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# AN APPRAISAL OF THE PERFORMANCE OF TWO (2) DEVELOPMENT FINANCIAL INSTITUTIONS (DFIS) IN MALAYSIA

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## ABSTRACT

*This paper aims to assess the financial performance of two (2) Development Financial Institutions (DFIs) in Malaysia namely; Bank Simpanan Nasional or National Savings Bank (BSN) and Bank Kerjasama Rakyat Malaysia or Cooperative Bank (BR) for a period of 5 years spanning from 2006 to 2010. The DFIs are specialized financial institutions established by the government to achieve the socio-economic development objectives of the country through developing and promoting the key strategic sectors of the economy. In this study, we employed most commonly used financial ratio tools on a sample of two (2) development financial institutions to evaluate their performances so as to indicate how well they are prepared to meet the socio-economic development objectives of the country. To the best of our knowledge, related study assessing the performance of DFIs in Malaysia is scant. Thus realizing from the scarcity of studies on this component of financial system particularly in the case of Malaysia, we consider the present effort to be worthy addition to the existing literature in this line. To achieve our objectives, we used data and other relevant information collected from the annual reports of individual Development Financial Institutions under consideration. In addition, we also utilized Annual Reports of Bank Negara Malaysia or Central Bank of Malaysia (BNM-AR). The results showed that the financial health of the two DFIs under this study is sound but comparatively Bank Rakyat (BR) is in better position than its peer Bank Simpanan Nasional (BSN). The sound financial health also indicates the potential ability to cater the financial needs of the strategic sector of the economy towards achieving the socio-economic development objectives of the country.*

**Keywords:** *Development Financial institutions, financial ratio, economic development.*

## 1.0 INTRODUCTION

The financial system in Malaysia plays important role in the economic development process of Malaysia through mobilizing financial resources and channeling them to meet the financial needs of various economic sectors. The importance of the financial system in providing financial resources to influence economic activities could be better indicated by its size in terms of assets and its supports for the financing needs of the economy. Recent statistics provided at Bank Negara Malaysia Annual Report 2010 (BNM-AR 2010) show that the total assets of the financial system in 2009 were RM2,749.71 billion which expanded by 10.17% to RM 3,029.38 billion in 2010. As at end-2010 total assets of the financial system were equivalent to 395.5% of Gross Domestic Product (GDP) [404.6% in 2009]. About RM2,080.64 billion or 68.7% of the total assets in the form of securities, loans and advances were channeled to support the economic activities in 2010. This figure represents an increase of 12.16% from the previous period. This shows that the financing activities of the financial system grew at a faster rate as compared to it its total growth of total assets. Development Financial Institutions (DFIs) as a group is one of the important components of the financial system. They also play vital role in achieving the development objectives of the country through mobilizing resources and channeling them into the economy. BNM-AR 2010 reports that the total assets of the DFIs were RM165.92 billion in 2009 and it

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grew by 12.28% to RM186.29 billion in 2010. This figure represents an equivalent to 25.1% of GDP in 2010. To support the financial needs of the economic activities, DFIs channeled over RM145.5 billion in the form of loans and advances; and investment in securities in 2010 which represents an increase of 14.7% from RM126.8 billion in 2009. This shows that the financing activities of DFIs also grew at a faster rate than the growth of DFIs total assets.

The DFIs in Malaysia was founded by the government with specific mandate to develop and promote some key sectors that are considered to be most vital and strategically important for overall socio-economic development objectives of the country[2]. It is generally acknowledged that a sound and well-structured financial institution is more efficient and effective in providing financial services to facilitate the economic activities than a diluted financial institution which may adversely affect the economic activities and hence can retard the economic growth. Given the roles of the financial system in the economy in general and the DFIs in particular, in this paper we aim to examine the financial performance for a sample of two (2) DFIs over a period of 5 years ranging from 2006 to 2010 and compare the relative financial strength and potential ability towards fulfilling their commercial commitment and the socio-economic development target of the country. We have chosen these two institutions from a total of 13 DFIs as listed in the BNM-AR 2010 (Annex, P12). This is an initial effort to diverse the traditional trend of research in analyzing the financial performance from banking institutions to focus on non-banking financial institutions such as DFIs. The study hopes that more research in this line of institutions will be followed in the future. The rest of the paper is structured as follows: Section 2 briefly highlighted some of the previous studies that have evaluated the financial performance of banking institutions (Islamic or Conventional) using different measures including financial ratio tools. In section 3, we gave a brief introduction of the two (2) selected DFIs. Section 4 discussed the types of ratio tools selected for our interest in this study and section 5 analyzed the results derived from the ratio calculation. Concluding remarks are provided in section 6.

## 2.0 RELATED LITERATURE

There are a number of studies available evaluating the performance of financial institutions particularly banking institutions. Virtually all studies focused either on conventional banks or Islamic banks or made comparisons between the performance of Islamic banks and conventional banks. Some commonly and extensively used approaches to analyze the financial performance of the banks (e.g., in terms of efficiency, profitability, risk and solvency, productivity, commitment to development and so on) are the traditional financial ratio analysis approach; data envelopment analysis (dea) approach, and the stochastic frontier approach (sfa). Some of the frequently cited studies who used traditional financial ratio analysis approach to evaluate the financial performance of banks (such as Islamic banks or conventional banks or Islamic Vs. conventional banks) are; Rosely, S. A. & Mohd. Afandy (2003); Samad, A. & Hassan, M.K., (1998); Samad, A., (1999); Akkas, Ali. (1996); Arif, Mohammad. (1989); Sarker, M.A., (1999); Bader, M.K., Shamser, M., and Taufiq, H., (2007); Hassan, M. K., and Bashir, A. M., (2003); and Hamid, M. A., & Azmi, S. M., (2011). Some studies used data envelopment analysis (also known as deterministic and non-parametric approach) to assess the efficiency of the banks (Islamic or conventional banks or Islamic Vs. conventional banks). Few of these studies in this line are Bader, Shamsher and Taufiq (2007); Boss and Kool (2006); Yudistria (2003); and Drake *et. al.* (2006) etc. Some studies are also found used stochastic frontier analysis (also known as stochastic and parametric approach) to analyze the efficiency of banks particularly in terms of cost and profitability. Weill (2004); Kraft, E., and Tirtiroglu, D., (1998); and Shamsher, M., Taufiq, H., and Bader, M. K. (2008) are few of them.

