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ANALYSIS OF PROFIT PERFORMANCE OF THE COSMOS CO-OPERATIVE BANK LTD.

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ABSTRACT

As a result of Prudential Accounting Norms (PAN) the urban co-operative banks came under the financial tsunami, and became non-viable. But the Cosmos Co-operative Bank Ltd. established in the year 1906, has been emerged as a role model for urban co-operative banks in our country. The relationship identities of profit model has revealed that its profit performance quantitified with spread and burden has increased from Rs. 39.79 crore in 2004-05 to Rs. 90.48 crore in 2008-09.

Thus the Cosmos Co-operative Bank Ltd. has emerged as a role model for other urban co-operative banks. The increasing profit performance of the bank is due to dynamic and effective leadership, professional approach of management, timely applications of information technology, new products profile and right type co-operative work culture among its operative personnel. The Malegaon Committee is exploring the possibility of using UCBs for financial inclusion of unbanked and underbanked areas in our country.

Keywords: Co-operative Banks, Profit Performance, Banking.

I. Introduction

The urban co-operative banks have been developed in our country for providing institutional, low cost and non-exploitative credit to urban poor, artisans, retailers and people working in the informal sector. At present there are around 1674 UCBs operating in India with 6900 branches, 20 million customers and deposit of Rs. 1.82 lakh crore as on March 1, 2011. This data high light the development of UCBs in our country.

The banking scenario in general and urban co-operative banks in particular have under gone a paradigm change since 1991 due to the economic reforms viz Liberalisation, Privatisation and Globalization (LPG). All controls have been removed and private sector has been given priority role in our development process. Indian economy is now integrated to global market. As a result the foreign banks entered into India's Financial Market for business. Our banks have to compete with foreign banks. In order to make our banks comparable and competitive with foreign banks, government appointed a committee on financial sector reforms and banking sector reforms, under the chairmanship of Narsimham, Ex-Governor of RBI. The Narsimham committee made series of recommendations on banking sector reforms in 1991 and the same have been accepted by government and introduced by RBI.

The applications of Prudential Accounting Norms (PAN) viz :

(i) Classification of assets
(ii) Recognition of income and
(iii) Provisioning

These PAN have seriously affected the profitability of commercial banks in general and urban co-operative banks in particular. Thus, many urban co-operative banks have become non-viable.

The Cosmos Co-operative Bank Ltd. established in the year 1906. This urban co-operative bank is oldest in our country with 105 years of age. The deposits of Cosmos Co-operative Bank increased from Rs. 2851.28 crore in 2004-05 to Rs. 6655.63 crore (233.43%) in 2008-09, credit from Rs. 3896.54 crore to 1581.27 crore in 2008-09 (246.42%) in 2008-09 and net profit from Rs. 39.79 crore in 2004-05 to Rs. 90.48 crore in (227.39%) in 2008-09. This shows that in the Financial tsumamy many urban co-operative banks have become non-viable but the Cosmos Co-operative Bank emerged as a role model for urban co-operative banks in our country. Therefore an attempt is made to analyse its Profit performance for period 2004-05 to 2008-09.

II. Survey of Literature

Banking commission (1971-72) analysed the cost and capital structure to explain the behaviour of profitability of banks in India.

R.B.I. appointed (1976), the working group on production efficiency and profitability in commercial banks. The committee examined the problem and made useful suggestions.

R.B.I appointed (1978) T.S.Raj committee to examine the effect of priority sector lending on profitability of banks.

S.P.Singh (1974) published his article on profitability of nationalized banks in economic and political weekly.

R.Raghupathy (May 1980) focus on the perspective of profit planning in commercial banks, Indian Banks Association Bulletin.

P.D.Nambiar (April 1970) examined the issue of monitoring profitability in banks in commerce.

M,Narayanan Bhat (Sept. 1974) analysed the decling profitability of banks in commerce.

S.G.Shah (August 1980) analysed the consideration for branch profitability, in Business India.

The above literature survey of bench mark of scholors has helped to build the foundation for applied thoughts.

