

# Financial Performance Management of The Bank

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**Abstract:** *The objective of this paper is to provide a theoretical review and a complete description about financial performance management of the bank. Method used in this review is the study of literature or theoretical studies. Result of this review indicates that (1) bank's financial performance is measured with some parameters such as Earning per Share (EPS), Return on Equity (ROE), Return on Asset (ROA), revenue growth, loan growth, net income growth compared to profit planning, saving growth, Return on Investment (ROI), and Net Present Value (NPV); (2) financial parameters are measured depending on accounting methods or treatments used to prepare the financial statement of the bank; (3) Financial ratio is the comparison of two variables of financial data to explain the relationship between those two; (4) Some financial ratios are used by an analyst to measure financial performance, such as: Profitability Ratio, Liquidity Ratio, Solvability Ratio, Activity Ratio, Growth Ratio, Market Value Ratio, and Economic Value Added; (5) The analysis over these ratios is fulfilling not only the internal interest but also external interest of the firm, because it is useful (a) to compare the firm with other firm at similar business sector, (b) to compare with other at different business, and (c) to compare the performance at different period of time.*

**Keywords:** *management, performance, financial, bank*

**Abstrak:** Tujuan dari penelitian ini adalah untuk memaparkan revid teori dan deskripsi lengkap tentang manajemen *performansi financial* pada bank. Metode yang digunakan dalam review ini adalah kajian *literature* dan kajian teori. Hasil dari review menunjukkan bahwa, (1) *performansi financial bank* diukur dengan beberapa parameter seperti *Earning per Share (EPS)*, *Return on Equity (ROE)*, *Return on Asset (ROA)*, pertumbuhan pendapatan, pertumbuhan pinjaman, pertumbuhan sisa hasil usaha dibandingkan dengan perencanaan keuntungan, pertumbuhan simpanan, *Return on Investment (ROI)*, dan *Net Present Value (NPV)*; (2) parameter *financial* diukur berdasarkan metode penghitungan atau perlakuan digunakan untuk menyiapkan pernyataan *financial* pada bank; (3) *financial rasio* adalah perbandingan antara dua variabel data *financial* untuk menerangkan hasil keduanya; (4) beberapa *financial rasio* digunakan oleh analisis untuk mengukur *performansi financial* seperti *Profitability Ratio*, *Liquidity Ratio*, *Solvability Ratio*, *Activity Ratio*, *Growth Ratio*, *Market Value Ratio*, dan *Economic Value Added*; (5) Analisis rasio tersebut tidak hanya memenuhi ketertarikan internal dan eksternal suatu perusahaan karena berguna untuk (a) membandingkan perusahaan satu dengan yang lain yang mempunyai sektor yang sama, (b) membandingkan dengan bisnis yang lain, dan (c) membandingkan *performansi* dalam jangka waktu yang berbeda.



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**Kata Kunci:** manajemen, kinerja, keuangan, bank

Financial performance of the bank is understood by measuring several parameters such as *Earning per Share (EPS)*, *Return on Equity (ROE)*, *Return on Asset (ROA)*, revenue growth, loan growth, net income growth compared to profit planning, saving growth, *Return on Investment (ROI)*, and *Net Present Value (NPV)* (Hilton, 1997). A ratio may be good in certain time, but others may not (Weston & Brigham, 1994).

The measurement of financial performance with financial parameters will depend on accounting methods or treatments used to prepare the financial statement of the bank. Bank's performance that is perceived as good and improving may not be such in reality.

Financial ratio is the comparison of two variables of financial data to explain the relationship between those two. An analyst may understand financial performance using several financial ratios such as following. First, *Profitability Ratio* is used to measure the ability of firm to obtain profit from sale, asset total or self capital. Second, *Liquidity Ratio* is used to measure the ability of firm to meet the short-term financial duty on deadline. Third, *Solvability Ratio* is used to measure the ability of firm to pay debts if the firm must be liquidated. This ratio also shows how much fund can be obtained by the firm from external or creditor. Fourth, *Activity Ratio* is used to measure the ability of firm to use the fund available in the capital circulation. Fifth, *Growth Ratio* is used to measure how good the firm is to maintain its economic position. Sixth, *Market Value Ratio* is used to provide indications to the management about investors' opinion on firm achievement in the past and also the future prospect. If other ratios are good, market ratio must also be good with favorable impact on stock price.