It is interesting to observe that all the previous literature as highlighted above concentrated their focus either on the conventional banks or Islamic banks or made comparative analysis between conventional and Islamic banks. Furthermore, to the best of our knowledge, there is no such study attempted to assess the performance of the development financial institutions particularly the performance of the two institutions that we are considering in this study. As such, this study is considered to be a new effort to add to the existing studies in this area as highlighted above. This study is thus different from others particularly with respect to the selected institutions that are not covered and evaluated elsewhere in Malaysia. We utilized the most commonly traditional financial ratio approach to assess the performance of these two (2) DFIs. Ratios are calculated based on the year end data provided in the Balance sheet and income statements of the Annual Reports of the respective institutions. The results from this study provided valuable information about the financial health of the 2 institutions, which can be beneficial for the managers of the concerned institutions, investors, depositors and the policy-makers at large.

[2] These strategic sectors include agriculture, small and medium enterprises (SMEs), infrastructure, maritime, export oriented sector as well as capital-intensive and high-technology industries.

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## 3.0 DEVELOPMENT FINANCIAL INSTITUTIONS (DFIs)

There are 13 institutions categorized as DFIs in BNM Annual Report (BN-AR 2010, Annex: Table A-15 & 16). However, for our purpose in this research we are focusing only on two (2) of them. They are, (a) Bank Simpanan Nasional or National Savings Bank (BSN); and (b) Bank Kerjasama Rakyat Malaysia Berhad or Cooperative banks or shortly Bank Rakyat (BR). The choice of selecting these two DFIs is based on their ages and the objectives of their establishment. For a quick overview, a brief introduction of these selected DFIs is given in the subsection below:

### *3.1 Bank Simpanan Nasional (BSN)[3]:*

The starts of savings bank in Malaysia can be traced back to the late 19th century. The savings bank of Perak and Selangor were such two savings banks started in 1888 and 1893 respectively. They were administered by the respective State Treasuries until they were taken over by the Postal Department. In 1907 the Perak and Selangor Savings Banks were dissolved and brought under the Federated Malay States Post Office Savings Banks which also provided services in the states of Negeri Sembilan and Pahang. Separate Savings Bank services under the Straits Settlement Post Office Savings Bank were also in existence in Penang, Malacca and Singapore as early as 1902 while the Unfederated Malay States had their own Post Office Savings Banks in the years prior to the Second World War. Subsequently, the functions and responsibilities of the Post Office Savings Bank were taken over by Bank Simpanan Nasional which was established in1974. BSN is governed under the BSN Act 1974 & BSN (Amendment) Act 2010. The Development Financial Institution Act 2002 places BSN under the purview of BNM. BSN's mandated roles are initiated by the Government. BSN has dual obligations to: remain sustainable and profitable and carry out mandated roles in: ensuring accessibility to banking for all segments of society and providing financing for micro enterprises through Micro Finance loans. Overall the bank aspires to utilize the funds it collects for investment including financing of economic development process of the nation. Since the launching of Bank Simpanan Nasional, Malaysia on 5th December 1974, it has made steady progress over time. The accumulated assets of the bank were over RM537 million at the time of its launching in 1974 which increased to RM20,289.71 at the end of year 2010. This figure represents over 38 times more than the amount in 1974 over the past 36 years. As for the commitment towards economic development, as at the end of 2010, BSN channeled over RM18 billion to enhance economic activities through investment in securities and lending to other sectors of the economy. As at the end of 2010, the Bank has a total of 5828 staffs, 856 Automated Teller Machines (ATMs) and 384 branches nationwide to provide financial services to its customers.

### *3.2 Bank Kerjasama Rakyat Malaysia Berhad (BR)[4]*

Bank Kerjasama came to its present state through several stages. It was first established in September 1954 under the Cooperative Ordinance 1948, following an expansion of the cooperative movement in Peninsular Malaysia. On 28 September 1954, it was named Bank Agong (Apex Bank) through merging of 11 union banks and then in 1967, it replaced Bank Agong with its membership opened not only to the cooperatives, but also to individuals. Subsequent changes in the by-laws also resulted in the creation of its subsidiary companies and opening of branches to serve members as well as customers. On 6 January 1973, the name was changed to Bank Kerjsama Rakyat Malaysia Berhad or better known as Bank Rakyat. Bank Rakyat is governed by its by laws and Bank Kerjasama Rakyat (M) Berhad Act 1978 (Special Provision 202), which allows Bank Rakyat to provide financing to non-members. On 8 May 1993, Bank Rakyat took a giant step towards becoming a *Syari'ah* co-operative bank by introducing Islamic banking products at four of its branches and by 2002, Bank Rakyat became a full-fledged Islamic cooperative bank, the third bank to offer total Islamic banking products in Malaysia. Bank Rakyat together with six other financial institutions was placed under the Development Financial Institution Act (DFIA) 2002 on 15 February 2002. The Bank Rakyat is currently placed under the supervision of Ministry of Domestic Trade, Co-operatives and Consumerism. Like BSN, Bank Rakyat also serving its customers as well as the socio-economic development purpose of the country since its inception. The total resources of Bank Rakyat were estimated about RM73.2 million in 1973 with a total number of 12 branches (BNM-AR: 1973). The bank also channeled about RM25.6 million to the economy through loan with different maturities in 1973. The total resources of the bank increased from RM73.2 million in 1973 to nearly RM62 billion as at the end of 2010. This figure represents an 85-fold increase over the last 37 years. Out of RM62 billion total assets, around RM47 billion were financed for promoting the economic activities. To date, Bank Rakyat has a total of 4280 staffs, 435 ATMs and 134 branches nationwide serving Islamic banking facilities to its customers.

