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Comparison of Profitability, Liquidity and Credit Performance of NBO and HSBC Bank in Oman

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Abstract

This main objective of the study is to examine the performance of National Bank of Oman (NBO) with Hongkong and Shanghai Banking Corporation (HSBC) bank for a period of 6 years from 2010 to 2015. Performance parameters such as Profitability, Liquidity and Credit ratios are used to examine the performance of the two banks and simple statistical tools are also used. Finding of the study shows that NBO has outperformed HSBC in term of profitability performance, while liquidity and credit performance both the same have similar performance. The study suggested that liquidity and credit performance of the both the banks have to improve for better financial performance of the banks.

Key Words: NBO, HSBC, Performance, Profitability, Liquidity and Credit.

1. Introduction:

A strong financial system is important for promoting sustainable economic development. The performance of banks in the financial system of a country is very important for the development of the economy. Banking business is increasingly led by customer expectations and successful delivery of service. Measuring the health of an economy can be accomplished by studying the financial performance of its bank, (Haque and Sharma, 2011). To enhance the quality of its products and services and diversity, and to keep pace with the rapid developments taking place in the world in this field. So banks attempt to find new method to improve their services. To understand the performance, managers and policy makers stated the major question "What drives performance?" To address this question, researchers have focused their efforts on the operational details (Soteriou and Zenios, 1999). The commonly used measures are profitability, liquidity and credit performance for analyzing the performance of banks. The widely used measures to assess banks' performance are return on total assets (ROA) and return on total equity (ROE). These measures have been used by analysts and bank regulators in (a) assessing industry performance (b) forecasting market structure trends (used to predict bank failures and mergers) and (c) other purposes where a profitability measure is wanted (Gilbert and Wheelock, 2007). Over the past several years, an increased attention has been received by financial institutions on performance analysis. The author in this research paper has used the same measures for analyzing the performance of NBO and HSBC.

2. Literature Review:

Berger & Humphrey (1997) assert that the whole idea of measuring bank performance is to separate banks that are performing well from those which are doing poorly. They further indicated that, "evaluating the performance of financial institution can inform government policy by assessing the effects of deregulation, mergers and market structure on efficiency" (p175). Bank regulators screen banks by evaluating banks' liquidity, solvency and overall performance to enable them to intervene when there is need and to gauge the potential for problems (Casu *et al,* 2006). On a micro- level, bank performance measurement can also help improve managerial performance by identifying best and worst practices associated with high and low measured efficiency.

Kiyota (2009) in a two- stage procedure investigated the profit efficiency and cost efficiency of commercial banks operating in 29 Sub-Saharan African countries during 2000-2007. The article employs the SFA for the estimation of profit and cost efficiency, financial ratios and the Tobit regression to provide cross-country evidence on the performance and efficiency of African commercial banks. The findings based on a range of performance ratios as well as stochastic cost and profit frontier estimation, suggest that foreign banks tend to outperform domestic banks in terms of profit efficiency as well as cost efficiency. The results are also in line with the research by Kirkpatrick *et al* (2007) who used a sample of 89 banks from Sub-Sahara African countries for the period 1992-1999 and found that banks are on average 67% profit efficient and 80% cost efficient, as indicated by the results from both the distribution free approach and SFA methods.

Hassan and Bashir (2003) who look at the determinants of Islamic bank performance and show Islamic banks to be just as efficient as conventional banks if one uses standard accounting measure such as cost to income ratio. Moreover, banks should have solid knowledge of how to manage their data and how to create and emend the database periodically. Samad and Hasan (1999) apply financial ratio analysis to see the performance of Malaysian Islamic bank over the period 1984-1997 and generally find that banker's lack of knowledge was the main reason for slow growth of loans under profit sharing.

Another study that provides a brief but interesting account of bank performance was conducted by Ncube (2009) who uses the stochastic frontier model to analyze the cost and profit efficiency of four large and four small South African banks. The results of the study show that South African banks have significantly improved their cost efficiencies between 2000 and 2005 with the most cost efficient banks also being most profit efficient. However, efficiency gains on profitability over the same time period were found not to be significant.
In the Gulf, Samad (2004) investigated the performance of seven locally incorporated commercial banks during the period 1994-2001. Financial ratios were used to evaluate the credit quality, profitability, and liquidity performances. The performance of the seven commercial banks was compared with the banking industry in Bahrain which was considered a benchmark. The article applied a Student's *t*-test to measure the statistical significance for the measures of performance. The results revealed that commercial banks in Bahrain were relatively less profitable, less liquid and were exposed to higher credit risk than the banking industry, in which wholesale banks are the main component.