The analysis over these financial ratios is useful in meeting not only the internal but also external interests of the firm (Hampton, 1998). These financial ratios will remain useful when: (a) to compare the firm with other firm at similar business sector, (b) to compare the firm with other at different business, and (c) to compare the performance at different periods of time.

Although the analysis over financial ratios may provide useful information, it still cannot escape from limit (Weston & Brigham, 1994).

Different from the analysis over financial ratios, a measurement of performance will show the actual achievement of management by fostering the activities or strategies which generate economical values (*value added activities*) and eliminating those which destroy values (*non-value added activities*). A relevant feature connecting the measurement of bank performance to that of bank profitability is *Economic Value Added (EVA)*. The background of this review is that research journals have stated that *EVA* is a hot topic discussed in several firms in USA. As defined by Stern Stewart, *EVA* represents the difference between after-tax net operational income of firm and the capital cost for equity and debt (Stewart, 1993). *EVA* is a very relevant new concept to assess bank financial performance because *EVA* can measure the performance (achievement) of management based on the added value created during certain period (Utomo, 1999:28).

Taking this into account, the author feels necessary to do a review about financial performance of bank to obtain a description of the development of a certain bank.

Therefore, the objective of this paper is to provide a theoretical review and a complete description about financial performance management of the bank. Method used in this review includes the study of literature or theoretical studies.

## FINANCIAL PERFORMANCE OF BANK

Helfert (1991:52) describes financial performance of firm as follows:

Firm performance is the outcome of all decisions made by the firm in sustainable manner. Therefore, firm performance is assessed by connecting the cumulative financial performance to the economic of those decisions. The analysis over financial performance is conducted based on published financial data as mirrored within financial statement prepared with generally accepted accounting principles.

Next, Helfert (1991:53–54) admits that party with interest in evaluating firm performance is firm stakeholders including investor, manager, creditor, government and peoples, or even investor candidates. They will assess firm based on financial measures.

A party who concerns with firm's daily activities is firm management. Managers take the responsibility for the efficient and effective usage of fund and other economic resources in managing the firm. Investors insist on understanding firm profitability as mirrored within profit growth and firm dividend, which in turn will increase firm value.

In other side, creditors and other lenders, either for short-term and long-term, feel necessary to recognize the payout of interest and principal in terms of number or timing of payment. The ability of meeting the duty is indicated by the value of firm that is used as guarantee against investment or risk incurred by the creditors. Other parties such as government and other group always feel important to acknowledge the true rate of tax and the ability to pay wage.

The decision made by the management may be different between banks. This difference can influence firm efficiency. Darmodaran (1997:657) says that *"The value of the firm is determined, in large part, by the decision that the management makes - what assets to invest in, how much leverage to take on, and how much to pay out as dividend, to name a few"*.

It means that the decision made by management about what assets to invest, how much leverage to take, and how much dividend to pay will determine firm value.

In bank business, Sinkey (2002:4) uses several terms which seem identical between bank context and general business context. These terms are asset management which is identical to investment decision (I), liability management which is identical to funding decision (F), and dividend decision which is identical to capital/dividend management (D).

Holt & Karen Walewski (1984) have studied banks with high profitability. Their result shows that factors influencing high profitability are: (1) Effective management over asset and liability in portfolio and risk if compared to the balance; (2) Aggressive price for service (*fee based*) to maintain high quality and (3) More funding is obtained from debt and more allocation is given to income-generating asset.

In aligned with phenomena of bank industries in Indonesia, a question rises: Is there a relationship between asset-liability management, financial performance, and firm efficiency within Indonesia

banks? Asset-liability management is reflected within asset-liability portfolio selected by the bank. It is estimated that there is a relationship between asset-liability management, financial performance, and firm efficiency, and there is different asset-liability management between efficient and inefficient banks.

Asset management is indicated in selected asset portfolio, which comprises of attributes such as: (1) placement indicators compared to other bank, (2) security, (3) credit issued, (4) other placement, (5) asset total growth, and (6) commitment-contingency receivable growth.

Liability management is shown by attributes such as (1) funding portfolio indicators based on demand deposit, saving, time deposit, and deposit certificate, (2) security, (3) receivable loan, (4) equity, and (5) commitment-contingency duties growth.