[3] For details refer to their website: http://www.mybsn.com.my
[4] Excerpted from its website: http://www.bankrakyat.com.my

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## 4.0 DATA AND THE TYPES OF FINANCIALRATIOS

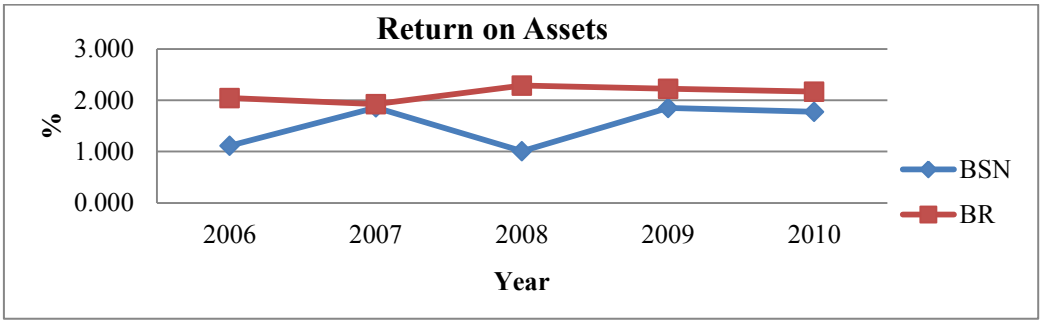
In this section we highlighted the sources of data and the types of financial ratios that we have used to make comparative analysis between BSN and the BR. The comparisons are made for a period of 5 years spanning from 2006 to 2010. The values used for calculating the financial ratios are taken from the year- end Balance Sheets and Income Statements provided in the Annual Reports of those selected DFIs. As for the ratio tools, there are dozens of financial ratios available for analysis. Among them, we have chosen twelve types of ratios that are considered more relevant to our purpose in this paper. They ratios are: Return on Assets (ROA), Return on Equity (ROE), Debt to Assets Ratio (DAR), Debt to Equity Ratio (DER), Times Interest Earned Ratio (TIER), Loan to Deposit Ratio (LDR), Loan to Assets Ratio (LAR), Investment to Assets Ratio (IAR), Operating Expenses to Deposit Ratio (OEDR), Operating Income to Operating Expenses Ratio (OIOER), Operating Expenses to Total Revenue (OETR), and Total Revenue to Total Assets Ratio (TRTAR)..

## 5.0 ANALYSIS OF FINANCIAL PERFORMANCE OF THE SELECTED DFIs:

### *5.1 Return on Assets (ROA)*

The total assets of a company are the investment that the shareholders have made. Therefore it is pertinent from the investors' perspective to see how the company can generate returns from their investments. The ROA indicates the profitability of a company's assets in generating revenue. In other words, this ratio is considered an indicator of efficient and effective management of a company's assets to generate earnings from invested capital before contractual obligations are paid. The higher the return, the more efficient the management is in utilizing its assets. Figure 5.1 shows the comparisons of ROA between BSN and BR. Return on assets of BSN from 2006 to 2010 were 1.112%, 1.859%, 1.006%, 1.850% and 1.774% respectively. It shows that ROA of BSN increased from 2006 to 2007 by 0.75% and then decreased by 0.85% again in 2008. In 2009 ROA again increased slightly followed by a slight decrease in 2010. On average, the ROA shows that the BSN is earning about RM152 after tax and zakat for each ringgit invested in their assets. ROA of BR from 2006 to 2010 were 2.042%, 1.923%, 2.285%, 2.224% and 2.166% respectively. It shows that ROA of BR decreased by 0.12% from 2006 to 2007 and then increased by 0.36% from 2007 to 2008 followed by slightly decrease in 2009 and 2010 respectively. Based on 5-year average, the ROA shows that the BR is earning about RM213 after tax and zakat for each ringgit invested in their assets. Overall the result shows that BR performs better than its peer BSN.

Figure 5.1: Comparisons of ROA between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 1.112 | 1.859 | 1.006 | 1.850 | 1.774 | 1.520 | 0.424 |
| BR (%) | 2.042 | 1.923 | 2.285 | 2.224 | 2.166 | 2.128 | 0.14566 |

### *5.2 Return on Equity (ROE)*

ROE measures how much the stockholders earned for their investment in the company. This ratio measures the ability of management of the company to generate adequate returns for the capital invested by the owners of a company. ROE of BSN from 2006 to 2010 were 40.898%, 51.205%, 23.920%, 32.560% and 25.554% respectively. The return on equity of BSN shows an increase of over 10% from 2006 to 2007 followed by a sharp decrease of over 27% in 2008. This is due to a drastic fall in profit after tax and zakat which was about RM168 million in 2008 as compared to RM283 million in 2007. The ROE increased by 9% in 2009 and decreased by 7% in 2010. In contrast, the ROE of BR showed upward trend throughout the periods. The ROE of BR from 2006 to 2010 were respectively 15.447%, 16.929%, 21.568%, 21.239%, and 22.531%. It shows that although on average BSN performed better than the BR, its earning was volatile relative to BR. The higher ROE of BSN also indicates its higher financial leverage which is on average more than 95% as compared to BR of 89% (figure 5.3). The ROE of BR during the periods show steady progress and also stable as indicated by a lower standard deviation. This is shown in figure 5.2.

