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Value Added Analysis: Evidence From Nepalese Commercial Banks

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Abstract : *This paper examines the value added or wealth created by the Nepalese commercial banks. In total 12 banks are considered sample for the study, which has been partition into six banks in each group on the basis of the age of the sample banks. The old age banks are generated higher amount of value added in comparison to young age banks. Nepalese banks are seemed to allocate sufficient portion of value added to the future business expansion and growth, which provided ample size of capital in the context of Nepal. The study finds value allocates to employees, government, providers of capital and retained on business is significantly difference between the old and young age Nepalese banks. Value Added Statement (VAS) is a supplementary additional report of Profit and Loss Statement. Now a day, such value added statement is one of the new technique as regard a part of social responsibility accounting and reporting to the stakeholders. In the context of the Nepal, still there is no mandatory provision for preparing and reporting VAS to their stakeholders.*

I. Introduction

Commercial banks having independent and separate legal entity provide financial services to their clients and therefore, the income from banking and non-banking services are higher than that of cost of services keeping required provision against non-performing assets. The excess of the income over the cost of services is known as value added. The value added is needed to survival stability and growth of such entity within the society largely depends on the wealth created by it through the collective efforts of all the stakeholders- shareholders, providers of loan capital, employees and the government. All these stakeholders are the parties to whom the result of business operation is communicated. To satisfy the information needs of the users; the conventional financial accounting system generates data relating to financial performance through Profit and Loss Statement giving emphasis on the interest of shareholders, i.e., owners [Mandal and Goswami (2008)]. The Profit and Loss Statement does not provide any information

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showing the extent of the value or wealth created by the company for a particulars period. The stakeholders cannot assess the contribution of the company using Profit and Loss Statement. Hence, Mandal and Goswami (2008) emphasis a need to modify the existing accounting and financial reporting system so that a business unit is able to give important to judge its performance by indicating the value or wealth created by it. To this direction inclusion of the Value Added Statement (VAS), supplementary of Profit and Loss Statement, is a newly developed technique, which is regarded as a part of social; responsibility accounting and reporting.

The paper focuses on the wealth or value created by the Nepalese commercial banks. Similarly, the paper examines the distribution of such value added among the different stakeholder - shareholders, providers of loan capital, employees and the government including the wealth retained in business to expansion and growth of the company.

In regard to the organisation of subsequent parts of the paper, Section II presents a brief review of previous studies regarding value added. Similarly, Section III outlines the methodology employed and describes the data used in this paper. Section IV presents the empirical results and finally Section V contains conclusion of the paper.

II. Literature Review

Value added is the difference between sales incomes and bought in goods and services. It measures the added value by the enterprise to its product or a service provided. A manufacturing firm begins with a certain quantum of raw materials and engages itself in a conversion process to yield a product wit new utility and market value, which is different from the original cost of materials. The excess of such market value over and above the cost of materials is defined as Value Added.

Various experts and institutions have defined the term Value Added differently. According to Chartered Institute of Management Accounting (CIMA), "the increase in realizable value resulting from an alteration in form, location or availability of a product or service, excluding the cost of purchased material and service." Such definition about the Value Added is followed by ICAI (1985). This can be expressed in the following equation:

Value added = Value after alteration - Value before alteration

Morely (1978), and Brown and Howard (1992) defined the term Value Added as the sales value less the cost of bought-in-goods and services used in producing those sales. In terms of equation it may be expressed as follows:

Value added = Sales – Bought-in-goods and services

From the above equation, it is shows that the Value added measures the wealth created by a business or industry. Thus, Van Staden (2000) defined Value Added as the value created by the activities of a firm and its employees, i.e., sales less bought-in-goods and services.

The term Value Added may be simply defined in Economics as the difference between the value of output produced and the value of the inputs purchased by a firm in a particular period. In the equation form it can be expressed as follows:

Value added = Value of outputs - Value of inputs

Above said approach of calculation of Value Added - difference between the outputs value and inputs value - is called subtractive method. Similarly, due to the fact that all the created wealth is also allocated in some way the value added can also bee computed by the additive method, which represents the sum of allocated or distributed parts of the created wealth. The additive method of value added calculation is shown as follows:

Value Added = Pay to employees + Pay to government + Pay to capital providers + Retained earnings

Both, Subtractive and Additive methods reveal the characteristic content of the value added concept, which can be split up into a performance and social aspect. The performance aspect is expressed by the subtractive method and social aspect by the additive one. So, value added information provides not only economic but social information too.