Asset-liability management describes the ability of the bank to integrate selected portfolios of asset-liability. Successful integration of asset-liability is measured by indicators such as *rate sensitivity rate to rate sensitivity liabilities (RSA/RSL)*, *net interest margin (NIM)*, equity to risking asset (*Capital Adequacy Ratio*), *burden ratio*, and ROA. The ratio of interest revenue to asset total, the ratio of non-interest revenue to asset total, and *loan to deposit ratio (LDR)* are also considered.

Bank management has three main activities which are interdependent to each other. First, activities in *liability* group are those related to the ability of bank to collect or mobilize fund from fund sources at low cost to meet the demand of bank asset. Second, activities in *asset* group are those related to the ability of bank to distribute the available fund to many credit facilities in order to obtain high interest income and to improve the profit derived from the difference between interest rates of the loaned fund and the collected fund. Third, the activities that are considered as *baking services* are the functions of bank to provide services in the payment traffic. Services given by the bank to customers will produce *fee-based income*. Final goal of all three activities is to obtain maximum profit.

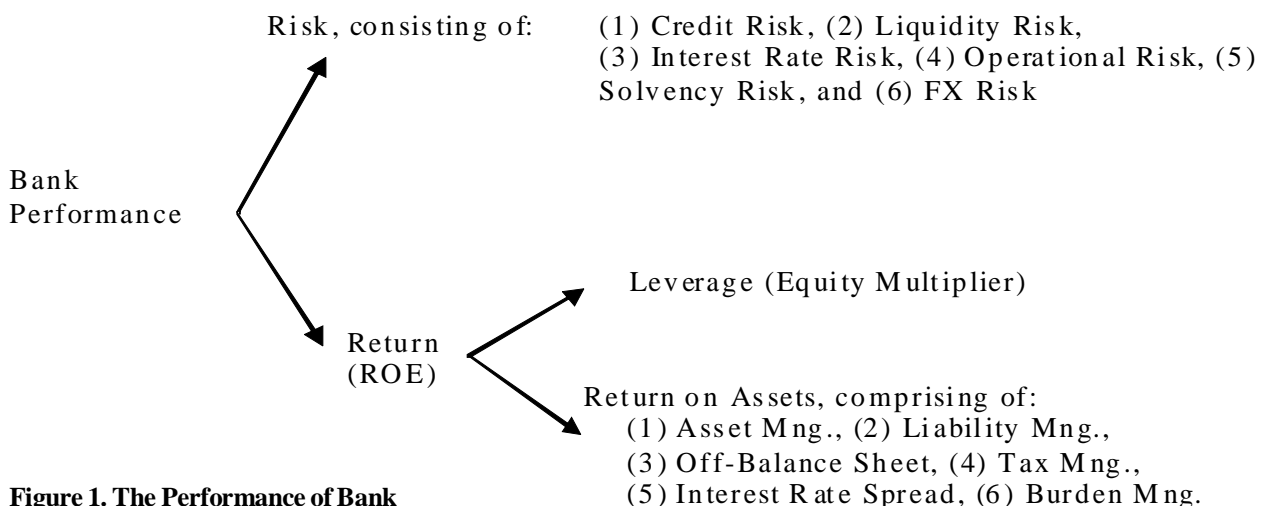
Sinkey (1986:197) explains that bank performance as reflected from ROA is determined by *net interest margin* or *interest spread* and *net non-interest income* or *burden*. *Net interest margin* is a function

of rate, volume and mix or  $NIM = f(\text{rate, volume, mix})$ . The higher difference between interest rates of loaned fund and collected fund is the higher ROA, so is the reverse. The higher comparison between volumes of loaned fund and collected fund, or called as LDR, is the higher ROA, so is the reverse. ROA of the bank is determined mostly by high or low level of interest spread rate and LDR (*Net Interest Margin*).

Sinkey (1986:212) adds that ROA of bank is determined not only by interest factor, but also non-interest factor, called *net non-interest income* or *burden*. The higher *non-interest* income from services provided by the bank is the higher ROA of the bank.

Francis (1994), as quoted by Santoso (1996:164–165), asserts that bank financial performance is involving some considerations or factors of risk, such as (1) Credit Risk, which is incurred when receivable is not paid; (2) Liquidity Risk, which is incurred when the fund needed for short-term duty is lacking; (3) Interest Rate Risk, which is incurred due to the sensitivity to the change of funding/costing in trade; (4) Operational Risk, which is incurred for operational efficiency of bank works; and (5) Solvency Risk, which is incurred to deal with cash flow problems.