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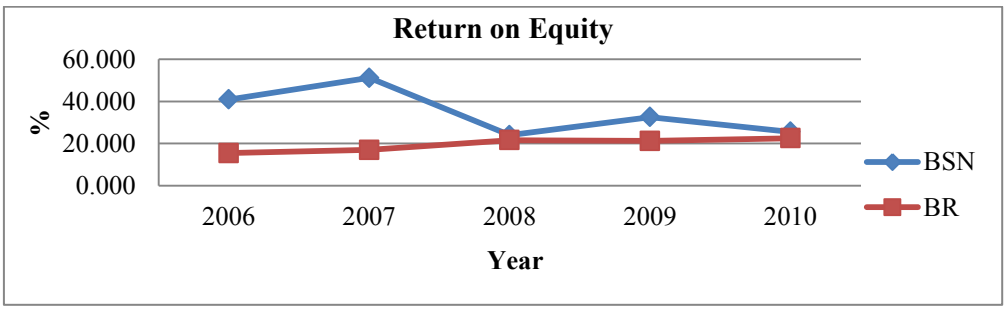
Figure 5.2: Comparisons of ROE between BSN and BR

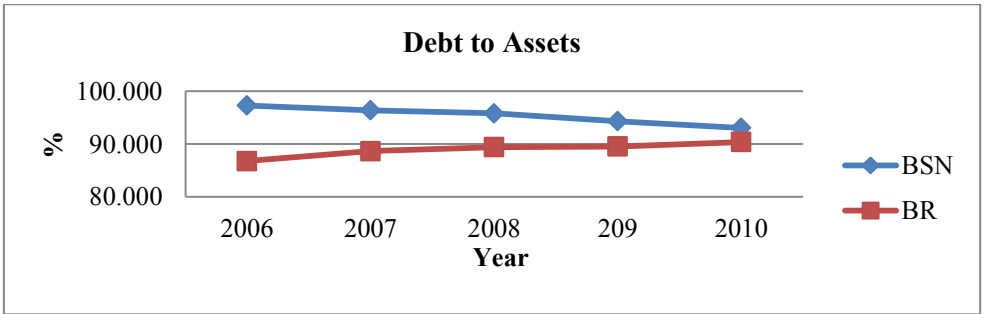



| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 40.898 | 51.205 | 23.920 | 32.560 | 25.554 | 34.828 | 11.349 |
| BR (%) | 15.447 | 16.929 | 21.568 | 21.239 | 22.531 | 19.543 | 3.143 |

### *5.3 Debt to Assets Ratio (DAR)*

DAR indicates the amounts of the company's assets are being financed through debt. In other words, how much the company is dependent on leverage or it borrowed from and/ or owed to others. If the ratio is less it indicates that the company is less risky and has good equity position and the vice versa. From the calculation, we find that the DAR of BSN from 2006 to 2010 registered 97.282%, 96.370%, 95.795%, 94.320%, and 93.058% respectively. The DAR shows a gradual decrease in the percentage of debt that makes up of the capital structure of BSN. In contrast, the DAR of BR from 2006 to 2010 were 86.782%, 88.642%, 89.404%, 89.530% and 90.385% respectively. The trend of DAR of BR is just opposite of BSN. While BSN is reducing its dependence on leverage, the BR is increasing its dependence on leverage. In other words, total assets of BSN are growing at a faster rate than its debt, while the opposite is true for the case of BR as shown in the figure 5.3.

Figure 5.3: Comparisons of Debt on assets ratio between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 97.282 | 96.370 | 95.795 | 94.320 | 93.058 | 95.365 | 1.680 |
| BR (%) | 86.782 | 88.642 | 89.404 | 89.530 | 90.385 | 88.949 | 1.360 |

### *5.4 Debt to Equity Ratios (DER)*

Debt to equity ratios indicates what proportion of debt a company has relative to its equity. This measure gives an idea to the leverage of the company along with the potential risks the company faces in terms of its debt-load. A high debt/equity ratio generally means that a company has been aggressive in financing its growth with debt which can results in volatile earnings as a result of additional interest expenses. As an extreme case this may lead the company even to bankruptcy. From the calculation, we find that the DER of BSN from 2006 to 2010 were 35.79, 26.55, 22.78, 16.60 and 13.41 respectively. The trend shows that in the initial period debt on equity ratios was very high but the figures slowed down gradually over time. Debts to equity ratio of BR from 2006 to 2010 were 6.57, 7.80, 8.44, 8.55 and 9.400 respectively. Like DAR, we also observe here a converging trend. While DER of BSN is showing a downtrend, the DER of BR is moving upward overtime. It shows that debt to equity ratio of BSN was very high in 2006 but started decreasing gradually throughout the next periods. The trend exhibited just opposite for BR. It is observed that as for every RM1, BSN has to pay a debt of RM 13.41 in 2010 while for BR the figure is RM9.40 in the same period.