III. Methodology

The present paper is based on the secondary data of the Nepalese Commercial banks. The 25 commercial banks are population of the study. The sample banks are selected on the following basis:

- The bank should be listed in Nepal Stock Exchange (NEPSE).
- The bank should not be less than 5 years old.
- The bank should be in positive net-worth in the study period 2007/08

Finally, the study covered with 12 banks for financial year 2007/08. The twelve banks are classified into 6 - 6 banks in each as old and young age groups (Annex – 1). The study employed both Subtractive and Additive methods to evaluate value created and distribution amongst the stakeholders of the banks. The study is also examined the wealth created and allocation to employees, government, capital providers and not appropriate incomes between old and young age banks. Table 1 reports the variables use in the study and its' descriptions.

Table 1: Variables and descriptions

S. No.	Variables	Descriptions
1	Income from banking services	Interest income, Commission and discount, Exchange fluctuation income, and other operating income
2	Cost of services	Interest expenses and other operating expenses
3	Non-banking incomes (losses)	Non-operating incomes or losses
4	Profit (loss) from extraordinary items	Gain or loss from extraordinary items
5	Provisions against non-performing assets	Loan loss provisions against non-performing assets
6	Provision for possible loss written back	Provision for loan loss written back
7	Pay to employees	Staff expenses and bonus
8	Pay to government	Income taxes provisions
9	Pay to capital providers	Cash dividend payable to shareholders
10	To expansion and growth	Retained earnings and stock dividends

IV. Value Added Statement and Analysis

Descriptive statistics

Table 2 shows the descriptive statistics of the variables. It reports mean, median, standard deviation, minimum and maximum values of the study variables to all sample banks; old and young age sample banks during the study period for one-year ending mid-July 2008. On the basis of the descriptive statistics, old age banks are performing satisfactory in comparison to young age Nepalese banks.

Table 2: Descriptive statistics of the variables

(Figures in Rs. Millions)

S. No.	Variables	Mean	Median	Standard Deviation	Minimum	Maximum
	All Banks			**Total 12 observations**		
1	Income from banking services	1549.17	1186.50	711.694	804	2641
2	Cost of services	746.17	627.00	269.958	480	1305
3	Non-banking incomes	5.67	3.50	8.585	-8	24
4	Profit (loss) from extraordinary items	-10.25	-5.50	24.174	-53	40
5	Provisions against non-performing assets	-79.92	-61.00	65.176	-264	-25
6	Provision for possible loss written back	56.33	25.00	59.147	4	184
7	Pay to employees	195.83	130.00	124.295	70	403
8	Pay to government	185.33	139.00	121.140	57	374
9	Pay to capital providers	120.00	11.50	174.472	0	497
10	To expansion and growth	273.67	283.50	146.033	76	607
	Old age banks			**Total 6 observations**		
1	Income from banking services	2111.83	2333.50	566.524	1093	2641
2	Cost of services	935.50	922.50	265.444	607	1305
3	Non-banking incomes	8.00	6.00	8.602	0	24
4	Profit (loss) from extraordinary items	-10.00	-9.50	31.477	-53	40
5	Provisions against non-performing assets	-80.67	-67.00	31.188	-136	-57
6	Provision for possible loss written back	73.00	60.50	66.314	11	184
7	Pay to employees	290.33	316.50	108.780	110	403
8	Pay to government	276.83	318.00	103.008	101	374
9	Pay to capital providers	230.83	192.50	193.601	0	497
10	To expansion and growth	368.67	327.50	124.487	248	607
	Young age banks			**Total 6 observations**		
1	Income from banking services	986.50	980.00	183.154	804	1280
2	Cost of services	556.83	559.50	61.934	480	647
3	Non-banking incomes	3.33	.50	8.664	-8	16
4	Profit (loss) from extraordinary items	-10.50	-5.50	17.167	-45	0
5	Provisions against non-performing assets	-79.17	-43.00	91.495	-264	-25
6	Provision for possible loss written back	39.67	15.00	51.306	4	135
7	Pay to employees	101.33	98.00	26.882	70	144
8	Pay to government	93.83	78.00	39.761	57	166
9	Pay to capital providers	9.17	9.50	2.483	6	13
10	To expansion and growth	178.67	152.50	98.788	76	348

Source: Author's self calculations

Value added statement

Table 3 depicts the value added and its' allocations to employees, government, capital providers and retained in business to expansion and growth of all samples, old and young age banks during mid-July 2008. As per prior expectations, the old age banks are able to create more value than that of young age banks. Similarly, both old and young age banks are distributed approximately one-forth of its value to employees benefits.

Young age banks made provision of 24.50 per cent to government for tax, whereas the old age banks little less 23.73 per cent. As per prior expectation, the old age banks paid the cash dividend higher (one-fifth) to young age banks (2.39 per cent). In case of the retained in business to future expansion and growth of the bank, the young age banks allocated 46.65 per cent, which is lee than that of old age banks (31.60 per cent).