The analysis over financial risks above is often conducted either in trade, industry or bank. A model of this analysis can be illustrated as following:



**Figure 1. The Performance of Bank**

Source: Francis, 1994

## Factors Influencing Financial Management

After analyzing over banking conditions, Amling (1989:14) has reported that the factors influencing firm performance are: (1) *Future earning*, (2) *Management*, (3) *Operating efficiency*, (4) *Current financial position*, (5) *Capital structure and long term debt analysis*, and (6) *Profitability*.

These factors are elaborated as follows: (1) *Future earning*. This factor is influenced by firm growth and measured by asset total growth. Bank with stronger position in competition will have relatively stable earning than the weaker bank. (2) *Management*. The quality of management can determine the future of firm. Without good management, a firm is unable to control the expended operational cost or to maintain its financial position. Managerial wisdom in leading the firm may be seen from the ability to produce profit in the future. (3) *Operating efficiency*. This factor reflects the relationship between firm expense and firm income. Operating efficiency is measured by several operating ratios. The lower operating ratio is the higher firm income. (4) *Current financial position*. This factor is also called liquidity position which is a fundamental issue in the finance. It is a measure to balance between liquidity and profitability. The balance of both attributes is a *tradeoff* between the supply of available fund to pay short-term duty of firm and the ability of firm to get profit. (5) *Capital structure*. The firm will use

methods to improve the fund to finance the operation. Capital structure of the firm may influence future income because it can determine the quantity and stability of income. The costing by the loan may put stockholders at risk. Big loan may lead to unstable income and accelerate firm failure due to the heavy expenses. (6) *Profitability*. This factor is used to estimate future income and also the expected income in the future. A more stable income growth will improve firm value in the future.

### Decisions in Financial Management

Three important decisions are made on financial management, and the goal of these decisions is to maximize firm value. According to Sinkey (1986:33), the goal of maximizing firm value is formulated as follows:

$$\text{Max } V = f(I, F, D)$$

where:

I = Decision of Investment or Asset Management

F = Decision of Financing or Liability Management

D = Decision of Dividend or Capital Management

V = Firm Value

$$V = V_D + V_E$$

$V_D$  = Market Value of Debt

$V_E$  = Market Value of Equity

Koch (2000) declares that the strategies to maximize firm value of the bank will need the policymaking on several issues such as (1) *asset management (composition, volume and pricing)*, (2) *liability management (composition, volume and pricing)*, (3) *management of off-balance sheet activities*, (4) *interest rate spread management*, (5) *credit risk management*, (6) *liquidity management*, (7) *management of burden*, and (8) *tax management*.

### Firm Value (Corporate Value)

Financial management is the management against financial function. Financial function of the bank is a matter of how to generate fund (*raising of fund*) and how to use fund (*allocation of fund*). The management against financial function is successful only if the expected goal is achieved. Usually, the goal is to maximize firm value.

Various models have been proposed by experts to measure firm value. Modigliani & Miller (1961) are measuring firm value as the present value of future cash flow. This feature is called as *market value added* (MVA). In practice, MVA is difficult to measure because market value always changes even for any reasons less related to operating performance. Meanwhile, it is impossible to use MVA for business which does not have market value or stock price.

Rappaport (1986:51) suggests that main components of firm value are: (1) *The present value of cash flow from operations during the forecast period*, (2) *Residual value, which represents the present value of the business attributable to the period beyond the forecast period*, and (3) *Current value marketable securities*.

Pursuant to Sinkey (1986:27), the measurement against firm value is applying a concept of *valuation rules* because of the effect of *value addition*, meaning that total value equals to the addition of the components. Sinkey exposes that "Market value of the firm,  $V$ , is simply the sum of the market value of equity,  $V_E$  plus the market value of debt,  $V_D$ . That is  $V = V_E + V_D$ ".