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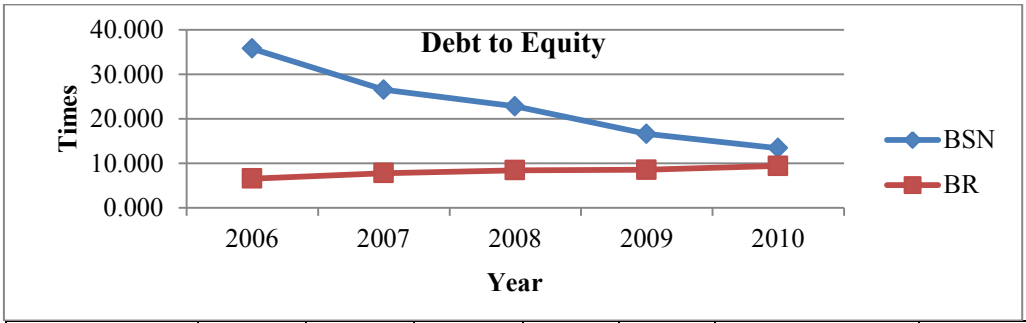
Figure 5.4: Comparisons of Debt to equity ratio between BSN and BR

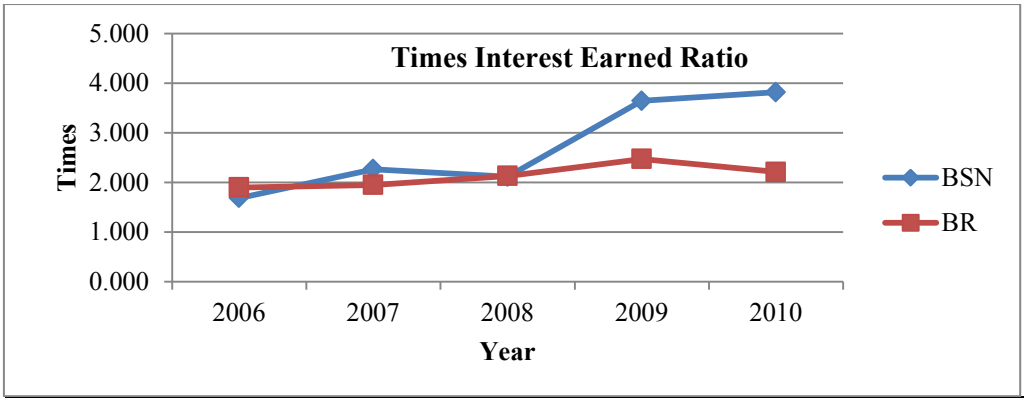



| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (times) | 35.79 | 26.55 | 22.78 | 16.61 | 13.41 | 23.03 | 8.79 |
| BR (times) | 6.57 | 7.80 | 8.44 | 8.55 | 9.40 | 8.15 | 1.05 |

### *5.5 Times Interest Earned Ratio (TIER)*

Times interest earned ratio is a measure of a company's ability to honor its debt payment obligation. The larger the TIER, the more capable the company is at paying the interest on its debt. In other words, higher TIER indicates that the company is generating enough cash from its operations EBIT (Earnings before interest and taxes). TIER of BSN from 2006 to 2010 were 1.685, 2.266, 2.113, 3.642, and 3.817 respectively. In contrast, the TIER of BR from 2006 to 2010 were 1.898, 1.950, 2.130, 2.470 and 2.209 respectively. The comparison shows that on average over the period, BSN has the higher TIER than its peer BR signifying its better position in generating enough cash from operations to meet its debt payment obligation. Figure 5.5 shows the trend.

Figure 5.5: Comparisons of Times interest earned ratio between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (times) | 1.685 | 2.266 | 2.113 | 3.642 | 3.817 | 2.705 | 0.962 |
| BR (times) | 1.898 | 1.950 | 2.130 | 2.470 | 2.209 | 2.131 | 0.228 |

### *5.6 Loan to Deposit Ratio (LDR)*

LDR is one of the important ratios that measure the extent of the liquidity condition of the company. A higher ratio indicates the company's lower liquidity position with higher risk as to meet its depositor's claims. Higher LDR also can be thought of from another angle as it is good in order to generate more profit from utmost utilization of its assets. On the other hand, lower LDR indicates higher liquidity position with lower risk, but may be potentially less profitable as the resources are not fully utilized to generate more profit. From the allocation of resources to economic agent perspective, higher LDR means more resources are available for economic activities which in turn can generate more resources (if utilized efficiently). The LDR of BSN increased overtimes from 40.92% in 2006 to 60.896% in 2010 indicating that lending activities grew at a faster rate than the deposit. The LDR of BR also increased over time with a slight decrease in period 2010. However the loan growth rate of BR is slightly slower than the BSN. On 5-year average, the LDR of BR is pretty higher than BSN as shown in the figure below:

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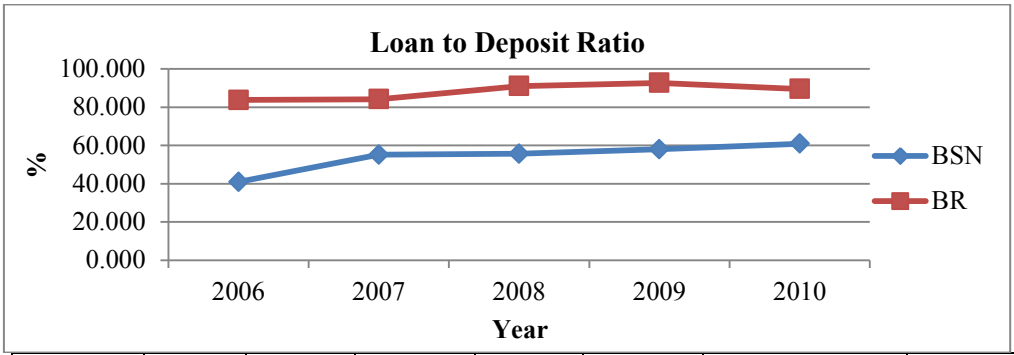
Figure 5.6: Comparisons of LDR between BSN and BR

