

Profitability Analysis

Service Offer



inspiring 
development

2021

managing
financial
institutions



Profitability Analysis

Background

Current Context

- The **covid pandemic continues to accelerate**, with manifold effects on the real economy and financial sector
- Increased **credit losses, shrinking portfolios, and reduced margins and earnings often lead to lower profitability**/negative results for businesses and FIs
- It cannot be expected that economies will return to pre-covid output or sustainable growth levels in the near future
- To achieve financial stability and sustainability, **many financial institutions may need to rethink their business models and strategies**
- This **requires a deep understanding of profit and loss drivers, areas of weak financial performance, and potential areas where improvements can be made**, for which a thorough analysis is crucial

Key Challenges

- A simple analysis of financial statements and ratios is insufficient. It is **important to establish a set of tools and indicators that provide an in-depth understanding of the factors influencing profitability**
- It is necessary to **split the overall business into segments/units and to understand the profitability of each segment and unit** and its key products
- The financial performance of many business segments/products, albeit good in the past, may have weakened: **it is important to identify which profitability components can be improved and how**
- An **in-depth assessment of margins and pricing** and their components is **crucial** for institutions to be able to identify drivers
- **Institutions** with established tools and profitability analysis **may need to review and adjust their models and approach** in order to reflect the current environment

- **Having in place a system of regular financial analysis and reporting, on both a segment or unit and institutional level, allows stakeholders to make well-informed decisions to better steer the institution forward.**



Profitability Analysis

Our Solutions

Profitability Analysis: Institutional Level

- Review/**development of tools** for profitability analysis; **setting of adequate indicators** and reporting tools
- **Review of main cost items and efficiency indicators as key profitability factors**, comparison with best practice benchmarks, recommendations for improvement
- **Review/(re)establishment of organizational setup** for the purpose of conducting profitability analysis and monitoring

Segment/Product Analysis

- Review/**development of tools for segment/product profitability analysis**
- **(Re)definition of client segments (and sub-segments)** and products for the purpose of profitability analysis
- Establishment of rules and **tools for allocating income and costs** (direct and indirect) to client segments/products
- **Definition of targeted or acceptable profitability levels**
- **Calculation of profitability of client segments/products**
- **Identification of loss-making or low-margin products and client segments**, and identification of sources of improvement

Branch Profitability

- **Review/development of tools for branch profitability** calculation and analysis
- Establishment of **rules and tools for allocation of income** and direct and indirect costs to branches
- Setting financial and efficiency indicators to identify areas of weak performance and make branches comparable
- Definition of targeted or acceptable profitability levels

Funds Transfer Pricing (FTP)

- **Implementation of FTP**
- Setting of **rules and tools for computation of key components** (FTP curve, commercial contribution margin, maturity transformation margin)
- **Provision of guidance on interpreting results**

Product Pricing

- **Development of pricing methodology** and setting of pricing components
- **Setting of rules for computation of cost of funding, risk premium, operating cost margin, capital charge and profit margin**
- **Provision of guidance on segmenting clients or products** for which different prices should be set



Implementation

Our Approach

Review and Analysis

- **Initial desk-based review of:**
 - **Existing tools, reports and indicators** being used for profitability analysis
 - **Operational and financial data** on key client segments/products
 - **Key efficiency indicators**; comparison with benchmarks
 - **Key processes**

Development of (New) Tools and Analysis

- **Setting up new tools, analysis and profitability and efficiency indicators** based on:
 - **Interviews with key managers** to understand their needs and challenges in managing the financial performance of their respective segments
 - **Discussion with managers and staff members on key processes and the work division between staff**, to define profitability centers and set models for distribution of income and expenses

Implementation Support

- **Support management in setting up an organizational framework for a new profitability analysis** and proper handling of the results by:
 - Redesigning the process of regular analysis of **profitability** and its components, and developing related reports
 - **Setting of target values for key profitability and efficiency indicators** by (staff) position or client segment
 - **Developing policies, procedures, and concept papers** on profitability analysis and monitoring
 - **Holding workshops with key staff members to explain the analysis methodology and results**, (new) profitability and efficiency targets set by segments/products, and their role in achieving those targets



Contacts

Ardian Salihu



Senior Banker

salihu@inspiring-development.com

+44 754 7606 739

We would be glad to discuss your specific requirements and to provide:

- Further information on our services and approach
- Possible service packages to address specific needs
- An individualized quote

Svetlana Tolmacheva



Senior Banker

tolmacheva@inspiring-development.com

+381 63 640 261

This document was compiled by:

I.D. Inspiring Development GmbH

Eschborner Landstrasse 42-50, Haus B
60489 Frankfurt am Main / Germany

Phone +49 69 678 30 79-0

Fax +49 69 678 30 79-99

info@inspiring-development.com

www.inspiring-development.com