Tarawneh (2006) found that the banks having high total capital, deposits, credits, or total assets does not always means that has healthier profitability performance. The operational efficiency and asset management, in adding to the bank size, positively influenced the financial performance of these banks. In the light of his empirical study he concluded that the operational efficiency and asset management, in addition to the bank size, strongly and positively influenced financial performance of the banks.

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3. Objective of the study:

The objective of the study is

a. To measure and compare the profitability performance of the banks.
b. To measure and compare the liquidity performance of the banks.
c. To measure and compare the credit performance of the bank.

4. Research Methodology:

Selection of the samples: Sample selected for this study are National Bank of Oman (NBO) and Hongkong and Shanghai Banking Corporation (HSBC) banks which are listed in Muscat Securities Market are selected at random.

Nature of date: The nature of data selected was secondary data which was collected from annual report of the selected banks from Muscat Securities Market Website and other related secondary data was collected from websites and journals.

Period of the Study: The project covers a period of 6 years from 2010 to 2015. Five years period has been taken for analysis, as all the short-term changes will be absorbed while all cyclic changes will be nullified in the period.

Mode of Analysis: The techniques of ratio analysis has been adopted for the purpose of analyzing the data. The following tools are used for analyzing the performance:

For analyzing the profitability performance the following ratios are used:

a. Return on Assets (ROA)
b. Return on Deposits (ROD)
c. Return on Equity (ROE)
d. Net Interest Margin (NIM)

For analyzing the liquidity performance the following ratios are used:

- **a.** Total Loans to Total Deposits Ratio (TLTD)
- **b.** Total Deposits to Total Assets Ratio (TDTA)

For analyzing the credit performance the following ratios are used:

- **a.** Total Revenue to Total Assets Ratio (TRTA)
- **b.** Provision to Total Loan Ratio (PTL)
- **c.** Provision to Total Assets Ratio (PTA)

5. Analysis of the study:

a. Descriptive Statistics: To know the mean differences among the selected variables within the observed period for NBO and HSBC banks descriptive statistics was done.

Table 1: HSBC Descriptive Analysis

Ratios	ROA	ROD	ROE	NIM	TLTD	TDTA	TRTA	PTL	PTA
Mean	0.0080	0.0103	0.0572	0.0428	0.6625	0.7846	0.0316	0.0037	0.0019
Median	0.0057	0.0069	0.0412	0.0432	0.6557	0.8028	0.0325	0.0034	0.0017
Maximum	0.0156	0.0221	0.1065	0.0490	0.8019	0.8259	0.0347	0.0059	0.0033
Minimum	0.0030	0.0031	0.0244	0.0336	0.5469	0.6896	0.0251	0.0023	0.0010
Std. Dev.	0.0053	0.0074	0.0358	0.0054	0.0837	0.0508	0.0035	0.0014	0.0008
Skewness	0.8582	1.0390	0.8380	-0.9070	0.5786	-1.6823	-1.6423	0.8722	0.8483
Kurtosis	-1.4880	-0.4663	-1.7445	1.1680	1.7139	2.7801	2.9610	-0.0959	0.0825

Note: Total observation are six years

Table 2: NBO Descriptive Analysis

Ratios	ROA	ROD	ROE	NIM	TLTD	TDTA	TRTA	PTL	PTA
Mean	0.0161	0.0220	0.1242	0.0363	1.0376	0.7281	0.0399	0.0022	0.0017
Median	0.0162	0.0215	0.1244	0.0356	1.0367	0.7329	0.0401	0.0018	0.0013
Maximum	0.0186	0.0267	0.1385	0.0408	1.1264	0.7524	0.0433	0.0045	0.0034
Minimum	0.0142	0.0190	0.1068	0.0348	0.9491	0.6894	0.0359	0.0007	0.0006
Std. Dev.	0.0016	0.0027	0.0137	0.0023	0.0585	0.0223	0.0027	0.0014	0.0011
Skewness	0.4348	1.1392	-0.1108	2.0815	0.0100	-1.1151	-0.3497	0.9113	0.9353
Kurtosis	-0.0847	1.7946	-2.3195	4.5629	1.1716	1.3288	-0.6994	-0.2796	-0.3284