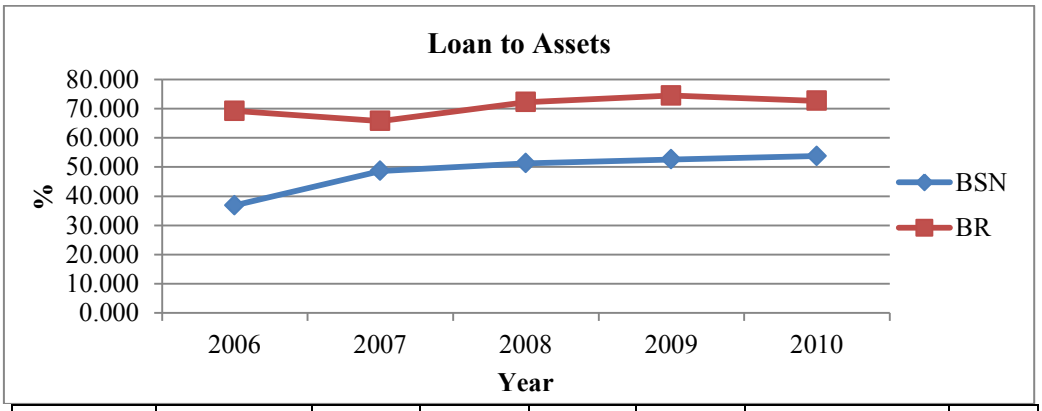



| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 40.919 | 55.146 | 55.612 | 57.973 | 60.896 | 54.109 | 7.719 |
| BR (%) | 83.759 | 84.159 | 91.066 | 92.739 | 89.576 | 88.260 | 4.085 |

### *5.7 Loan to Asset Ratio (LAR)*

Both LDR and LAR measure the liquidity status of the company except the former which is in relation to its deposits while the later in relation to its total assets. Higher ratio indicates lower liquidity with higher risk while lower ratio suggests higher liquidity position associated with lower risk but tends to be potentially less profitable. The LAR of BSN and BR show more or less the similar upward trend like the LDR. The LAR of BSN increased from 36.85% in 2006 to 53.75% in 2010, nearly a 17% increase during the 5-year periods, while LAR of BR increased to 72.66% in 2010 from 69.19% in 2010, a 3.47% increase in 5 years. However, on average, the LAR of BR is pretty above of the figure that of BSN as shown in the table below the figure 5.7. The higher LAR of BR conforms to the result we have drawn before in the case of the return on assets.

Figure 5.7: Comparisons of LAR between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 36.85 | 48.66 | 51.26 | 52.57 | 53.75 | 48.62 | 6.844 |
| BR (%) | 69.19 | 65.72 | 72.22 | 74.43 | 72.66 | 70.84 | 3.429 |

### *5.8 Investment to Assets Ratio (IAR)*

IAR represents the proportion of the total assets allocated for investment in securities (bonds or shares). This is also a good indicator of the commitment of the banks towards economic development by providing financial resources to undertake economic activities through investment. An increase of IAR may represent more resources flowing to the economy. Looking at IAR, we find that BSN has allocated more resources for investment than the BR. Although the IAR of BSN showed a gradual decrease over time, on average, BSN's investment activities are larger than that of BR.

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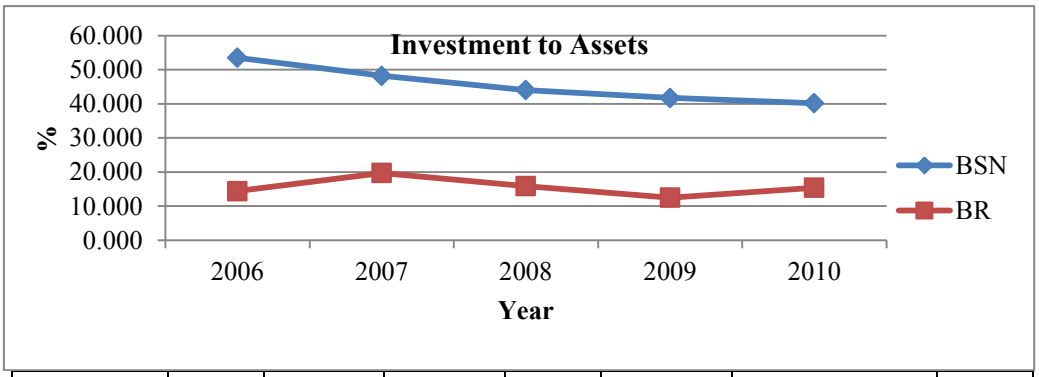
Figure 5.8: Comparisons of IAR between BSN and BR

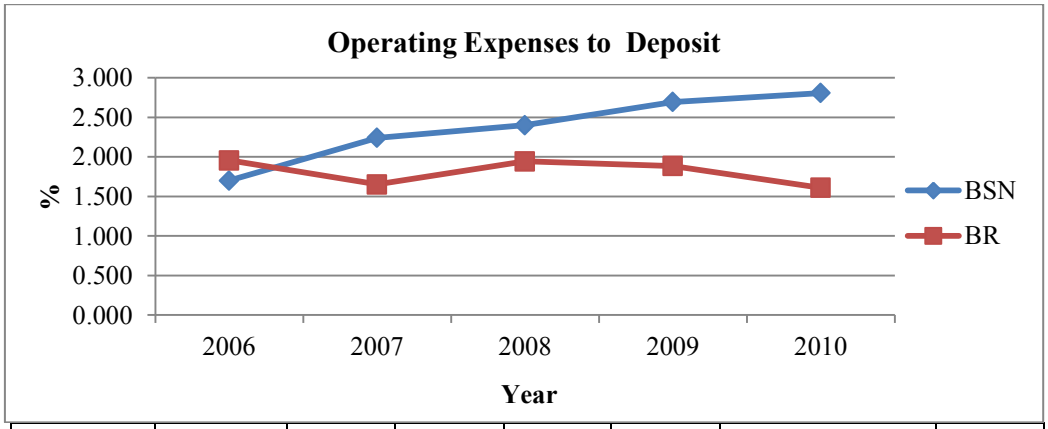



| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D |
|---|---|---|---|---|---|---|---|
| BSN (%) | 53.50 | 48.21 | 44.02 | 41.74 | 40.16 | 45.53 | 5.389 |
| BR (%) | 14.43 | 19.72 | 15.88 | 12.51 | 15.42 | 15.59 | 2.646 |