III. Objectives

To probe into the effect analysis of economic reforms and banking sector reforms on profit performance of the Cosmos Co-operative Bank.

To identify the key sensitive variables of profit performance of the Cosmos Co-operative Bank Ltd.

To quantify the profit performance of the Cosmos Co-operative Bank, with the help of structured frame work of functional relationship identity of profit.

To identify the sensitive variables having strong positive and negative impact on profit performance of the Cosmos Co-operative Bank.

Hypothesis

"Other things being equal the profit performance of the bank is strongly determined by spread and burden."

IV. Coverage and Research Methodology

The coverage of research study is confined to the Cosmos Co-operative Bank for the time frame of 2004-05 to 2008-09. The ratio analysis, a tool of financial management is used for the analysis of financial data, drawn from the profit and loss account and balance sheet published in its annual reports for period 2004-05 to 2008-09. The statistical tools viz, Descriptive Statistics, Mean & Standard Deviation, Karl Pearson's Correlation Metrix, Regression and Value of R and R^2 have been used for validation of ratio analysis.

In the structured frame work outlined in Table 1, the spread and burden play key roles in determining the profit of the Cosmos Co-operative Bank Ltd. The profit of the bank can be increased by increasing the spread and by reducing the burden. The model of RIOP is shown in exhibit I.

The structured frame work of profit model in terms of spread and burden is developed with help of following equations.

A Segment of Interest Earning Assets and Total Interest Income Equation is as follow:

$$\text{Interest Income} = \sum_{i=1}^{n} (x_i y_i)$$

Where :

n = Total interest earning assets
xi = Components of interest earning assets
yi = Interest income earned on 'n'
i = 1,2,3,…..n.

B Factors of Interest Expenses Present in the following formula

$$\text{Interest Expense} = \sum_{i=1}^{e} (d_i t_i)$$

Where:

e = Total interest carrying liabilities
di = Components of interest carrying liabilities
ti = Interest paid on liabilities
i = 1,2,3,…..e

C Interest Surplus / Spread :

$$\text{Spread} = \sum_{i=1}^{n} (x_i y_i) - \sum_{i=1}^{n} (d_i t_i)$$

D Burden / Non-Interest Load

Non-Interest Expenses

$$NIE = \sum_{t=1}^{m} (J_t K_t)$$

Where :

m = Total non-interest expenses
Ji = Components of non-interest expenses
Ki = Amount paid on components of 'm'
I = 1,2,3,…..m.

Non-Interest Income

$$NII = \sum_{t=1}^{n} (L_t P_t)$$

Where :

N = Total non-interest income
Li = Components of non-interest income
Pi = Amount earned on components of 'N'
i = 1,2,3,…..N.

Non-Interest Burden

$$NIB = \sum_{t=1}^{m} (J_t K_t) - \sum_{t=1}^{n} (L_t P)$$

E P = S – B

$$P = \left[\sum_{t=1}^{n} (x_t y_t) - \sum_{t=1}^{e} (d_t t_t)\right] - \left[\sum_{t=1}^{m} (J_t K_t) - \sum_{t=1}^{n} (L_t P_t)\right]$$

V. Analysis of Data and Interpretations

Analysis of Functional Relationships Between Spread Burden and Profit:

Table 2 revels the financial analysis of spread. Spread is the difference between interest earn and interest paid. The spread is the major determinant of profit performance of bank. The spread of the Cosmos Co-operative bank recorded rise from Rs. 93.71 crore in 2004-2005 to Rs. 199.14 crore in 2008-09.

Table 3 shows the behaviour of burden of the bank. The non-interest expenses (NIEs) minus non-interest income (NII) is the burden of the bank. The burden has a negative effect on profit performance of the bank. The burden of the Cosmos Co-operative Bank Ltd. Increased from Rs. 53.92 crore in 2004-05 to Rs. 108.24 crore in 2008-09.

Table 4 reveals the functional relationship between spread, burden and profit. The spread and burden both have consistently increased for the period under study. But increase in spread was relative much higher than burden for the time frame of study. As a result the profit of the bank consistently increased from Rs. 39.79 crore in 2004-05 to Rs. 90.48 crore in 2008-09.