Note: Total observation are six years

Table 1 describes the descriptive analysis of HSBC. It can be understood for the table 1 that Return on Assets (ROA) has a mean value of 0.0080 (i.e. 0.08%) which is very low while the standard deviation is 0.0053. The mean value of Return on Deposits (ROD) is 0.0103 (i.e. 1.03%) which is also very low and its standard deviation is 0.0074. Return on Equity (ROE) have a mean value of 0.0572 (i.e. 5.72%) and standard deviation of 0.0358 which is low. Net Interest Margin (NIM) mean value is 0.0428 (i.e. 4.28%) which indicates very low interest margin while the standard deviation is 0.0054. The mean of Total Loan to Total Deposits (TLTD) is 0.6625 (i.e. 66.25%) and its standard deviation is 0.0837, Total Deposits to Total Assets (TDTA) mean value is 0.7846 (i.e. 78.46%) and its standard deviation is 0.0508, Total Revenue to Total Assets (TRTA) has a mean value of 0.0316 (i.e. 3.16%) and its standard deviation is 0.0035. The Provision to Total Loans (PTL) showed a mean value of 0.0037 (0.37%) which is very low and its standard deviation is 0.0014, while Provision to Total Assets (PTA) has a mean value of 0.0019 (i.e. 0.19%) which is also very low and standard deviation is 0.0008.

Table 2 depicts the descriptive analysis of NBO. It can be inferred for the table 2 that Return on Assets (ROA) has a mean value of 0.0161 (i.e. 1.61%) which is very low while the standard deviation is 0.0016. The mean value of Return on Deposits (ROD) is 0.0220 (i.e. 2.2%) which is also very low and its standard deviation is 0.0027. Return on Equity (ROE) has a mean value of 0.1242 (i.e. 12.42%) and standard deviation of 0.0137 which is low. Net Interest Margin (NIM) mean value is 0.0363 (i.e. 3.63%) which indicates very low interest margin while the standard deviation is 0.0023. The mean of Total Loan to Total Deposits (TLTD) is 1.0376 (i.e. 103.76%) and its standard deviation is 0.0.585, Total Deposits to Total Assets (TDTA) mean value is 0.7281 (i.e. 72.81%) and its standard deviation is 0.0223, Total Revenue to Total Assets (TRTA) has a mean value of 0.0399 (i.e. 3.99%) and its standard deviation is 0.0027. The Provision to Total Loans (PTL) showed a mean value of 0.0022 (0.22%) which is very low and its standard deviation is 0.0014, while Provision to Total Assets (PTA) has a mean value of 0.0017 (i.e. 0.17%) which is also very low and standard deviation is 0.0011.

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Comparison of Descriptive Analysis of HSBC and NBO:

It can be examined from table 1 and 2 that the mean of Return on Assets, Return on Deposits, Total Loan to Total Deposits, and Total Revenue to Total Assets of NBO is better than HSBC, while the mean of Return on Equity, Net Interest Margin, Total Deposits to Total Assets, Provision to Total Loans and Provision to Total Assets of HSBC is better than NBO.

b. Comparison of Banks Performance Based on Ratios:

Selected banks performance is analyzed by comparing the profitability, liquidity and credit performance.

i. Profitability Performance:

Return on Assets (ROA): Return on assets (ROA) is a financial ratio that shows the percentage of profit a company earns in relation to its overall resources. It is commonly defined as net income divided by total assets. An increasing trend of ROA indicates that the profitability of the company is improving. Conversely, a decreasing trend means that profitability is deteriorating.

As a rule of thumb, investment professionals like to see a company's ROA come in at no less than 5%. Of course, there are exceptions to this rule. An important one would apply to banks, which strive to record an ROA of 1.5% or above.