Sinkey formulates firm value from three components as follows:

Firm Value of The Bank	=	Value of All-Equity	+	Present Value of Tax Shield From Debt	-	Present Value of Cost of Financial Distress
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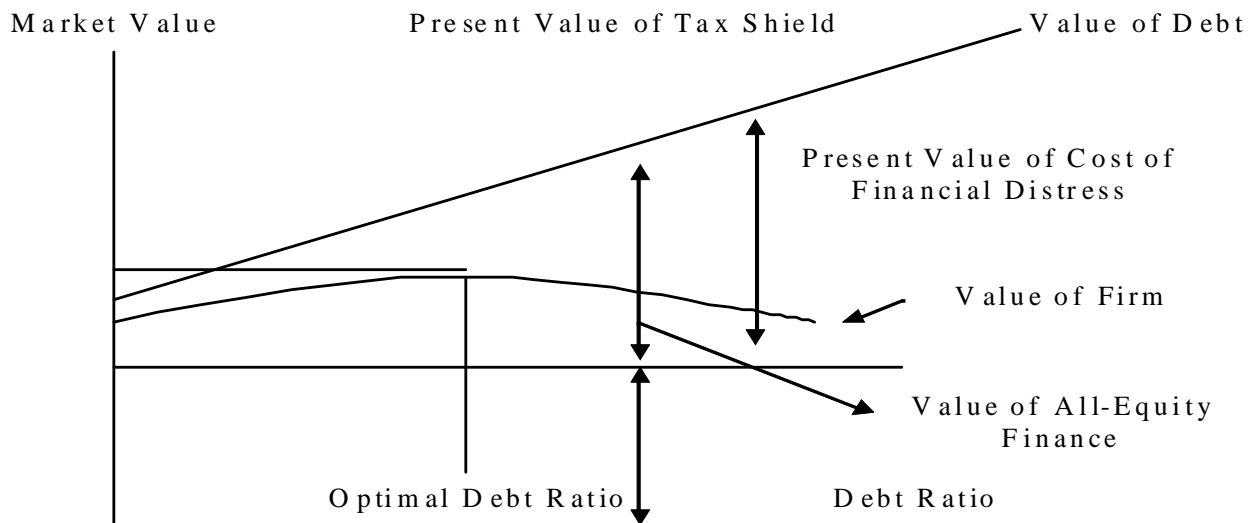
Here, Sinkey stresses that firm value of the bank is summed from the value of all bank equities plus the present value of tax shield minus the present value of cost of financial distress.

*Present value of tax shield* is the saving of tax due to the use of debt. *Cost of financial distress* is a complex interaction of *liquidity cost*, *bankruptcy cost*, *capital regulation* and *deposit insurance*.

A moderate debt has low probability of *financial distress*. Therefore, present value of *cost of financial distress* may increase fast with additional loan, and *cost of financial distress* can erode work value of the firm.

Hempel (1991:87) admits that for any banks which their stocks are not actively traded, value maximization is given only to the owner by *discounting the net cash benefits*.

Copeland (1994:131-151) asserts that EPS (*earning per share*) is a value indicator which



**Figure 2. The Value of Banking Firm**

Source: Sinkey JF, Jr (1986:34)

disregards the important factor influencing firm value and leaves the manager alone to make destructive decisions for long-term issue. Even, stock price is difficult to improve at short term. EPS is also *maximum accounting earning*. The approaches of *entity model* or *discounted cash flow* (DCF) have determined that work value is future cash flow which is discounted at a certain level to reflect the risk of cash flow. Some experts argue, however, that in practice, the definition of cash flow is often ambiguous because it is difficult to determine the appropriate *discount rate*.

In elaborating *Economic Value Added* (EVA) or *Economic Profit Model* (EPM), Copeland (1994:145) says that the measurement of the value added of firm at single period is using a formula: *Invested Capital x (ROIC - WACC)*. "Economic Profit Model (EPM) is the spread between return on invested capital and the cost of capital, times the amount of invested capital". Firm value equals to the addition of the invested capital with the premium, which is *present value* of the value that may be created in the future. Compared to DCF, EPM is better measurement for annual performance of firm, while *free cash flow* is not.

### Conventional Measurement of Financial Performance

A conventional method to measure financial performance is often causing troubles because it only

relies on *debatable* assumptions. Such assumptions are easily triggering *miss-estimation* and *mark-up practice* that must be beyond control of the management itself. This phenomenon is visible during banking failure in Indonesia where many projects/works are considered as feasible based on conventional measures such as *Payback Period*, *IRR*, *NPV* and others. But, this feasible status cannot help these projects to show the expected performance (Kaplan & Anthony, 1998).