Table 3: Value added statement (Mid-July 2008)

(Rupees in Millions)

Value added	**All banks (12 observations)**		**Old age banks (6 observations)**		**Young age banks (6 observations)**	
	Amounts	**Per-centage**	**Amounts**	**Per-centage**	**Amounts**	**Per-centage**
Income from banking services	18590		12671		5919	
Cost of services	8954		5613		3341	
Value added by banking services	**9636**		**7058**		**2578**	
Non-banking incomes	68		48		20	
Profit (loss) from extraordinary items	(123)		(60)		-63	
Provisions against non-performing assets	(959)		(484)		-475	
Provision for possible loss written back	676		438		238	
Total value added	**9298**		**7000**		**2298**	
Value allocated						
To employees Salaries, allowances and other benefits	2350	25.27%	1742	24.89%	608	26.46%
To government Income tax	2224	23.92%	1661	23.73%	563	24.50%
To capital providers Cash dividends	1440	15.49%	1385	19.78%	55	2.39%
To expansion and growth Retained in business	3284	35.32%	2212	31.60%	1072	46.65%
Total value added	**9298**	**100%**	**7000**	**100%**	**2298**	**100%**

Source: Author's self calculation

Testing of hypothesis

To test significance of difference between two means of the old and young age banks regarding the generated value allocation to employees, government, capital providers and retained in business to expansion and growth, applying the student's t-test has tested the following null and alternative hypothesis.

Null hypothesis: H_0 : There is no significance difference between the mean values of the value allocation to employees, government, capital providers and retained in business to expansion and growth.

Alternative hypothesis: H_1 : There is no significance difference between the mean values of the value allocation to employees, government, capital providers and retained in business to expansion and growth.

Table 4 reports the means, standard deviations, p-values and its' statistical test results of two means of the old and young age banks regarding the generated value allocation to employees, government, capital providers and retained in business to expansion and growth.

It is obvious from the table 4 that the null hypothesis has been rejected in respect of all four components of value allocation to employees, government, capital providers and retained in business to expansion and growth. Hence, the alternative hypothesis of statistically significant difference has been accepted. From the result, it can be inferred that the value allocation between the old and young age banks was statistically significantly different during the period of study.

Table 4: Mean values, standard deviation and t-test (Mid-July 2008)

(Rupees in Millions)

Value allocated	Old age banks (6 observations)		Young age banks (6 observations)		p-value	Result
	Mean	S.D.	Mean	S.D.		
To employees Salaries, allowances and other benefits	290.33	108.78	101.33	26.88	0.002	Significant at 1% level
To government Income tax	276.83	103.01	93.83	39.76	0.002	Significant at 1% level
To capital providers Cash dividends	230.83	193.60	9.17	2.48	0.019	Significant at 5% level
To expansion and growth Retained in business	368.67	124.49	178.67	97379	0.015	Significant at 5% level

Source: Author's self calculation

V. Conclusion

The old age banks are generated higher amount of value added in comparison to young age banks. Nepalese banks are seemed to allocate sufficient portion of value added to the future business expansion and growth, which provided ample size of capital. The wealth distribution to employees, government, capital providers and retained on business is significantly difference between the old and young age Nepalese banks.

Value Added Statement (VAS) is a supplementary additional report of Profit and Loss Statement. Now a day, such value added statement is one of the new technique as regard a part of social responsibility accounting and reporting to the stakeholders. In the context of the Nepal, still there is no mandatory provision for preparing and reporting VAS to their stakeholders. The study provides financial information in a better way and it is very much useful to judge the performance and productivity of the Nepalese commercial banks for decision-making aspect by the stakeholders.

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Annex – 1: List of sample banks

S. No.	Bank's Name	Established Date	Group
1	Nabil Bank Limited	1984/07/16	Old age bank
2	Nepal Investment Bank	1986/02/27	Old age bank
3	Standard Chartered Bank Nepal Limited	1987/01/30	Old age bank
4	Himalayan Bank Limited	1993/01/18	Old age bank
5	Nepal SBI Bank Limited	1993/07/07	Old age bank
6	Everest Bank Limited	1994/10/18	Old age bank
7	Bank of Kathmandu Limited	1995/03/12	Young age bank
8	Nepal Industrial & Commercial Bank Limited	1998/07/21	Young age bank
9	Machhapuchhre Bank Limited	2000/10/13	Young age bank
10	Kumari Bank Limited	2001/04/03	Young age bank
11	Laxmi Bank Limited	2002/04/03	Young age bank
12	Siddhartha Bank Limited	2002/12/24	Young age bank

Source: List of banks and established date are from Bank statistics, NRB, No. 51, group formation by author