ANALYSIS OF LIQUIDITY AND PROFITABILITY LEVELS AS MEASURES OF MICROFINANCE BANKS PERFORMANCE, A STUDY OF YOBE MICROFINANCE BANK LIMITED (YBMFB), DAMATURU

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ABSTRACTS

The topic, Analysis of Liquidity and Profitability levels as measures of Microfinance Bank's Financial Performance, a study of Yobe Microfinance Bank Limited (YBMFB), Damaturu attempts at examining the financial positions of Microfinance Institutions in effort to determine their health standards. The task would indicate their abilities to meet the wealth maximization objective of the banks owners in the one hand and all other parties; workers, customers and the government on the other hand. Source of data were the financial records and other related documents of the bank. Ratio analysis have been employed to determine performance in terms of profitability and liquidity, profitability were measured through ratios including Returns on Assets (ROA), Earning Assets to Total Assets (EATA), Returns on Loans (ROL), Returns on Deposits (ROD) and Returns on Equity (ROE). Liquidity Positions which assessed the level of solvency were examined through ratios in the likes of Loans to Deposits and Deposits to Assets. The ROA hovered around 9.5-9.7% within the periods 2018-2019 is considered stable. The EATA of between 83-85% is better and 3.20-2.90 loan interest charged is average. However, the net profit to total deposits was bad at 0.0025 for 2018 compared with 0.026 in 2019. Similarly, ROE of 0.00050 was poor in 2018 compared with the value, 0.0042 in the year 2019. Conversely, the liquidity position of 2.64 was challenging in 2019 compared with 2.34 in the year, 2018. Also, for both 2019 and 2018, the bank assets were financed by deposits hovered around 55-57% indicating impending danger of illiquidity particularly when depositors wishes to withdraw more than 50% of their deposits. Despite these circumstances, this research adjudged the YMFBL as okay considering that the bank had recently switched to microfinance from mortgage finance with attendant problems of economic instabilities, security challenges and advent of corona pandemic. Also, ratios have some limitations; the decimations of all variables into monetary standards, the issues related to comparisons and the lack of uniform acceptable values across ratio users. The recommendations were that the

bank should seek better investment alternatives to maximize shareholders wealth, reduction of operating expenses to improve operating income, better management of deposits to loans and loans to assets so as to guide against inherent danger of illiquidity.

***Keywords**: Liquidity, profitability, financial performance, microfinance banks, ratios.*

Introduction

Financial Performance reflects the ability of an organization to gain and manage its resources to develop competitive advantage. It has to do with how better the shareholder is at the end of a period. This is because the main objective of investment in a business is wealth maximization. Therefore, the measurement of performance of the business must give an indication of impact of investment on the wealth of an investor. That is, how wealthier the shareholder has become as a result of the investment over a specific period of time (Iswatia & Anshoria, 2007).

Financial measures have long been the foundation for business performance measurement. These measures expressed the performance and achievement in monetary terms (Adam 2014). In addition, the fundamental reliance by managers on financial performance measures dominates organization strategy and has been in use for decades to the extent that managers are frequently comfortable with them. Financial performance emphasizes on variables related directly to financial report which is expressed in monetary terms and accounting terminologies such as profits or loss. The Financial performance of a firm can thus be analyzed in terms of profitability, dividend growth, sales turnover, and returns on capital or asset employed among others (Maranga 2015)

According to Walker (2001) return on sales (ROS) measures how much a firm earns relative to sales, return on assets (ROA) indicates firm's ability to effectively utilize its assets, and return on equity (ROE) reveals the amount of returns which investors receives for their investments. Three dimensions of financial performance assessment are possible. These include firms productivity; efficiency of processing of inputs into outputs, profitability; company earnings on costs, and the market premium; the level at which a firm market value exceeds its book value (Almajali, Alamro & Al-Soub 2012).

The experience of micro- finance activity in Nigeria had not been quite successful compared with the formal model (Arogundade 2010). Also, despite the efforts by the government in the area of credit delivery and policy guidelines for micro lending, a lot is left to be much desired (Dada & Salisu 2008). The observation therefore is that

microfinance does not reach the poorest of the poor and their performance standards are subjects to criticisms. Prior to CBN's intervention, microfinance was taking a swift decline into the abyss in Nigeria. This is because the sector was riddled with fraud and mismanagement of funds attributable to lack of understanding of the practice of microfinance activity by the senior managers in some of the microfinance banks (Orodje, 2012). Also, A significant challenge facing these banks is the battle to control its portfolio and risk to remain within the international bench mark (Idama, Asongo & Nyor 2014).

