Comparative Financial Statement Analysis of Microfinance Banks in Pakistan

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Abstract

This study is aimed at comparative financial statement analysis of microfinance banks in Pakistan. Although financial literature exists covering financial analysis on microfinance banks in Pakistan, comparative financial analysis has not been attempted. This study is an effort to fill the gap. In Pakistan, several microfinance institutions are converted into microfinance banks. Currently, ten microfinance banks are operating in Pakistan. Financial analysis has been performed in sustainability, profitability, asset/liability management, portfolio quality, efficiency, and productivity by computing appropriate formula-based ratios and conducting the comparative study. As such, it also provides a trend analysis of the performance of microfinance banks. The data was obtained from the State Bank of Pakistan's official website and the microfinance banks' annual reports from 2010 to 2015. The comparative financial statement analysis results indicate improvement and growth, particularly in 2014 and 2015, when indicators show positive trends.

Keywords: Microfinance Banks, Sustainability, Outreach, Profitability, and Financial Statements.

INTRODUCTION

Poverty alleviation has always been a concern in the developing countries where the distribution of resources among the population leaves a much wider gap between haves and have-nots with the result that a much larger population lives below the poverty line. The severity of the problem was noticed and realized at world forums such as World Bank, which took the initiative and organized a Consultative Group to Assist the Poor (CGAP), the United States Agency for International Aid (US AID), and the United Nations Development Program (Mbeba 2008). These institutions structured several packages to provide relief to the poor, mainly in the developing countries. The programs comprised food support, health, sanitation, education, and infrastructural support, which indirectly benefit the poor (Pakistan Microfinance Review 2015). Substantial funds were accumulated in donations from several donor organizations, and these funds were channelized through government and non-government organizations (NGOs). The term 'microfinance' was coined since the objective was to ensure that the funds reach the individual households as a micro-level economic unit. The Microfinance Information Exchange (MIX, 2016) has defined microfinance as "the practice of providing financial services in very small increments to the working poor."

Microfinance evolved as a significant step in poverty alleviation and became popular mainly in the developing economies. Generally, poverty has been defined in absolute poverty and relative poverty (Chen and Ravallion, 2007). As defined by the World Bank, the absolute poverty is the condition where someone is living on less than US$1.25 per day, and this condition is referred to as extreme poverty. Another measure to define moderate poverty is US$2 a day. The concept of relative poverty is further expanded to include income perspective, basic needs perspective, and capability (empowerment) perspective (Foster, 1998).

The concept of microfinance was originally initiated informally by non-government organizations (NGOs) that soon culminated in more formal Micro Finance Institutions (MFIs). The current form of microfinance is microfinance banks, which receive deposits and give loans to poor people. The loans are given to the poor people who naturally possess the entrepreneurial capability but could not access the conventional banks to obtain loans simply because these poor people lack adequate collateral to offer as security. A microfinance bank is a commercial bank licensed under the Microfinance Institutions Ordinance 2001 to service the microfinance market exclusively and is prudentially regulated by the State Bank of Pakistan. Although microfinance is predominantly relevant within developing countries where the proportion of poor and unemployed is high, it is well-practiced in developed countries such as the USA and Canada.

The idea of microfinance quickly spread like bushfire the world over. The developing countries that have poverty in large proportions were quick to adopt microfinance in letter and spirit. Still, the developed countries were also active in setting up formal microfinance institutions for the poor. Initially, the prime source of funds was charity and donations. With the unprecedented growth in outreach, and the enormous demand for microfinance, the question of continuity in the availability of funds became a severe concern for the microfinance institutions. This was the time when the concept of sustainability surfaced, and the idea of self-financing was advocated. This caused the transition from microfinance institutions to microfinance banks. Today, more formal microfinance banks work on conventional banks' pattern as they accept deposits and charge a high-interest rate to cover finance costs and meet operating costs.

The transition to microfinance banks was to achieve sustainability to expand outreach, ultimately leading to poverty alleviation. However, the literature available discusses the subject of microfinance in totality and leaves much to be desired. This

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study provides a comparison between microfinance banks for significant indicators specifically.

This study is an attempt to analyze the financial statements of microfinance banks in Pakistan to highlight and compare the performance in terms of significant financial indicators relevant to microfinance banks. This study is an effort to explore the linkage between sustainability and outreach in alleviating poverty in Pakistan.