Table 3: Return on Assets (ROA)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.0156	0.0136	0.0030	0.0062	0.0052	0.0044
NBO	0.0157	0.0142	0.0166	0.0149	0.0168	0.0186

Table 3 indicates that HSBC has the highest ROA in the year 2010 with 0.0156 and lowest ROA in the year 2012 with 0.0030 but for NBO ROA is highest in 2015 with 0.0186 and lower in 2011 with 0.0142. The trend of ROA for NBO is showing an increasing trend from 2013 to 2015 but for HSBC it is showing a decreasing trend in the same period. This show

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that NBO is improving its profitability than HSBC in terms of ROA. It also shows that NBO has the higher ROA than HSBC in all the years. When compared to HSBC, NBO has a better ROA. It can be concluded that in majority of the year (i.e. 2010, 2012, 2014 & 2016) ROA is more than the standard ratio of 1.5% for NBO Bank. But for HSBC is only in the year 2010 it is more than the standard ratio of 1.5%.

Return on Deposits (ROD): To most financial analysts, Return on Deposit (ROD) is one of the best measures of bank profitability performance. This ratio reflects the bank management ability to utilize the customers' deposits in order to generate profits. (Tarawneh, 2006) have used this ratio as a profitability measurement. Thus higher values of return on deposits show that business is more profitable.

Table 4: Return on Deposits (ROD)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.0221	0.0165	0.0031	0.0061	0.0066	0.0072
NBO	0.0205	0.0214	0.0216	0.0190	0.0231	0.0267

Table 4 reveals that HSBC has the highest ROD in the year 2010 with 0.0221 and lowest ROD in the year 2012 with 0.0031 but for NBO ROD is highest in 2015 with 0.0267 and lower in 2013 with 0.0190. The trend of ROD for both banks is showing an increasing trend from 2013 to 2015. From the table it is clear that NBO is have more returns than HSBC in terms of ROD except in 2010 where HSBC is having more returns. When compared to HSBC, NBO has the higher ROD in all the years except in 2010. It can be concluded that ROD is better than HSBC for NBO.

Return on Equity (ROE): The return on equity ratio or ROE is a profitability ratio that measures the ability of a firm to generate profits from its shareholders investments in the company. This is an important measurement for potential investors because they want to see how efficiently a company will use their money to generate net income. ROE is also indicator of how effective management is at using equity financing to fund operations and grow the company. The higher the ROE, the better.

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Table 5: Return on Equity (ROE)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.1065	0.0984	0.0244	0.0448	0.0375	0.0313
NBO	0.1068	0.1125	0.1384	0.1311	0.1385	0.1177

It can be examined from the table 5, that HSBC has the highest ROE in the year 2010 with 0.1065 and lowest ROE in the year 2012 with 0.0244. For NBO ROE is highest in the year 2014 with 0.1385 and lower in the year 2010 with 0.1068. The trend of ROE of HSBC was decreasing trend till 2012 and after that in the year 2013 it increased then again it shows a decreasing trend after 2013. But for NBO it is a fluctuating trend from 2010 to 2015. It can be concluded that both the bank ROE is less than 1. It implies that banks have not used share capital efficiently to generate net income. When compared to HSBC, NBO is better in terms of ROE even the ratio showing less.

Net Interest Margin (NIM): Net interest income is the difference between interest income and interest expense. It is the gross margin on a bank's lending and investment activities. The higher the ratio the cheaper the funding or the higher the margin the bank is obtaining. A bank's net interest margin is a key performance measure that drives ROA (Peters, Raad & Sinkey, 2004).

It can be observed from the table 6, that HSBC has the highest NIM in the year 2013 with 0.0490 and lowest NIM in the year 2012 with 0.0336. NIM for HSBC showed a decreasing trend till 2012 but in the year 2013 it had increased again and from 2014 it showed a decreasing trend.

Table 6: Net Interest Margin (NIM)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.0467	0.0443	0.0336	0.0490	0.0421	0.0409
NBO	0.0408	0.0348	0.0351	0.0361	0.0348	0.0361

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The trend is almost similar for NBO but except in 2015 it showed increasing trend. NIM for NBO is highest in 2010 with 0.0408 and lower in 2011 and 2014 with 0.0348. It can be inferred that both the bank NIM is low. When compared to NBO, HSBC is better in terms of NIM in almost all the years except in the year 2012. It can also be concluded that both the banks have lower ratio indicating margin of interest is lower.