Therefore, though the importance of capital and Financing structure in the operational and financial sustainability of Microfinance Institutions (MFIs) cannot be over emphasized (Fersi, & Boujelbéne 2017), good attention must be given to financial performance so that business objectives are not jeopardized.

According to Haile, Getacher & Tesfay (2014) banking institutions have become increasingly complex; the key drivers of their performance remain earnings, efficiency, risk-taking and leverage. Accounting data are useful in assessing not only the economic prospects of microfinance banks but for all firms. This research attempts to examine microfinance performance using financial ratios in assessing MFIs profitability, and evaluate the quality of its earnings. This is done by examining the bank liquidity positions, returns on assets and profitability. The data is the records of the banks financial statement; balance sheets, income statements and profit and loss accounts. The analysis covers periods 2018-2019.

Literature Review

According to Idama, Asongo & Nyor (2014), Microfinance Banks have a critical role of providing different financial products and services to the people most especially the low income earners who lack collateral to borrow from formal financial institutions like the commercial banks. This category of financial institutions serves the poor section of the populace via provision of small units of financial services to low income clients which are usually excluded from mainstream financial system (Ehigiamusoe, 2008).

The Microfinance Banking concept in Nigeria is an extension of the old community banking system. With the establishment of community banking system, the Micro Small and Medium Enterprises access to credit had greatly improved (Oladejo 2008).

In the opinion of Rolando (2010), microfinance has been said to be a good way of supporting entrepreneurs; prividing poor borrowers with access to sustainable livelihood through zero or very low interest loans. The microfinance institutions (MFIs) are the agencies that attract global concern due to their importance and serves

as specialized financial institutions in ensuring financial inclusion and as well as helping in addressing poverty level (Abubakar, Zainol, & Abdullahi2015).

Karlan & Goldberg (2007) put it that microfinance is the provision of small-scale financial services to people who lack access to traditional banking services. Crabb & Keller (2011) see microfinance as providing financial services to individuals traditionally excluded from the banking system, especially women. Consequently Microfinance refers to the provision of financial services to the rural and urban poor who are self-employed. It concerns with the supply of loans, savings, money transfers, insurance, and other financial services to low-income people (Belwal, Tamiru & Singh (2011). Also, Udeaja & Ibe (2006) sees micro finance institution as one that focuses on providing financial services to the low-income persons in the community. Simply, Microfinance Institutions are specialized financial institutions that serve the poor. In the work of Matul & Tsilikounas, (2004): the results of their findings provide evidence that microenterprise performance is strongly linked with household well-being and security.

Accordingly, the CBN (2005) characterized the operation of microfinance industry in Nigeria to include, weak institutional capacity, weak capital base, the existence of a huge un-served market, weak economic empowerment of the poor and poverty reduction, the need for increased savings opportunity and the low interest of local and international communities in micro financing.

Liquidity and Bank Performance

Liquidity is of paramount importance as a core issue of the banking industry (Caruana & Kodres, 2008). Performance efficiency of a bank is significantly influenced by the availability of sufficient liquidity in the financial operations of a bank. This is because banks must meet their operational financial obligations by executing payments as at when due in order to avoid being declared illiquid (Crocket, 2008).

According to sekoni (2015) liquidity is fundamental to the well-being of financial institutions particularly banking industry. It determines the growth and development of banks as it ensures proper functioning of financial markets. Therefore, liquidity is very critical phenomenon for smooth operation of banking businesses because the growth and survival of banks depend on liquidity management.

Concisely, liquidity can be referred to as a bank's ability to meet the cash demands and obligations that it holds with minimal of tolerable loss. Inability to easily convert assets to cash results to liquidity shortfalls which can impair the growth of the whole economy. It is worth to note that the cause of liquidity problems is not limited only to mismatch between obligations and maturity, other sources of liquidity issues are

traceable to different factors. This could even result from poor coordination and linkages between cash inflows and outflows. Therefore, preventing liquidity shortages requires efficient and effective coordination of the cash inflows and cash outflows. A bank a times could unexpectedly experience extreme shortages of liquidity which could be triggered by larger amount of standby credit drawn or an unexpected reduction in the availability of deposits. Efficient coordination of the cash inflows and cash outflows is required to meet the cash flow shortfalls; that is, effective risk management structure for managing liquidity (Nagret, 2009). Accordingly, understanding the banks' funding sources as well as the potential causes of liquidity shortages is very critical for proper liquidity management (Sekoni, 2015)

Financial Performance in the Banking Industry

Financial performance could be defined as a measurement of the results of a firm's polices and operations in monetary terms. In assessing the overall financial condition of a company, the income statement and the balance sheet are important reports. While the income statement captures the company's operating performance, the balance sheet shows the net worth (Adam, 2014). Financial performance could be assessed via descriptive and analytical measures. The descriptive measures include total assets, total liabilities, stockholders equity, total revenues, total expenses and net income. The analytical measures of financial position and performance could include profitability, efficiency, liquidity and solvency standards.