Quantitatively, the quality of conventional system is quite accountable, but in qualitative sense, it raises big question. Using the result of conventional method may be a controversy because the inputted data are produced from the regression against historical data which may be *unpredictable*.

The systematic diagram of conventional assessment is illustrated in the following figures 3.

The input in form of assumptions with questionable accuracy may produce output with quite great deviation. There are three (3) levels of sensitivity, as follows 4.

Three sensitivity levels above have double implication to the assumptions. Over-estimation is occurred if data are too optimistic and under-estimation is apparent when data are pessimistic. Both implications are risky because these are not reflecting the actual condition. Conventional assessment over financial performance has weaknesses such as (1)

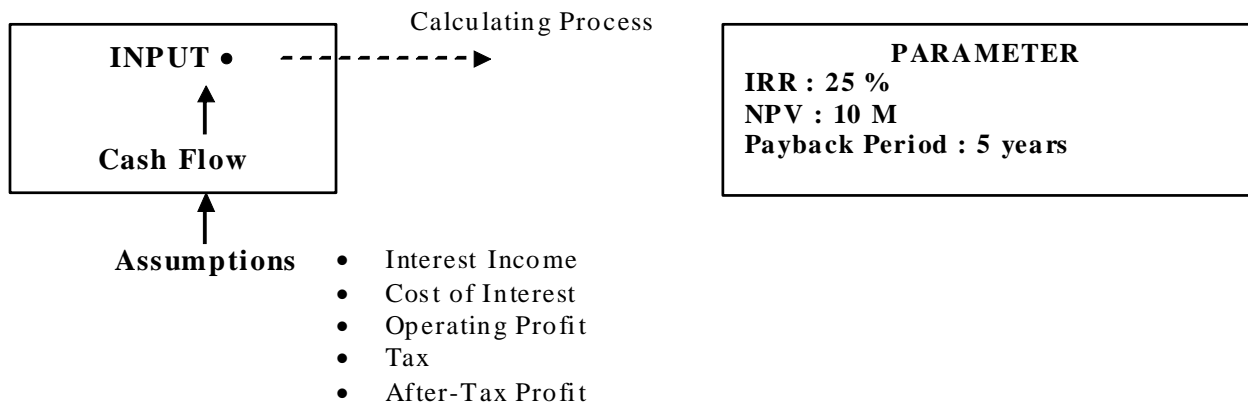


Figure 3. Conventional Assessment

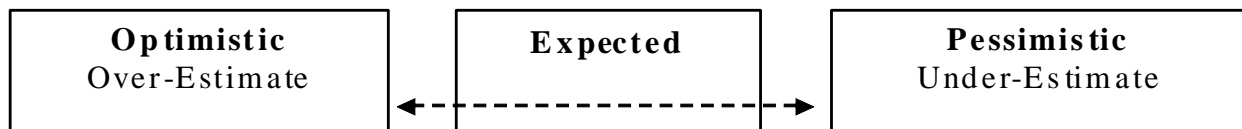


Figure 4. Sensitivity Levels

input and output are greatly influenced by the realization of operational steps; (2) the management is only passive and unable to do something to influence the assumptions; and (3) strategic steps are lacking and the realization is only depending on *spot condition* where assumptions may not be relevant.

### Financial Ratios

Finnerty (1986:84), Foster (1986:96), and Gibson (1990:120) have explained that firm performance is measured to ensure whether it grows or not. This measure is also useful to be used as the base for future decision making by the management.

The experts above also declare that the most usually used measure is financial ratios. The use of financial ratios to evaluate firm performance is also supported by reviews and studies of the experts and researchers in financial management field.

Van Horne (1992:725) has supported Gibson by stating that financial performance of the firm is evaluated with certain measures. The most usually used measure is ratios or indexes related to financial data. Ratio can be defined as the relationship of two components.

The development of this analysis is through evolution since the beginning of 1900 until now. Many

researches on financial field have used financial ratios as their research variable such as Altman (1968:589), Beaver (1969:580), and Vitranen (1984:371), and Latinen (1990:150).

Bowlin et al (1990:13) have said that:

*"Financial analysis utilizes the information contained in the firm's financial statements, the balance sheet and the income statement. The primary tool of financial analysis is financial ratios"*.

In other words, Bowlin attempts to say that information from firm's financial statement, balance sheet and income statement are useful materials in the financial analysis, while the most important tool for financial analysis is financial ratios.