Overall it can be observed that profitability performance of NBO is better than HSBC.

ii. Liquidity Performance:

Total Loan to Total Deposits (TLTD): Total Loan to Total Deposit is the most important ratio to measure the liquidity condition of the bank. Bank with Low TLTD is considered to have excessive liquidity, potentially lower profits, and hence less risk as compared to the bank with high TLTD. However, high TLTD indicates that a bank has taken more financial stress by making excessive loans and shows risk that to meet depositors' claims bank may have to sell some loans at loss.

Table 7: Total Loan to Total Deposits (TLTD)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.8019	0.6880	0.6451	0.5469	0.6269	0.6663
NBO	1.0290	1.0444	1.0131	0.9491	1.0639	1.1264

It clear from the table 7, that HSBC has the highest TLTD in the year 2010 with 0.8019 and lowest TLTD in the year 2013 with 0.5469. TLTD for HSBC showed a decreasing trend till the year 2013 but from there it started to increase. But for NBO it is highest in 2015 with 1.1264 and lower in 2013 with 0.09491. When compared to NBO, HSBC has the lowest TLTD. It can be concluded that HSBC has less risk than NBO. It shows that NBO has more financial stress by making excessive loans.

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Total Deposits to Total Assets (TDTA): Like TLTD, Total Deposits to Total Assets (TDTA) is also another important ratio that measures the liquidity condition of the bank. Whereas TDTA is a ratio in which liquidity of the bank is measured in terms of its deposits, TDTA measures the percentage of assets that are tied up in deposits. The higher is the ratio the less the liquidity is for the bank. Similar to TDTA, the bank with low TDTA is also considered to be more liquid as compared to the bank with higher TDTA. However, high TDTA is an indication of potentially higher profitability and hence more risk.

Table 8: Total Deposits to Total Assets (TDTA)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.6896	0.7985	0.7674	0.8072	0.8259	0.8193
NBO	0.7341	0.7177	0.7435	0.7524	0.7317	0.6894

Table 8 clearly portrays that HSBC has the highest TDTA in the year 2014 with 0.8259 and lowest TDTA in the year 2010 with 0.6896. For NBO TDTA is highest in 2013 with 0.7524 and lower in the year 2015 with 0.6894. The trend of TDTA of HSBC was fluctuating till 2013 and after that it showed an increasing trend. But for NBO it shows a two year fluctuating trend for from 2010 to 2015. It can be concluded that both the banks TDTA is high indicating high profitable and more risk. But when compared to NBO, HSBC is having high ratio, this shows that HSBC is earning high profits but has more risk. It can also be concluded that the both banks have weak liquidity position.

iii. Credit Performance:

Total Revenue to Total Assets (TRTA): This ratio measures how efficiently a firm uses its assets to generate revenue, so a higher ratio is always more favorable. Higher ratios mean the company is using its assets more efficiently. Lower ratios mean that the company isn't using its assets efficiently.

It can be revealed from the table 9, that HSBC has highest TRTA in year 2010 with 0.0347 and lower in the year 2012 with 0.0251 whereas NBO has highest in the year 2010 with 0.0433 and lowest in the year 2013 with 0.0359. HSBC showed a decreasing trend till 2012

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and after that it showed an increasing trend till 2015. NBO showed a decreasing trend till 2013 and then has an increasing trend. When compared, NBO TRTA is better than HSBC. Over all the ratio is less for both the bank. It shows that both the banks are not using its assets efficiently to generate revenue.

Table 9: Total Revenue to Total Assets (TRTA)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.0347	0.0337	0.0251	0.0309	0.0317	0.0334
NBO	0.0433	0.0414	0.0389	0.0359	0.0384	0.0416

Provision to Total Loan (PTL):

Table 10: Provision to Total Loan (PTL)

Bank	2010	2011	2012	2013	2014	2015
HSBC	0.0059	0.0045	0.0039	0.0023	0.0025	0.0029
NBO	0.0033	0.0045	0.0018	0.0017	0.0012	0.0007