The significant recognition that has occurred in the financial sector industry has increased the importance of performance analysis for modern banks. The analysis is an important tool used by various parties operating either internally or externally to a bank. These parties include all those that are interested in bank's performance such as depositors, shareholders, regulators, managers, direct competitors, credit-rating companies, financial markets, and other market participants (Casu, Girardone & Molyneux 2006). Performance measurement serves as an important factor of understanding of the paths of success or failure of a bank. Also, such measures can play key roles in initiating or implementing technological innovations and organizational change to achieve improved performance and progress towards goals (Adam, 2014).

Empirical Review

Kumbirai, and Webb (2010) investigated the performance of South Africa's commercial banks, 2005- 2009 using financial ratios to measure profitability, liquidity and credit quality. The study revealed significant increase in the overall

bank performance within the first two years. But, there was considerable decrease performance reflecting in falling profitability, low liquidity and deteriorating credit quality in the periods, 2008-2009 attributable to the global financial crisis commencing 2007. Almazari (2011) attempted to measure the financial performance of seven commercial banks in Jordan between the period 2005-2009, using simple regression analysis to estimate the impact of independent variable, the banks; the size, asset management, and operational efficiency of banks on dependent variable; financial performance in terms of return on assets and interest income size. It was discovered that there exists a positive correlation between financial performance and asset size, asset utilization and operational efficiency of those banks. However, the study also found out that higher total deposits, credits, assets, and shareholders' equity by a bank does not always means better profitability performance; asset size, utilization and efficiency are significant determinant factors of performance.

Almumani (2014) analyzed the performance of Saudi banks listed in stocks market between the periods 2007-2011. The financial performance was measured through financial ratios and secondary data and variables were adopted. The researcher adopted two approaches; trend analysis and inter-firm analysis. The results indicated increased assets, operating expenses, and costs as causes of decreased profitability. On the other hand, increased operating income causes increased profitability. Also, the analysis indicated significance of all the variables; increased assets, operating expenses, and costs on the bank income. Adam (2014) investigated the financial performance of Erbil Bank between the periods of 2009-2013. Financial ratios were used to measure the financial position of the studied-banks, and broader range statistical tools were adopted in the analysis. The findings indicated positive relationship between the banks financial positions and factors of bank activity relative to weakness and ability of the banks.

Idama, Asongo & Nyor (2014) identified significant challenge facing Nigerian microfinance banks as lack of control of credit portfolio and suggested the place of Operations Research experts in tackling Microfinance Banks challenges to guarantee sustainability. Oadejo (2013) evaluated microfinance activity in Osun state relative to SMEs in terms of the latter's credit, adequacy, and credit supplied and demand, timeliness of credit to operation, and cost of credit as a component of total overhead. Data were collected through Questionnaire administered on SMEs as well as the annual reports and accounts of the selected MFBs. Analysis of the data and hypotheses tested showed positive and significant relationship between microcredit delivery service of selected MFBs and SMEs performance. However most MFBs seem to be competing with the commercial banks in universal banking rather than the microfinance banking they were purposely established to undertake. Sekoni

(2015) concluded that liquidity is fundamental to the well-being of banking business because it determines the growth ensures proper functioning of financial markets.

Yobe Microfinance Bank Limited (YBMFB)

Yobe Microfinance Bank Limited was initially Incorporated as Yobe Savings and Loans Limited (YBSL) in September 28th, 1992 and licensed by the Central Bank of Nigeria in 2001 as a Primary Mortgage Institution. The bank was engaging in Mortgage Banking Business, until the year 2012 when the Central Bank of Nigeria raised the paid-up capital for the category of this bank to N2.5billion. The Yobe Sate Government which is the sole owner of Yobe Savings and Loans Limited decided to convert to Microfinance Bank. Approval to engage in Microfinance Business was granted by the Central Bank of Nigeria on the 19th of June 2014. The Bank has three branches located at Damaturu, Potiskum and Geidam all in Yobe State.