Table 5 highlights the analysis of burden. The non-interest expenses (NIEs) increased from Rs. 76.5 crore in 2004-05 to Rs. 183.68 crore in 2008-09. The establishment expenses recorded rise from Rs. 28.32 crore in 2004-05 to Rs. 46.83 crore in 2008-09. The other expenses recorded rise from Rs. 32.42 crore in 2004-05 to Rs. 59.90 crore in 2008-09. The provisions have increased from Rs. 15.77 crore in 2004-05 to Rs. 77.07 crore in 2008-09. Therefore, bank has to minimize its provisions by minimizing the non-performing asses. The NPAs have been the most critica; and sensitive variable affecting the profit performance of the bank.

Statistical Analysis:

Profit is considered as dependent variable and SPREAD and BURDEN as independent variables. The statistical analysis is done to assess data validation and to prove the inter functional relationship among the variables selected for research probe. The descriptive statistics explains the mean and standard deviation of profit spread and burden variables. It shows inter relative standard deviation from mean among profit, spread and burden. The standard deviation gives the data variability from its mean. Out of the three key variables selected for the study, the major deviation is seen in the spread. It is quite apparent that banks would strive to increase its spread and there by would intent to increase profit, and hence the spread would enhance, more variability from its mean.

The Karl Pearson's correlation is also calculated to ascertain the direction of change between dependent variable and independent variables. The 'Karl Pearson's Correlation Matrix', shows strong positive inter-variate correlation. The Pearson's Correlation Matrix shows relatively high positive correlation between dependent variable profit and independent variable spread. There is also negative correlation between profit and burden and spread and burden.

Moreover, the value of correlations for three variables for bank is very high and near one, which undoubtedly support the relationship established in the analysis.

Pearson's Correlation analysis gives an idea about the direction of change in the variables but does not given information about the degree of change. For calculating the degree of change, linear regression model is used. In application of linear regression model, profit is assumed to be dependent variable and spread and burden are independent variables. The regression analysis shows the effect of change in independent variable on dependent variable. The regression equation is as under:

$$Y = a + bx + cz + ei$$

The model summary gives the value of coefficient of regression i.e. R and R square give the extent / degree of dependency of dependent variable on independent variables. The value of R square is one. So, it implies that the independent variables viz spread and burden perfectly explain the dependent profit variable. Thus the profit of Cosmos Co-operative Bank is dependent on the spread and burden. The bank can increase its profit by increasing spread and reducing burden.

The burden analysis explains the sensitive financial variable responsible for increase in the burden of non-interest expenses variables. The standard deviation shows the data variability from its mean. Out of three key variables selected for the study the major deviation is seen in the provisions provided by the bank. Increase in burden / non-interest expenses (NIEs) is mainly due to an increase in provisions provided by bank.

The Pearson's Correlation Matrix shows an increase / negative relationship between establishment expenses and NIEs, other expenses and NIEs but positive correlation between provisions and NIEs. Morever, the value of correlations for the three variables of bank, is very high and nearly to one, which undoubtedly support that the relationships established in the analysis preserve and a high correlation exists among the variables selected for the study.

For calculating the degree of change, linear regression model is used. The model summery gives the value of coefficient of regression i.e. R and R square gives the extent / degree of dependency of dependent variable on independent variables. The value of R square is near one. Thus the degree of dependency of dependent variable. NIEs on independent variables viz, provisions, establishment and other expenses is very high. So, it implies that independent variables perfectly explains the dependent variables.

VI. Conclusion

As a result of Prudential Accounting Norms (PAN) the urban co-operative banks came under the financial tsunami, and became non-viable. But the Cosmos Co-operative Bank Ltd. established in the year 1906, has been emerged as a role model for urban co-operative banks in our country. The relationship identities of profit model has revealed that its profit performance quantitified with spread and burden has inceased from Rs. 39.79 crore in 2004-05 to Rs. 90.48 crore in 2008-09.