Table 10 shows that HSBC has the highest PTL in the year 2010 with 0.0059 and lowest PTL in the year 2013 with 0.0023 but for NBO PTL is highest in 2011 with 0.0045 and lower in the year 2015 with 0.0007. The trend of PTL for HSBC is showing a decreasing trend from 2010 to 2013 and started to increase after 2013. But for NBO it is showing a decreasing trend from 2011 to 2015. The ratio is very low for both the banks. When compared to HSBC, NBO has the lower ratio in all the years. It can be concluded that both the banks are having very less non-performing loans, which increased the net income and earnings per share.

c. Correlation Analysis of Variable between HSBC and NBO:

From the table 11, it can be understood that there is a positive correlation for Net Interest Margin, Total Loan to Total Deposits, Total Revenue to Total Assets, Provision to Total Loans and Provision to Total Assets between HSBC and NBO and for Return on Assets, Return on Deposits, Return on Equity and Total Deposits to Total Assets there is a negative correlation between the two banks.

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Table 11: Correlation Analysis of Variable between HSBC and NBO

Ratios		2010	2011	2012	2013	2014	2015	Correlation	Result
ROA	**HSBC**	0.0156	0.0136	0.0030	0.0062	0.0052	0.0044	**-0.60**	**Negative**
	NBO	0.0157	0.0142	0.0166	0.0149	0.0168	0.0186		
ROD	**HSBC**	0.0221	0.0165	0.0031	0.0061	0.0066	0.0072	**-0.25**	**Negative**
	NBO	0.0205	0.0214	0.0216	0.0190	0.0231	0.0267		
ROE	**HSBC**	0.1065	0.0984	0.0244	0.0448	0.0375	0.0313	**-0.82**	**Negative**
	NBO	0.1068	0.1125	0.1384	0.1311	0.1385	0.1177		
NIM	**HSBC**	0.0467	0.0443	0.0336	0.0490	0.0421	0.0409	**0.43**	**Positive**
	NBO	0.0408	0.0348	0.0351	0.0361	0.0348	0.0361		
TLTD	**HSBC**	0.8019	0.6880	0.6451	0.5469	0.6269	0.6663	**0.37**	**Positive**
	NBO	1.0290	1.0444	1.0131	0.9491	1.0639	1.1264		
TDTA	**HSBC**	0.6896	0.7985	0.7674	0.8072	0.8259	0.8193	**-0.29**	**Negative**
	NBO	0.7341	0.7177	0.7435	0.7524	0.7317	0.6894		
TRTA	**HSBC**	0.0347	0.0337	0.0251	0.0309	0.0317	0.0334	**0.56**	**Positive**
	NBO	0.0433	0.0414	0.0389	0.0359	0.0384	0.0416		
PTL	**HSBC**	0.0059	0.0045	0.0039	0.0023	0.0025	0.0029	**0.74**	**Positive**
	NBO	0.0033	0.0045	0.0018	0.0017	0.0012	0.0007		
PTA	**HSBC**	0.0033	0.0025	0.0019	0.0010	0.0013	0.0016	**0.75**	**Positive**
	NBO	0.0025	0.0034	0.0014	0.0012	0.0010	0.0006		

Findings:

1. In majority of the year (i.e. 2010, 2012, 2014 & 2016) ROA is more than the standard ratio of 1.5% for NBO Bank. But for HSBC is only in the year 2010 it is more than the standard ratio of 1.5%.
2. NBO has better ROD than HSBC.
3. NBO is better in terms of ROE even the ratio.
4. Both the banks have lower ratio indicating margin of interest is lower.
5. NBO has more financial stress by making excessive loans.
6. Both banks have weak liquidity position.
7. Both the banks are not using its assets efficiently to generate revenue.
8. Both the banks are having very less non-performing loans, which increased the net income and earnings per share.

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Recommendation and Conclusion:

The study measured the performance of NBO and HSBC in term of profitability, Liquidity and Credit performance for a period of 6 years from 2010 to 2015. The results showed that NBO performed better than HSBC in term of profitability performance. In term of liquidity performance, TLTD is better for HSBC whereas TDTA for both the banks have very low ratio. It showed that the liquidity performance of both the banks is not satisfactory. Credit performance too showed a dissatisfactory performance. It is recommended that liquidity and credit performance of both the banks have to improve for better financial performance of the banks.

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