In relative with the use of financial ratios, Shapiro (1991:729) has suggested that:

*"In seeking such clues, the most important tool for financial detection is ratio analysis. This technique can help you to interpret relationship between figures of two or more comparable sets of financial statements for different periods of time or different companies."*

Indeed, Saphiro attempts to say that ratio analysis will be helpful if it used to interpret the

relationship between figures of two or more sets in financial statements made at different schedules or by different companies.

Gibson (1990:123) suggests the use of financial ratios in analyzing financial performance as follows:

*"Using the past history of firm for comparison is called trend analysis. By looking at a trend in particular ratio, one sees whether that ratio is falling, rising, or remaining relatively constant. From this, a problem is detected or good management is observed. The analysis of an entity's financial statements can be more meaningful if the results are compared with industry averages and with results of competitors."*

Gibson attempts to conclude that financial analysis that uses firm historical data for base of comparison is called *trend analysis*. By observing a trend of certain ratio, whether the ratio is decreasing, increasing, or relatively constant is then understood. A problem is then easily identified and whether management works well is also recognized. The analysis over firm's financial statement will be meaningful if the results are compared with the average figures of firms/industries or with those of competitors. Indeed, the average figures of firms/industries are representing the financial average of some similar firms that compared to each other to determine firm position.

Foster (1986:176) supports this suggestion by stating that:

*"Financial statement data are often used in comparative mode, such as in cross-sectional application, which is a comparison of one entity with other entities at the same point of time, or in time-series application, which is a comparison of one entity at different points of time."*

Foster attempts to propose that financial statement data are often used in comparison models. A comparison model is cross-sectional which compares one firm to other firm at similar period of time, while other is time-series model which compares only one firm at several periods of time. In other words, there are two kinds of financial evaluation, which are the analysis of trend and the analysis of average figures of firms/industries. Both evaluations are more accurate if used simultaneously.

Pursuant to opinions of the experts above, financial ratios shall be used as a tool to measure the successful activities of the firm in the financial field. The usage may be more accurate if financial ratios are relevant and/or if the ratios are interdependent to each other. Finally, financial ratios may be compared to previous financial performance to ensure whether there is progress or not.

## Earning and Earning Growth

The word "earning" is used to refer income or profit. In the accounting, earning is measuring the successful operation of firm at certain period. Income statement (profit/loss statement) provides information which must be helpful for investors and creditors in estimating amount, time and uncertainty of future revenue.

Accounting method that is used to prepare income statement is very influential to earning. A financial accounting book has stated that *"income numbers are often affected by the accounting methods employed"* (Kieso and Weygant, 1998:147). Different methods to assess the inventory and the depreciation of fixed asset across periods may produce different earning. The owner of firm often underestimates the importance of measuring the successful operation of the firm. The owner is always to compare income statement across periods to ensure whether the management performs well or not. It is then concluded that earning or profit is a measuring instrument that cannot be used independently to evaluate the performance of management.

*Earning growth* or profit growth is a misleading financial performance because earning growth never considers the added-value created by the firm. For example, two different firms, Firm X and Firm Y, are producing similar amount of earning and have similar earning growth. Firm X invests more capitals than Firm Y to maintain its earning growth. Firm X tends to use any forms of investment as long as its earning growth is fixated. Firm Y is superior in capital usage because this firm is more efficient in using the capital. The growth without commitment to good capital planning is a sign of the falling of the firm. *"In such, rapid growth can be misleading indicator of added-value because it can be generated simply*



by pouring capital into a business. Earning on acceptable rate of return is essential to create value. Growth adds to value only when it is accompanied by adequate rate of return” (Stewart, 1999:40).

### Return on Investment

Return on Investment (ROI) is a measuring tool that is mostly used to measure performance of an investment center. “Indeed, ROI can measure effectively the company’s assets that are used to generate profits” (Bierman & Dyckman, 1976:391). A formula to calculate ROI is that operating profit is divided with average rate of investment in one period. Moreover, ROI is better than earning if it is to measure the profit from operating activities of the firm.