***5.9 Operating Expenses to Deposit Ratio (OEDR)***

This measures show how cost effective the banks are in mobilizing deposits. Besides being a good financial performance indicator, it also helps to assess the operational performance of the bank. A high ratio indicates higher cost per unit of deposit mobilized. This in turn will reduce the profit. Therefore, from profitability ratio perspective, the deposit should be cost effective. Looking at our results, we find that the operating cost of BSN increased over time from 1.701% in 2006 to 2.81% in 2010. In other words, to mobilize RM100, it spent RM1.701 in 2006 and RM2.81 in 2010. In contrast, the per unit deposit mobilized cost for BR was relatively lower as shown in the figure below. Average cost per unit of deposits mobilized for BSN was RM2.37 and for BR was RM1.81 respectively.

Figure 5.9: Comparisons of OEDR between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5- year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 1.701 | 2.241 | 2.401 | 2.696 | 2.808 | 2.369 | 0.437 |
| BR (%) | 1.957 | 1.653 | 1.945 | 1.884 | 1.610 | 1.810 | 0.166 |

***5.10 Income to Expense Ratio (IER)***

IER ratio shows the efficiency in managing the expenses of the banks. Figure 5.10 below shows the trend of the comparative performance of BSN and BR in terms of efficiency in managing expenses. In this study we defined income as the total profit before tax and zakat and expense as the operating expense (includes personal expenses plus other overhead cost). The results show that IER of BR were higher in all years than that of BSN. On average, BR generates RM1.863 for every 1 ringgit of expenses as compared to RM0.870 by BSN for every 1 ringgit of expense spent. In other words, the performance of BR in managing expenses is better than its peer BSN.

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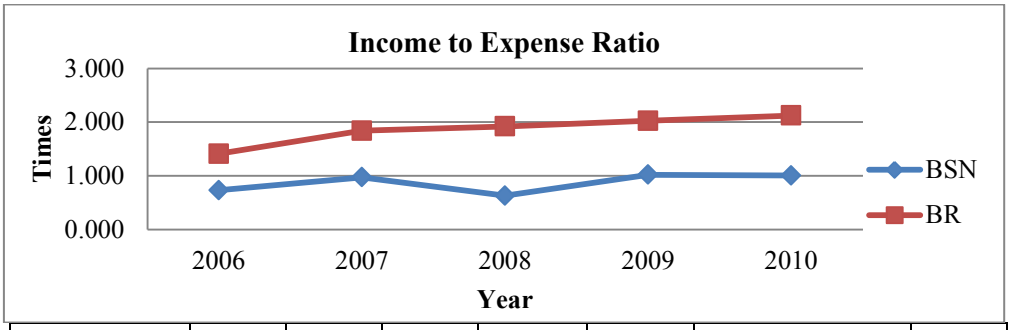
Figure 5.10 Comparisons of IER between BSN and BR

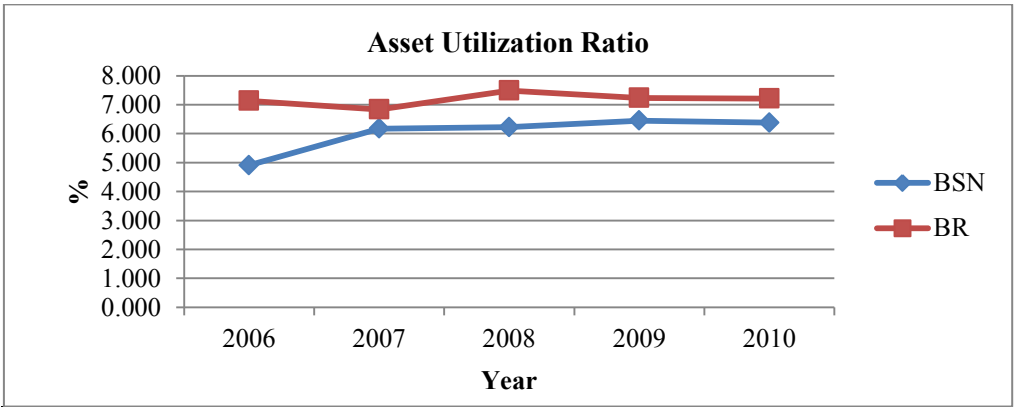



| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (Times) | 0.728 | 0.970 | 0.629 | 1.020 | 1.004 | 0.870 | 0.129 |
| BR (Times) | 1.410 | 1.840 | 1.918 | 2.024 | 2.123 | 1.863 | 0.275 |

***5.11 Asset Utilization Ratio (AUR)***

The asset utilization ratio measures the bank's effectiveness in utilizing all of its assets in order to generate revenues. In other words, AUR calculates the total revenue earned for every ringgit of assets the bank owns. A well-managed bank is expected to have a higher AUR that reflects its efficiency in putting the assets to good use. A low AUR indicates that the bank's assets are not efficiently used. Our calculation shows that the AUR of BSN were lower than the AUR of BS throughout the periods as viewed in figure 5.11. Based on 5-year average, the BSN has a AUR of 6.03% as compared to AUR of BR which was 7.18%. This means that BSN earned RM0.0603 for each ringgit of assets it held as compared to RM0.718 earned by BR for each ringgit of assets it held. The result shows that the BR is relatively more efficient and effective in managing its resources than the BSN.

