The Assessment of Banking Performances- Indicators of Performance in Bank Area

Caruntu, Genu Alexandru and Romanescu, Marcel Laurentiu

University of Constantin Brancusi Targu Jiu, Romania

16 October 2008

THE ASSESSMENT OF BANKING PERFORMANCES-INDICATORS OF PERFORMANCE IN BANK AREA

Căruntu Genu Alexandru – Lect. Univ. dr.

Universitatea Constantin Brâncuşi Tg-Jiu

Romanescu Marcel Laurențiu – Lect. Univ. dr.

Universitatea Constantin Brâncuşi Tg-Jiu

Abstract

Profitability is a management concept with the objective of assessment bank's results from efficiency point of view both for entirely activity and for differently management compounds.From conceptual point of view, profitability represents the modality to achieve the major goal of bank's activity, respectively the maximization of profit in minimization risk conditions. The approach from a quality perspective of activity results conducts to assessment of application modalities of different compunds of management, in comparison to the strategy elements, thus must to result the concrete degree to achieve the politic and banking strategy compunds.

Keywords: profitability, assets, balance, rentability

The profitability analysis are achieved on a set of indicators to measure the banking performances. The indicators result/arise from the accounting dates, which illustrate the reference periods in the most synthetic expressions of balance sheet and the profit and loss account.

Must be said that, during the incomes situation, the interests cashed which represent incomes, also the paid interests which represent expenses are determined as yearly medium account balances, by application to every one the usually interest percentage.The taxes are settled by application the topic tax quotations.

On the basis of balance sheet for the analysed period and the profit and loss account, are determined the necessary elements in order to express the profit indicators, and afterwards is proceeding to their's determinations. The main performance indicators computed for banks are:

1. **Return on Equity** or profit to equity, is the most signficant indicator for profit, which measures the banking management in all its dimensions, and offers an image over the way to use the capitals brought by shareholders, the effect of their retainer in bank's activity. The indicator are determined thus :

$$ROE = \frac{Net\ \ profit}{Capital} \cdot 100$$

It is considered the net profit after deduction of all expenses and taxes and the capital is a sum of nominal capital, of unshared profit and the reserve funds. The speciality literature allots important studies to this indicator, considered one of the most characteristic barometer of some commercial enterprise performances. In the banks situation, a normal margin of this indicator is appreciate to be located /situated between the significant thresholds of 10% and respectively 30% .

2.**Return on Assets**. This indicator is an expression of rentability for the entirely activity of a banking society. This indicator known also as profit to assets or in a consecrete definition accepted already in banking literature from our country, the assets rentability, measures the effect of management capacity to use the financial and real resources of bank society in order to generate profit. It is appreciate that the return of assets indicator is the most exact measure of banking activity due the fact that expressed directly the result, accordingly to the specific management of banking intermediate, of active operations optimization, related to a volume of resources considered. The computation formula of the indicator is:

$$ROA = \frac{Net\ \ \mathrm{Pr}\,ofit}{Assets} \cdot 100$$

The limits of indicator's variations is generally between 0,5-1,6%. Specifically to the big banks is the small value (< 1%), while to the small and medium banks is characteristic an extraunit dimension of indicator.

3. **Leverage Multiplier.** This indicator is very characteristic for the bank, known also under the title of leverage effect, measures also the degree in which the attraction and using of new resources conduct to an increase of capital rentability.The indicator illustrates how many time a bank successed to multiply the invested capital by resources atraction.The leverage multiplier surpass normally the value 100 and illustrates the fact that involving of new resources is efficient for the bank, respectively when the resources cost is lower then the return costs.

The indicator is computed thus:

$$MC = \frac{Assets}{Capital} \cdot 100$$

The indicator changes in proportion with the capital's share in total banking assets. As much as the capital share is higher, the bank risk is lower and the leverage effect is lower, too. In the contrary case, when the share is smaller, the banking risk and the leverage effect are higher.

As a value, the big banks recording levels of over 20%, while to the small banks is characteristic the level of 10-20% for leverage. Must be marked the correspondence between these three indicators presented until now.When the indicator compounds are identically, could determine directly the leverage multiplier from the underneath relation:

$$Mc = ROE/ROA$$

4. **The profit rate.** In the banking area are computed the profit rate, on which the dimension depends first by the ratio between bank income and expenses, and second by the structure of incomes and the costs of banking activity. As much as the banking services tariff are made in an explicit/outspoken manner, meaning that every service is differential by peculiar prices, the indicator could be computed on various compounds of bank's activity, after the following formula:

$$Rp = \frac{Net\,\mathrm{Pr}ofit}{TotalIncomes} \cdot 100$$

The indicator represents the main instrument/tool of analysis when is following/chasing the costs decreasing with banking activity.

5.The margin of assets utilization. The dimension of this indicator depends by the active interest measured on market and the banking assets structure. The indicator is defined as a ratio between the total operational income and the assets total, illustrating the total incomes obtained from assets utilization (incomes from interests, commissions, taxes):

$$RAC = \frac{TotalIncomes}{TotalAssets} \cdot 100$$

6.**Margin Profit,** indicator which illustrates the profit percentage from profit (or net income) achieved from total operational incomes:

$$Rm = \frac{\mathrm{Pr}ofit\ net}{Totalincomes} \cdot 100$$

Must be marked that these two indicators could determine directly the assets rentability :

$$ROA = Pm*Au$$

and indirect the capital leverage: $Mc = ROE/(Pm*Au)$

The connections/links between the indicators presented above illustrate the existence of one bank performances assessment pattern, named by the experts after the indicator considered the most important in assets rentability issues. That's why, commercial bank analysis are made on the basis to accentuate/illustrate the indicators from ROA model (or ROE model in other expert's conception) or theirs derivations.Thus , the above indicator could be "split" on the compounded elements of discussed variable, illustrating the impact which as an example, each active, capital, income or expense element detains over the level and quality of profit.

The profitability concept can be defined both to vertical coordinates, in local version(which takes into account the financial efficiency of the branch on short term and the strategies to increase the efficiency on various terms), and to horizontal coordinates through analysis of one certain part of bank's activity, all this conceptual elements beeing included in general version of bank's strategy.

In order to determine one bank activity efficiency (considered in assembly or to the branch level) the simple elaboration of indicators is not enough. This indicators must be compared with the similar indicators in order to determine the real bank's position from profitability point of view. Are practise, in general, three comparison types :

1. comparison with same bank indicators during years flowing;
2. comparison with the medium indicators of other banks inside same period frame;
3. comparison with the planned indicators, when the bank elaborates strategies on various structural terms in plans which aim to obtain certain profit levels .

It could be deduced the necessity to ensure a single conception to banking system level related to performance indicators, and same time, the ensuring of informational system necessary to comparison achievements.

BIBLIOGRAPHY

1.	Dănilă N., Berea A. O.	– „Banking Management , bases and theories”, Economic P.H, Bucharest, 2003;
2	Nițu I.	– „Banking financial management ”, Expert P.H, Bucharest 2000;
3	Todorache D., Rusu L., Târdea P. P., Ivan M. V.	– „Banking financial management ”, University Chart P.H, Bucharest, 2004;
4	Stoica M.	– „The banking management”, Economic P.H, Bucharest, 1999;
5	Roxin L.	– „Administration of banking risks ”,Didactic and Pedagocic P.H, Bucharest, 1997;
6	Paxino D., Moşteanu N. R.	– „Management of foreign currencies risks and applications in international transactions”, Sylvi P.H , Bucharest, 2002;