LITERATURE REVIEW

The significance of financial analysis was highlighted by Sultan (2014), stressing a better understanding of an organization's "stability, viability and profitability." Accounting ratios such as Return on Assets (ROA) and Return on Equity (ROE) were used to assess the Baghdad Soft-Drinks Industry's performance during 2004-2013. The study revealed declining trends in the business of soft drinks, mainly attributed to political instability. Financial statement analysis of agricultural bank for rural development was conducted by Masoud and Badugu (2015). It was stated that financial statements analysis helps identify the liquidity situation, long-term solvency, financial feasibility, and prosperity of a firm. Financial ratio analysis shows whether the firm is performing well or not in past years. It helps the investors decide which firm the threat is less or maximum benefit can be earned. Before deciding on investing in a company, one must study its financial status and worth cautiously. The study is conducted from 2010-2011, and the various amount was calculated. Based on that comparative statement analysis position, the bank has a strong solvency position as all the solvency development plays a prominent role in India's rural area. This bank mostly plays a perfect role in rural development and agriculture.

The cost-efficiency of Philippine commercial banks was examined by Manlagnit (2011) by using stochastic frontier analysis and specifically incorporating risk and asset quality measures in the estimation. The results show substantial inefficiencies among domestic banks, and that risk and asset quality affect the efficiency of banks. The significant increase in the cost inefficiency could be attributed to the adverse effects of the 1997 Asian financial crisis and the subsequent costs of banking reforms and regulatory changes enacted to stabilize and strengthen the sector. The instabilities, particularly the banking crisis, could have distorted banks' incentive structure, making resource allocation to achieve efficiency a more difficult task. This study highlights the economic importance of encouraging increased efficiency in the banking sector by tapping the potential for significant improvements in the banks' cost-efficiency.

The need to formulate and implement financial reporting standards for microfinance institutions was highlighted by Tulchin, Sassman, and Wolkomir (2009). The standards “promote transparency, facilitates comparability, improves decision-making, and increases investment by making it easier to observe and understand an MFI’s financial health." The ratios indicated include capital adequacy ratio, uncovered capital ratio, foreign currency risk ratio, the yield on liquidity and investment ratio, savings liquidity, the effective financial expense of savings, effective operating expense of savings, and average deposit balance per account.

The disclosure of financial ratios in the annual reports of Turkish firms listed at the Istanbul Stock Exchange was examined by Kilic and Merve (2012) using count data regression models (Poisson and Negative Binomial) to test the hypothesis. The multivariate analysis results indicated that firm size, auditor size, profitability, and ownership diffusion have a significant positive association with voluntary disclosure level of financial ratios, while leverage does not.

A study on mission drift by Mersland and Øystein (2010) suggests that “this selection bias can come not only through an increase in the average loan size, which allows for financially stronger individuals to get the loans, but also through MFI's particular lending methodology, main market of operation, or even the gender bias as further mission drift measures. And as it may follow, this selective funding would lead to lower risks and lower costs for the firm”.

The financial performance of firms listed at the Pakistan Stock Exchange was reviewed by Mirza and Javed (2013) in the context of economic indicators, corporate governance, ownership structure, and risk management by using the fixed-effect model and found a positive relationship between firms performance and corporate governance while mixed results were observed for other determinants impacting profitability.

The growth and performance of microfinance in Pakistan was examined by Rauf and Mahmood (2009) within the context of six dimensions of outreach, asserted that the “breadth of outreach is below the targeted outreach, depth of outreach is concentrated in big urban cities, the scope of outreach is mostly limited to credit. The sector's financial performance is weak, its cost per borrower is increasing, and productivity ratios are low. The sector's growth is being led by a few unsustainable institutions that are neither operationally nor financially self-sufficient.

A study to analyze three listed firms' financial statements in the education sector was conducted by Tugas (2012) for the period 2009-2011 by using liquidity ratios, activity ratios, leverage ratios, and market value ratios. The assertion was made that risks tend to prevent firms from achieving objectives and, therefore, the need to structure the scientific bases of decisions is likely to reduce the risks. The financial statement analysis is considered as one of these structured and scientific bases in financial management. Financial performance ranked the firms.

RESEARCH METHODOLOGY

Research Methodology is the mechanism to research the right direction to achieve the stated objectives and find a solution to the problem outlined. The approaches to problem-solving vary depending on the nature of the research. It could be quantitative, qualitative, and \ or a mixture of the two. Although research could be qualitative in finance, quantitative research is widely used to conduct the test and draw results. Research methodology describes the methods used, and the collection of data techniques. It also provides a brief introduction of the variables used and the proxies used to measure the variables.

The data for the financial analysis of microfinance banks have been collected from the data warehouse of State Bank of Pakistan and the published annual reports of the banks. As such, it is secondary data. The period selected for the study is the years 2010 and 2015.