Figure 5.11 Comparisons of AUR between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (%) | 4.905 | 6.174 | 6.221 | 6.452 | 6.378 | 6.026 | 0.637 |
| BR (%) | 7.134 | 6.840 | 7.489 | 7.235 | 7.214 | 7.182 | 0.233 |

***5.12 Operating Expense to Revenue (OER)***

OER measures the efficiency of the bank in its operation. This ratio calculates the amount of operating expenses per ringgit of operating revenues. Generally, lower ratio is preferred to higher ratio as it shows that lower amount of expense is incurred in order to generate one unit of revenue. For example, an OER of 30% means RM0.30 is incurred to generate RM1.00 amount of revenue. Our results show that the OER of BSN is increasing over time from 31.2% or RM0.312 in 2006 to 38.9% or RM0.389 in 2010. Based on 5-year average, BSN incurs RM0.351 as operating expenses in order to generate RM1 of revenue. In contrast, the OER of BR showed a bit fluctuating trend. The OER of BR was 22.7% or RM0.227 in 2006 which declined to 18.9% or RM0.189 in 2007. The trend was quite stable in 2008 and 2009 as shown in the figure below. The figure reduced to 18.1% or RM0.181 in 2010. On average, the OER of BSN was 35.1% or RM0.351 as compared to 20.2% or RM0.202 of BR. Overall, the result shows that in terms of efficiency in generating revenues and controlling expenses, BR also performs better than BSN.

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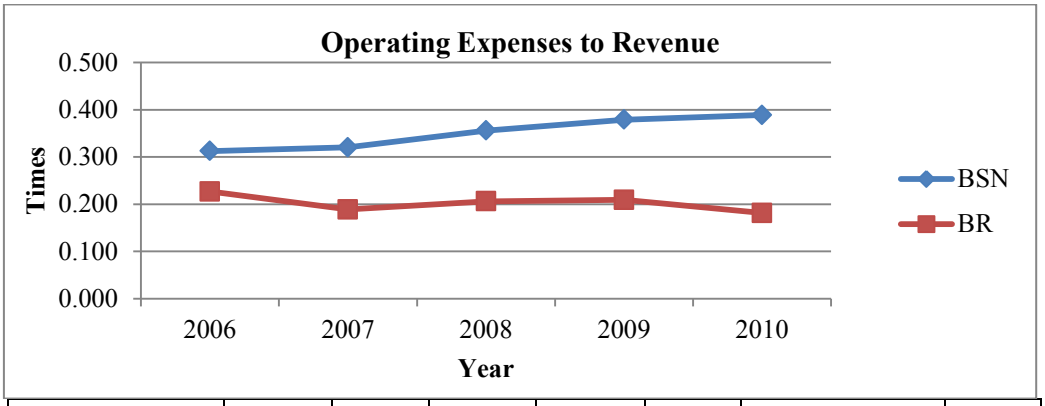
Figure 5.12 Comparisons of OER between BSN and BR




| | 2006 | 2007 | 2008 | 2009 | 2010 | 5-year average | S.D. |
|---|---|---|---|---|---|---|---|
| BSN (times) | 0.312 | 0.320 | 0.356 | 0.379 | 0.389 | 0.351 | 0.034 |
| BR (times) | 0.227 | 0.189 | 0.206 | 0.209 | 0.181 | 0.202 | 0.018 |

## 6.0 CONCLUDING REMARKS

DFIs are one of the important components of the Malaysian financial system operating as a catalyst towards achieving the socio-economic development objectives of the country. In this study, we have selected a sample of 2 DFIs out of 13 institutions in order to assess their financial performance. For this, we have used twelve (12) key financial ratio analysis tools. Based on the calculations, we find that except ROE, TIER and IAR, in all other nine (9) financial ratios, BR performs better than its peer BSN. BSN has a higher ROE than BR. This is reflected in a higher debt-load of BSN as indicated in its higher debt ratios (DAR and DER). Higher debt ratio may lead to increase in the interest expenses and as such reducing the income. Furthermore, BSN turns out to be relatively inefficient in managing of its assets and appears to suffer from potential problem of controlling its operating expenses as reflected in higher OEDR and OER with lower IER and AUR. Therefore, the BSN should focus on reducing the debt-load so that DAR and DER will improve which in turn can lead to increase in income. BSN also should focus on finding mechanism to reduce its operating expenses. One way to do is by expanding the financing activities to generate more income from the invested capital. This can improve OER, IER and AUR. Available data shows that the average growth rate of loans, advances and financing of BSN were about 18.1% while the growth rate of investment was only 0.0003%. In contrast, the average growth rate of advances and financing of BR was about 24.1% while the investment growth rate was over 29%. This may also translate the greater commitment of BR towards socio-economic development objectives of the country along with improvement of efficient and effective management of its resources. Overall based on the ratio analysis we may conclude that the BR is more effective and efficient than its peer BSN in many respects particularly in managing its expenses, generating more income and utilization of its assets with full capacity.

## APPENDIX

### Formula used to calculate ratios

| Name of Ratio | Formula |
|---|---|
| 1. Return on Assets | Net Income(profit after tax & zakat)/Total Assets |
| 2. Return on Equity | Net Income/Total Shareholders' Equity |
| 3. Debt to Assets | Total liabilities/Total Assets |
| 4. Debt to Equity | Total Liabilities/Total Shareholders' Equity |
| 5. Times Interests Earned | EBIT (Earnings Before Interests & Taxes)/Interest Expenses |
| 6. Loan to Deposit | Loans (loan+advances)/Total Deposit |
| 7. Loan to Assets | Loans/Total Assets |
| 8. Investment to Assets | Investment (investment in securities)/Total Assets |
| 9. Operating Expenses to Deposit | Operating Expenses(Non-interest expenses)/Deposit |
| 10. Operating Income to Operating Expenses | Operating Income/Operating Expenses |
| 11. Operating Expenses to Revenue | Operating Expenses/Revenues |
| 12. Assets Utilization Ratio | Total Revenues/Total Assets |

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