### Economic Value Added (EVA)

Different from the analysis over ratios, a measurement of performance may show the actual achievement of management by aiming to foster the activities or strategies which generate economical values (*value added activities*) and to eliminate those which destroy values (*non-value added activities*). A component that is relevant to connect the measurement of bank performance to that of bank profitability is *Economic Value Added* (EVA). The background of this review is that research journals in USA have stated that EVA is the hottest topic discussed in several firms. Stern Stewart says that EVA represents the difference between after-tax net operational income of firm and the capital cost for equity and debt (Stern Stewart, 1993). EVA is also a new concept which is very relevant to assess bank financial performance because EVA can measure the performance (achievement) of management based on the added value created at certain period (Utomo, 1999:28).

The use of EVA to assess the achievement of financial operation (performance) of a bank will present the appropriate measure to implement *stakeholder satisfaction concept* because the positions of employee and capital owner are respected. It is said so because EVA is based on a fact that the measured profit of a firm is considered as fair enough if the expectations of each of *capital providers* (creditor and stockholder) are considered (Syakir, 2001:63).

EVA is also used as the guidance for *goal setting*, *capital budgeting*, *performance assessment* and *incentive compensation* of a firm (Grant, 1996). The influence of added-value in a bank must be very important because it is not negligible thing in the setting of bank strategies. EVA may also be a relevant item to measure financial performance based on value because EVA is a measure of economic value-added produced by firm/bank due to the activity or strategy of management at certain period. The principle of EVA has given a good measurement system to assess a performance and/or an achievement of firm’s financial management because EVA is closely related to the market value of a company (Stewart, 1993: 224).

Furthermore, O’Byrne (1996) adds that EVA has strengths such as: (1) EVA is an independent measure of performance and thus, other measures are not necessarily used. Also, EVA does not need trend analysis or comparison with other firms. (2) EVA can be used as the base to assess bonus given to employees. (3) EVA is focusing its assessment of firm/bank performance on value creation, which aims to maximize firm value and to improve stockholder value. (4) EVA can allow the firm to give more concern to the wisdom of capital structure. (5) EVA is useful to identify the projects with higher return from capital cost.

The weaknesses of EVA are as follows: (1) EVA only describes value creation at certain year. The value of a firm is actually the accumulation of EVA throughout firm age. It is then possible that a firm may have positive annual EVA but firm value is still low because future EVA sees it as negative. In the activities which take longer time to give return, EVA may be negative in the beginning of year, but positive in end of project because assets are sold in the end of rent schedule. Therefore, the use of EVA at certain year to assess firm operating performance is not appropriate, and therefore, *value-added* creation period must be set. (2) EVA calculation process needs to estimate capital cost and this estimation is hardly proper for go public companies.

### CONCLUSION

Financial performance of the bank is measured from several parameters such as *Earning per Share*

(EPS), *Return on Equity (ROE)*, *Return on Asset (ROA)*, revenue growth, loan growth, net income growth compared to profit planning, saving growth, *Return on Investment (ROI)*, and *Net Present Value (NPV)* (Hilton, 1997). A ratio may be good in certain time, but others may not (Weston & Brigham, 1994).

The measurement of financial performance with financial parameters is depending on accounting methods or treatments that are used to prepare bank's financial statement. Bank's performance may be perceived as good and improving but the reality may not.

Financial ratio means to compare two variables of financial data to describe the relationship between those two. An analyst understands financial performance through using several financial ratios such as following. First is *Profitability Ratio* which is used to measure the ability of firm to obtain profit from sale, asset total or self capital. Second is *Liquidity Ratio* which is used to measure the ability of firm to meet the short-term financial duty on deadline. Third is *Solvability Ratio* which is used to measure the ability of firm to pay debts if the firm must be liquidated. This ratio also explains how much fund can be obtained by the firm from external or creditor. Fourth is *Activity Ratio* which is used to measure the ability of firm to use the fund available in the capital circulation. Fifth is *Growth Ratio* which is used to measure how good the firm is to maintain its economic position. Sixth is *Market Value Ratio* which is used to provide indications to the management about investors' opinion on firm achievement in the past and also the future prospect. If other ratios are good, market ratio may also be good with favorable impact on stock price. Seventh is *Economic Value-Added (EVA)* which is a relevant measurement of financial performance because it is based on *value-added*. EVA is a measure of economic value-added produced by the firm due to managerial activity.

The analysis over these financial ratios is useful in satisfying not only the internal but also external interests of the firm (Hampton, 1998). Indeed, these financial ratios will remain useful when: (a) to compare the firm with other firm at similar business sector, (b) to compare the firm with other at different business, and (c) to compare the performance at different period of time.

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