The financial analysis is mainly quantitative, and it is conducted based on well- known accounting and financial ratios. The total number of microfinance banks in Pakistan is ten. However, more microfinance banks are in the pipeline for the establishment, and these are in various stages of progress. The State Bank of Pakistan is the main source for obtaining quantitative data relating to microfinance banks.

Comparative Financial Analysis

The comparative financial analysis is conducted of the microfinance banks as under:

Return on Assets (ROA)

The ratio 'return on assets' indicates how well a microfinance bank has utilized its assets to generate returns. The computation excludes non-operating items and donations.

Table 1: Return on Assets

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	-7.65	-13.20	-14.34	13.80
APNA	-7.33	-6.53	-6.05	-4.06	0.35	-0.52
FINCA	-14.19	-10.04	-6.45	0.03	2.76	1.97
KHUSH	2.41	1.54	1.69	2.73	4.21	3.09
NRSP	-38.03	0.87	2.63	2.49	1.68	3.21
Pak Oman	3.27	0.68	-0.20	-3.24	-0.65	0.51
Tameer	4.72	1.62	2.80	2.51	4.32	4.04
First	-2.67	-1.34	-0.77	1.50	1.02	2.56
U	-3.08	7.38	-1.55	-3.26	-5.29	0.35
Waseela	0	-5.16	-2.98	-11.29	-4.21	-0.76

Source: State Bank of Pakistan

The return on assets indicates low performance during the period 2010 to 2013. Khushhali Micro Bank and Tameer Micro Bank have reported positive and steady returns during the period under study. Other microfinance banks have generally reported negative returns during 2010-2015. However, improvement in the return on assets ratio is apparent during 2015, where microfinance banks have indicated positive results, except APNA and Waseela continue to show negative results.

Return on Equity (ROE)

This ratio indicates the rate of return on equity for a given period. The numerator is net operating income after tax, and it does not include donations or non-operating items. As such, it is used as an indicator of commercial viability.

Table 2: Return on Equity

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	-8.61	-15.78	-16.24	16.54
APNA	-8.39	-6.96	-31.51	-51.68	0.68	-1.48
FINCA	-49.71	-71.08	-14.54	0.03	4.18	2.78
KHUSH	7.86	6.49	6.79	13.21	21.40	20.95
NRSP	61.51	4.26	14.39	17.90	9.69	18.58
Pak Oman	3.48	0.72	-0.21	-3.45	-0.68	0.54
Tameer	18.84	9.22	20.49	17.40	25.11	23.28
First	-22.63	-12.02	-6.64	13.14	9.21	21.08
U	-3.11	6.44	-1.55	-4.23	-10.02	0.75
Waseela	0	-5.23	-3.37	-26.03	-10.32	-3.73

Source: State Bank of Pakistan

A review of the return on equity table indicates that Khushhali Micro Bank, NRSP, and Tameer Micro Bank show positive returns throughout the period under study. Other micro banks generally indicate negative returns for most of the period. However, Advance Micro Bank and First Micro Bank show significant results in 2015 at 16.54% and 21.08%, respectively, while APNA and Waseela show negative results during the period.

Portfolio to Assets

This ratio is an indication of the allocation of assets of microfinance banks to their lending activity. It also indicates management's ability to allocate resources to its primary and most profitable activity of providing microloans to the community.

Table 3: Portfolio to Assets

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	0	5.54	15.89	32.20
APNA	19.61	1.33	14.95	24.29	43.56	45.65
FINCA	35.04	47.69	53.88	50.75	62.61	64.11
KHUSH	50.03	50.69	57.44	65.89	72.52	64.60
NRSP	0.00	50.45	47.70	48.91	43.44	62.90
Pak Oman	14.19	16.27	18.41	15.52	19.82	31.82
Tameer	57.69	61.03	50.10	54.71	54.55	57.58
First	34.97	31.08	35.96	36.27	41.38	45.34
U	0.29	1.97	0.04	2.97	18.78	40.20
Waseela	0	0.00	0.05	9.27	19.59	27.43

Source: State Bank of Pakistan

There is a significant improvement in advances as a percentage of total assets from FINCA, Khushhali, NRSP, and Tameer Microfinance Banks during 2014 and 2015. Other microfinance banks that include APNA, Pak Oman, First and U Microfinance Banks indicate low results from 2016 to 2017 and report improvements in 2020 and 2021.

Gross Advances to Borrowings and Deposits

This ratio indicates the relationship of gross advances to borrowings and deposits.