The bank presently has a customer deposit of N47, 882,862.00 as at 30/11/2019 and a customer base of 9430 broken into:

Current account holders 6326

Saving account holders 3104

Equally, the bank had extended various loan facilities totaling the sum of ₦83,242,033.28 as shown below:

S/N	Type of loan	Total amount
1	National Housing Fund Loan	₦5,198,004.76
2	Commercial Loan	₦444,166.60
3	Medium Term Loan	₦18,055,176.28
4	Short Term Loan	₦22,536,664.95
5	Staff Loan	₦12,357,829.55
6	Overdraft	₦24,650,191.14
	TOTAL	₦83,242,033.28

Source: YMFB 2019 Record

The bank has a shareholders fund of ₦157,055,889.45 as at 30th November, 2019 as detailed below:

1 share capital	225,643,068.06
2 Statutory reserves	5,135,514.00
3 Retained earnings	102,128,160.33)
4 unaudited Profit for 2019	28,405,467.72
Total shareholders fund	₦ **157,055,889.45**

Financial Performance of Yobe Microfinance Bank Limited

This research adopts an internal way to the study of financial performance of YBMFB using a group of the financial ratios related to items of the financial statements of the bank. The following categories of ratios are employed.

Profitability Performance: Profitability ratios typically used in banking include the followings: **Return on Assets (ROA):**
Often described as the primary ratio and relates to income earned by the bank. It is commonly defined as net income (or pre-tax profit)/total assets. It provides information about management's performance in using the assets of the business to generate income. Here, return is taken as profit before extraordinary items because they fall outside the scope of the bank normal operations. However, it does not suggest that those extraordinary items are ignored completely but, they are rather assessed as a separate exercise from the analysis of the bank performance. Thus, profit before tax is generally ideal because calculations using net income after tax figures may show trends due simply to changes in the rates of taxation (Bodie, Robert, Merton & David 2009)

Earning Assets to Total Assets Ratio:
Earning assets are the interest-bearing investment, loans and advances of a bank. To calculate this ratio, the total of interest-bearing investment plus loans and advances is divided by the total assets. It reflects the extent to which the banks management put assets of a bank into productive use. Thus, investment on building and equipment are not included because they may not directly generate income. = EA/TA x 100.

Returns on Loans (ROL):
An important earning asset of a bank is loans. This is the ratio of interest and fees on the average figure, loans flow over a period time which thereby implies the use of average figure rather than the year-end totals. It attempts to measure management's ability to price the bank loans and achieve optimum loan mix.

Return on Deposits (ROD):
To most financial analysts, (ROD) is one of the best measures of bank profitability performance. It is calculated by dividing net profits by total deposits i.e. NP/TD. This ratio reflects the bank management ability to utilize the customers' deposits in order to generate profits. Usually express in percentages; the higher this ratio, the better for a bank.

Return of equity (ROE):
This ratio relate to profit earned after tax to the resources contributed by the bank owners; ordinary share capital plus reserves. It therefore measures profitability by revealing how much profit a company generates with the money that shareholders

have invested. The higher of such ratio, the more efficient is the profitability performance of a bank. The ratios thus measure the financial performance and the managerial efficiency of bank. = Profit after tax/Equity x 100

Profitability performance YBMFB; 2018-2019

RATIOS	COMPUTATIONS	2018	2019
ROA	Pre-tax profits/Total Assets	0.096= 9.67%	0.095= 9.52%
EA:TA	Earning Assets/Total Assets	0.837 = 83.8%	0.847 = 84.7%
ROL	Average Loans/Interest-Charged	2.90	3.20
ROD	Net Profits/Total Deposits	0.0025 = 0.25%	0.026 = 2.6%
ROE	Profit after tax/Equity x100	0.00050 = 0.05%	0.0042 = 0.43%

Source of Data: YBSL Records 2018-2019

ROA- Returns on Assets
EATA- Earning Assets to Total Assets
ROL – Returns on Loans
ROD – Returns on Deposits
ROE- Returns on Equity

Discussions and Findings

i. ROA defines the income earned by the bank assets. Both years has balance yields on assets hovered around 9.51 %(2019) and 9.67% in 2018. Returns on Capital is therefore better off in the year 2018
ii. EATA explains the ability to put assets into earnings capability; productive use of assets. Here, 84% of the total assets have been put into productive use by the bank for the years 2019 and 2018. This is a better position for the bank.
iii. ROL reflects the ratios of interest and fees on the band average loans. It's a potent factor because loans constitute a major source of returns for banks.
iv. ROD attempt to measures real profitability- net profits in terms of total deposits; 2.6% in 2019 is better than 0.25% in 2018. This could result from low net profit for 2018 compared with 2019.
v. ROE depicts the bank ability to generate returns for its shareholders; 0.43% in the year 2019 is efficiently better to 0.05% for the year 2018.

