES has highest standard deviation (15.35%) and coefficient of variation (12.39%). YES Bank is utilizing Efficiently long term funds and making good profits compare to other banks.

Hypothesis:

H0: $\mu1 = \mu2 = \mu3 = \mu4$ (There is no significant relationship between Return on long term funds ratio among different new private sector banks in India)

H1: $\mu1 \neq \mu2 \neq \mu3 \neq \mu4$ (There is a significant relationship between Return on long term funds ratio among different new private sector banks in India)

Profitability	Degrees of Freedom	Calculated value (Chi Square)	Tabular value at 5% level of significance	H0 : Null Hypothesis Accepted/Rejected
Operating Margin	6	2.739	12.592	Accepted

Since the calculated value of Chi-square (2.739) is less than the table value (12.592) as shown in table, Null hypothesis is accepted. It is therefore, concluded that there is no significant relationship between the Return on long term funds ratio among (AXIS, HDFC, YES, KOTAK) new private sectors banks in India.

CONCLUSION:

By analyzing the performances on the basis of profitability it can be concluded that the YES Bank is good in profitability ratios and is efficiently managing its funds and giving high returns to shareholders compare to AXIS Bank, HDFC Bank and KOTAK MAHINDRA Bank.

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