Table 4: Gross Advances to Borrowings and Deposits

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	0	421.15	701.18	1379.28
APNA	212.28	43.46	26.89	44.86	66.92	58.38
FINCA	58.36	61.66	66.72	74.43	82.94	88.76
KHUSH	76.55	75.85	82.34	89.68	98.60	81.34
NRSP	0	67.84	62.45	59.99	55.45	79.61
Pak Oman	393.75	488.95	522.58	484.74	1011.53	1485.36
Tameer	85.61	80.30	68.63	74.86	71.85	77.30
First	44.42	40.66	43.96	43.14	49.56	54.72
U	1.60	32.08	13.69	20.17	49.32	86.30
Waseela	0	0	0.58	27.63	38.85	42.23

Source: State Bank of Pakistan

The ratio of gross advances to borrowings plus deposits indicates steady performance during the period 2016 to 2021. The Advance Microfinance Bank shows a significant ratio of 1379.28 percent, attributed to a 96.6 percent increase in advances in 2015. The Pak Oman microfinance bank indicates a significant ratio of 1485.36 percent, attributed to a 64.9 percent increase in advances during 2021.

Debt to Equity

It measures microfinance banks' overall leverage and how much cushion it has to absorb losses after all liabilities have been settled.

Table 5: Total Liabilities to Total Equity

Microbank	2016	2017	2018	2019	2020	2021
Advance			11.07	16.34	8.29	13.54
APNA	12.60	6.20	62.02	60.63	69.15	81.39
FINCA	67.25	82.88	86.56	72.24	79.90	77.12
KHUSH	69.34	71.22	74.99	79.24	80.31	85.20
NRSP	106.00	78.03	79.99	85.19	81.98	82.21
Pak Oman	6.14	6.36	6.23	6.86	4.10	4.68
Tameer	74.40	82.18	86.22	85.46	82.65	82.48
First	88.15	88.67	88.06	88.35	88.41	87.33
U	22.59	8.58	2.62	24.81	47.78	53.85
Waseela	0	1.42	11.37	40.21	59.21	78.56

Source: State Bank of Pakistan

The total liabilities ratio to total equity indicates low leverage for Advance Microfinance Bank and Pak Oman Microfinance Bank, which is 13.54 percent and 4.68 percent, respectively. All other microfinance banks indicate high leverage of around 80 percent.

Cash and Cash Equivalent to Total Assets

It indicates how much cash and cash equivalents an institution maintains to cover short-term liabilities.

Table 6: Cash and Cash Equivalent to Total Assets

Microbank	2016	2017	2018	2019	2020	2021
Advance			92.05	59.43	43.58	38.18
APNA	5.08	2.35	54.21	43.21	33.81	35.21
FINCA	39.77	26.18	25.43	28.38	14.39	9.07
KHUSH	10.29	12.77	12.81	6.99	6.32	7.29
NRSP	1.65	40.92	21.76	19.48	16.92	15.55
Pak Oman	3.40	2.55	2.28	1.68	0.71	2.12
Tameer	23.42	21.44	12.42	11.82	12.74	12.85
First	13.25	15.54	15.99	16.01	11.54	13.68
U	47.13	1.94	93.78	52.87	28.77	30.48
Waseela	0	93.46	11.04	56.17	50.23	54.52

Source: State Bank of Pakistan

The ratio of cash and cash equivalent to total assets indicates a significantly low ratio for Pak Oman Microfinance Bank at 2.12 percent. Advance Microfinance Bank, APNA Microfinance Bank, U Microfinance Bank, and Waseela Microfinance Bank indicate significantly high ratios above 30 percent, with Waseela indicating a 54.52 percent ratio.

Write-off Ratio

It is the percentage of an institution's loans that have been removed from the balance of the gross loan portfolio because they are unlikely to be recovered. The write-off policies may vary depending on the size of the loan and the clients' credit history. The formula is given below:

Table 7: Write-off Ratio

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	0	100.00	169.83	126.16
APNA	140.65	376.50	6.19	129.46	60.17	45.66
FINCA	141.62	78.20	137.83	96.66	139.32	175.85
KHUSH	112.23	162.87	321.87	164.98	119.09	126.66
NRSP	0	103.19	54.28	119.91	93.03	165.08
Pak Oman	138.40	222.99	233.36	1105.78	105.86	174.69
Tameer	49.99	-112.50	187.12	261.67	291.65	131.94
First	147.55	51.88	129.30	121.22	173.71	63.81
U	409.68	81.82	161.44	106.14	86.51	76.50
Waseela	0	0	100.00	99.40	61.12	66.64

Source: State Bank of Pakistan

Risk Coverage Ratio

It indicates how much of the portfolio at risk is covered by the institution's impairment loss allowance.