Liquidity Performance versus Liquidity Ratios

A bank must be able to meet its obligations as at when due. If depositors and other lenders do not have confidence that their claims can be met appropriately, they might

stop depositing or lending with the bank. Liquidity ratios provide fundamental means of judging banks liquidity positions.
Among measures of liquidity for a bank are:

Loans to Deposits Ratio:
This ratio is a commonly used measure for assessing liquidity and credit risk, which is measured by dividing the banks total loans (total financing) by its total deposits i.e. loans/deposits. This ratio indicates the percentage of a bank's loans funded through deposits. A high value of this ratio indicates a potential source of illiquidity and insolvency because deposits are quite stable source of funding for a bank and loans are riskier asset than other financial assets. Simply, the higher the ratio, the lower the liquidity position of a bank. Therefore, a higher loan deposit ratio means more financial stress for a bank.

Deposits to Assets Ratio (TDP/TA): The ratio of total deposits to total assets is another liquidity measure, which is achieved by dividing the banks total loans or total financing by its total assets i.e. loans/assets. This ratio indicates the broad base of funding for the bank, which reflects how much of the bank's assets are funded by deposits rather than borrowed funds or equity.

Liquidity Positions YBMFB; 2018-2019

RATIOS	COMPUTATIONS	2018	2019
LD	Total Loans/Total deposits	2.341	2.636
DAR	Total Loans/Total assets	0.573 = 57.38%	0.559= 55.87%

Source of Data: YBSL Records 2018-2019
LD - Loan to Deposits Ratio
DAR - Deposit Assets Ratio

Discussions and Findings
i. LD relate important issue about liquidity; % of banks loans funded by deposits. The higher value of 2.64% in 2019 indicate some stress of possible insolvency and illiquidity compared to 2.34% for the year 2018
ii. DAR represents another way to measure liquidity but on broader base as it reflects the levels of assets funded by deposits. The position of 57.4% in 2018 is better to 55.9% in 2019 as higher value may indicate higher deposits employed in funding the bank assets.

Limitations of Ratio Applications
A major limitation is that it could be difficult except the analyst has access to internal data of a bank.

Ratios reduced performance into accounting figures without taken into consideration other factors such as human, policy, environment, social and many others in examining the health status of a firm.

Ratios by themselves are useless until when a comparison is made between one firm and the other or between one period and the other of a same company. Therefore there is no established standard parameter to determine acceptable or healthy values of a ratio.

Lay man could find the application of ratio very difficult because of level of understanding and thereby make no use to majority of customers of microfinance bank that happens to be local farmers and traders with little educational background.

Also, no standard means to measuring banks liquidity and usually, larger banks can practice standardized liability management and greater flexibility in liquidity planning.

Conclusions

Ratio analysis has some limitations. Second, analysis could indicate some areas of discomforts. But, fluctuations in ratio values within the year of assessment could result from economic instability since 2017/2018 which was further compounded by downturns in late 2019 and early 2020 resulting from the advent of the pandemic corona virus. Ratio analysis provide a good means of assessing performance of microfinance banks because the assessment is done largely based on real facts and figures already provided by the bank. Also, these are figures backed up with auditor's reports. The results are not bad for YBMFB given the new shift from Mortgage finance to microfinance and other volatilities that characterized the economy in the year of investigation.

Recommendations

Based on the analysis, the following recommendations are made.

i. Given the values 0.026 and 0.0025 returns on deposit, the bank could adopt additional ways to utilize its deposits to make better returns. This is expected to improve the low net profit and operating income for the bank.
ii. Similarly, it is advisable that the bank cut down it operating expenses because such expenditures could account for the low net operating income
iii. The returns on equity0.00050 to 0.0042 could signal negative performance and consequently shareholders could think otherwise. Hence, additional efforts must be made towards maximizing shareholders wealth.

iv. Also, the liquidity positions of 2.64 in 2019 indicate the need for the bank to find additional sources to finance loans instead of heavy reliance on deposits. This avoids the danger of insolvency in case customers reduced level of deposits.

v. Bank must deduce other means of funding of assets beside deposits from customers. Because more than average 55-57% of total assets are finance by deposits, it constitute broad base insolvency should the number of deposits dropped.

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