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Tables

Table : 1
Functional Relationship Identities of Profit

Relationship Identities	Income	Expenses	Difference	Symbols
i	I Interest Income	E Interest Expenses	Surplus (I – E)	S
ii	D Non-Interest Income	F Non-Interest Expenses	Burden (F – D)	B
iii	J Total Income (J = I + D)	K Total Expenses (K = E + F)	Net Profit (J – K)	P

Table 2
Spread

(Rs. In Crores)

	2004-05	2005-06	2006-07	2007-08	2008-09
Interest Income	268.31	305.72	347.09	476.45	630.60
Interest Expenses	174.60	193.95	222.31	322.75	431.46
Spread	93.71	111.77	124.78	153.70	199.14

Source: Annual reports of Cosmos Co-operative Bank Ltd., 2004-05 – 2008-09.

Table 3 Burden

(Rs. In Crores)

	2004-05	2005-06	2006-07	2007-08	2008-09
Non-Interest Expenses	76.51	98.55	143.76	114.56	183.38
Non-Interest Income	22.59	36.90	79.30	33.79	75.14
Burden	53.92	61.65	64.48	80.77	108.24

Source: Annual reports of Cosmos Co-operative Bank Ltd., 2004-05 – 2008-09.

Table 4 Profit

(Rs. In Crores)

	2004-05	2005-06	2006-07	2007-08	2008-09
Spread	93.71	111.77	124.78	153.70	199.14
Burden	53.92	61.65	64.48	80.77	108.66
Profit	39.79	50.12	60.32	72.93	90.48

* P = S – B

Table 5 Analysis of Burden

(Rs. In Crores)

	2004-05	2005-06	2006-07	2007-08	2008-09
Burden	53.92	61.65	64.46	80.77	108.24
Non-Interest Expenses	76.51	98.55	143.76	114.56	183.38
Establishment Expenses	28.32	32.18	37.10	42.78	46.83
Other Expenses	32.42	33.02	41.60	47.14	59.90
Provisions	15.77	33.35	65.02	24.64	77.07

Source : Annual reports of Cosmos Co-operative Bank Ltd., 2004-05 – 2008-09.

Table 6 Regression and Correlations

Descriptive Statistics

	Mean	Std. Deviation	N
Profit	62.7280	19.78109	5
Burden	73.8080	21.59147	5
Spread	136.6200	41.22940	5

Correlations

Pearson Correlation	Profit	Burden	Spread
Profit	1.000	.971	.992
Burden	.971	1.000	.994
Spread	.992	.994	1.000
Sig. (1-tailed)			
Profit		.003	000
Burden	.003		.000
Spread	.000	.000	
N			
Profit	5	5	5
Burden	5	5	5
Spread	5	5	5

Regression Equation

y = a + bx + cz + ei

Variables Entered / Removed

Model	Variables Entered	Variables Removed	Method
1	Spread[a] Burden		Enter

a. All requested variables entered.

b. Dependent Variable : Profit

Regression

Descriptive Statistics

	Mean	Std. Deviation	N
Non Interest Exp/Non Interest Income	38.5080	10.57500	5
Establishment Exp/Non Interest Income	31.6660	5.78319	5
Other Exp/Non Interest Income	35.7200	5.78781	5
Provisions/Non Interest Income	32.6380	11.36333	5

Correlations (N=5)

Pearson Correlation	Non Interest Exp/Non Interest Income	Establishment Exp/Non Interest Income	Other Exp/Non Interest Income	Provisions/ Non Interest Income
Non Interest Exp/Non Interest Income	1.000	-.872	-.928	.916
Establishment Exp / Non Interest Income	-.872	1.000	.917	-.980
Other Exp / Non Interest Income	-.928	.917	1.000	-.978
Provisions / Non Interest Income	.916	-.980	-.978	1.000
Sig (1 tailed)				
Non Interest Exp/Non Interest Income		.27	.012	.014
Establishment Exp / Non Interest Income	.027		.014	.002
Other Exp / Non Interest Income	.012	014		.002
Provisions / Non Interest Income	.014	.002	.002	

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