Table 8: Risk Coverage Ratio (%)

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	0	88.76	95.29	87.61
APNA	37.91	55.37	26.17	24.86	32.09	55.35
FINCA	151.89	98.44	113.70	127.45	93.96	47.55
KHUSH	68.99	102.30	138.81	147.18	97.35	51.41
NRSP	0	0	294.91	360.71	130.88	594.47
Pak Oman	44.26	37.26	28.16	26.21	34.35	31.67
Tameer	345.63	46.39	21.81	41.27	53.28	106.47
First	113.96	346.24	187.09	155.92	170.62	128.11
U	8.09	4.35	50.00	1554.55	885.77	153.19
Waseela	0	0	0	0	37000.00	0

Source: State Bank of Pakistan

Efficiency and Productivity:

Earnings per Share

It is an indicator of the earnings against one ordinary share of a microbank. The formula for computation is given below:

$$\frac{\text{Net Income} - \text{Tax}}{\text{Number of Shaes}}$$

Table 9: Earnings Per Share

Microbank	2016	2017	2018	2019	2020	2021
Advance	0	0	-0.79	-1.25	-1.11	0.97
APNA	-0.62	-0.48	-1.64	-1.78	0.06	-0.13
FINCA	-2.32	-1.94	-0.84	0.00	0.37	0.26
KHUSH	1.02	0.89	0.98	2.13	4.12	4.83
NRSP	- 230.31	0.42	1.67	2.44	1.32	3.07
Pak Oman	0.32	0.07	-0.02	-0.32	-0.06	0.05
Tameer	1.85	1.00	2.78	2.83	5.26	6.32
First	-1.71	-0.84	-0.47	1.06	0.81	2.31
U	-0.20	0.44	-0.15	-0.38	-0.82	0.06
Waseela	0	-0.50	-0.31	-1.90	-0.74	-0.26

Source: State Bank of Pakistan

The overall financial and non-financial highlights provided by Pakistan Microfinance Review for the year 2015 is given below which is indicative of the significant improvement made in the direction of borrowers, gross loan portfolio, active woman borrowers, branches, total staff, total assets, deposits, total debt, total revenue, and finally it shows improvement in operating and financial self-sufficiency while decline in the portfolio at risk as measured by PAR>30 percentage.

Table 10: Microbanks Consolidated

Year	2016	2017	2018	2019	2020
Active Borrowers (in millions)	1.7	2. 0	2.4	2.8	3.6
Gross Loan Portfolio (in billions)	24.8	33.1	46.6	61.1	90.2
Active Women Borrowers (in millions)	0.9	1.3	1.4	1.6	2.0
Branches	1.550	1.46	1.60	1.747	2.754
Total Staff	14,202	14,64	17,45	19,88	25,56
Total Assets (billions)	48.6	61.9	81.5	100.7	145.1
Deposits (billions)	13.9	20.8	32.9	42.7	60.0
Total Debt (Billions)	38.3	24.9	26.9	31.1	44.5
Total Revenue (billions)	10.1	12.5	17.3	24.3	32.8
OSS (percentage)	108.4	109.5	118.1	120.6	124.1
FSS (percentage)	100.5	107.5	116.5	119.6	121.0
PAR>30 (percentage)	3.2	3.7	2.5	1.1	1.5

Source: Pakistan Microfinance Review 2021

Conclusion

The comparative financial analysis of microfinance banks in Pakistan from 2016 to 2021 indicates improvement worldwide, particularly in 2020 and 2021, as evidenced by the analysis. The share of microfinance banks of the total microfinance market was 42 percent in the year 2020. It was reported by Pakistan Microfinance Review (2015) that the share of microfinance banks was 39 percent of the total microfinance market in 2021. The microfinance banks account for 61 percent of the microfinance industry's gross loan portfolio, mainly due to larger loan sizes than other forms of microfinance institutions. As reported by Pakistan Microfinance Review (2015), the total gross loan portfolio for the microfinance industry stood at PKR90.1 billion, out of which microfinance banks share stood at PKR55.4 billion. The microfinance banks have a 25 percent ratio when the depth of outreach is measured through proxy indicator: average loan balance per borrower in proportion to per capita Gross National Income (GNI) while 20 percent is assumed to mean that the microfinance provider is poverty focused. As for gender classification, microfinance banks have 24 percent woman borrowers (Pakistan Microfinance Review 2015).

The number of depositors also increased from 5.7 million in 2014 to 10.6 million in 2015, signifying an increase of 88 percent. The Tameer Microfinance Bank has emerged, having 4.95 million depositors (Pakistan Microfinance Review 2015). However, credit

growth continues to outpace the growth in deposits, leaving little choice for the microfinance banks and meeting their funding needs through a combination of debt and deposits.

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