# Financial and Operational Performance of Cooperatives in Northern Province

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**ABSTRACT**

There is huge investment employed during the last four years by cooperative societies in the Northern Province. Since the overall performance of them are not at the expected level, there is a need to examine them in terms of their financial and operational performance of the cooperatives so as to establish their current status in terms of assets utilization, performance of their business activities and see whether they satisfy the needs of their stakeholders.

In this study, the researchers adopted multiple methods such as focus group discussion, key informants interview, and direct observation for primary data collection. The researchers designed tools for collecting data from different stakeholders of the co-operative societies. The secondary data were collected from the documents related to all the activities from 2009/2010 to 2012/2013.

Though considerable amounts of resources are available for the cooperatives, it seems that the Board of Directors and the management do not know how to utilize the resources at their maximum and get benefit from them. The examination of their business activities indicates that most of the activities are very relevant and potential to the societies. However, most of the activities are running at losses. This raises questions as to why those activities are running at a loss. After the civil war, the cooperatives concerned received altogether Rs. 231.56 million as support from the organizations such as UN agencies, International NGOs, Local NGOs and the Government. However, it was found that the returns out of these investments are meager and inefficient management is the challenge that has to be addressed immediately to revive them**.**

**Keywords:** Performance, Co-operatives, Finance

## 1. INTRODUCTION

The main purpose of the co-operative societies is aimed at meeting the common needs of the people in societies in the world. It is a form of organization in which the members unite together to satisfy their common needs such as economic, social and cultural needs. Delivering essential goods, providing credit facilities to poor members, and marketing facilities to market their products are some of the major functions of the co-operatives. *Sri Lanka being agriculture based country; the co-operative sector has a major role to play in uplifting the living standards of the people.* This sector has been an exemplary field in the Northern Province.

Co-operative societies in the Northern Province are expected to take part in uplifting the lives of vulnerable people and displaced communities. During the conflict, they lost considerable assets and most of their administrative records were lost. In the meantime, during the past three years, they have been supported by many organizations such as Department of Cooperative Development (DCD) and various donor agencies and NGOs. Many facilities were provided by these organizations for improving, reestablishing and establishing the co-operatives in the North. The facilities were given in the form of buildings, equipments, vehicles, factories etc.

## 2. LITERATURE REVIEW

According to the Business Dictionary, Operational performance is measured against standard or indicators of effectiveness, efficiency and environmental responsibility such as productivity and waste reduction.

Financial performance is a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues. This term is also used as a general measure of a firm's overall financial health over a given period of time, and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation (Investopeida).

Financial analysis is the process of identifying the financial strengths and weaknesses of the firm by properly establishing relationship between the items of the balance sheet and the income statement. . In financial analysis, benchmark ratios are used for evaluating the financial position and performance of the firm. Ratios help to summarize large quantities of financial data and to make qualitative judgment about the firm's financial performance and financial position [1].

The rising intensity of worldwide business compe tition has led business entities to use different types of performance assessment tools for evaluating their financial situation. Generally, performance evaluation of the firms is conducted within the context of financial analysis. As the financial performance has a broad concept, including economic growth, return, and productivity, using the financial ratios in the performance assessment can be appropriate for companies and their counterparts [2].

According to Stallwood [3] the basic accounting information derived from financial reports does not indicate whether gained profit is sufficient or not; or are assets being used proficiently? Is the overall productivity efficient? Do the financial problems exist within the business? To answer such questions, ratio analysis can be performed in which required data are extracted from income statements and balance sheets. Rees [4] stated that financial ratio analysis responses to the amounts of information held in the set of financial statements and the problem of comparison between firms with different sizes. Using them, both analysts and investors would be able to summarize and analyze related quantitative information to obtain momentous data for appraising the firm's operation, investigating its situation in the sector, and making financial decisions [5].

## 3. RESEARCH PROBLEM

There is a huge investment employed by the co-operative societies in the North. Many NGOs and governemnt are supporting these organizations through various means. However, they are running at losses. They are facing many challenges such as most of the Boards of Directors are newly elected or temporality appointed, in some organizations, the key management posts have been filled only recently, and these posts are still vacant in the other organizations, Lack of effective HRM practices such as staffing, Human Resource Planning, Performance appraisal system, compensation, Training and development etc. are not addressed properly. Due to the emerging new operational and competitive environment, and the potential new market opportunities throughout the entire country as well as abroad, they are facing challenges,

## 4. OBJECTİVES OF THE STUDY

Since there is a huge investment made in the last four years in cooperative societies particularly in the northern province, this study aims to examine the financial and operational performance of the cooperative societies so as establish their current status in terms of assets utilization and performance of their business activities.

## 5. METHODOLOGY

In this study, the researchers designed tools for collecting data from the different stakeholders. The tools were Interview guidelines and Focus Group Discussion (FGD) guidelines which were used to collect primary data. Direct observation was also used to collect primary data. The primary data were collected using different method to cross check the information because the records were not properly maintained.

The respondents for the key informant interview were Assistant Commissioner of Cooperative Department (ACCD), Cooperative Development Officers (CDO), Presidents and General Managers, Accountants, Project Staff officers of UN Agency and Project staff officers of NGOs. Focus Group Discussions were conducted with Board of Directors, Employees, and NGOs consortium.

The secondary data were also collected by reviewing the documents related to all the activities. The collected data were analyzed. The researchers selected 6 cooperative societies in the Northern Province. The multistage sampling technique was adopted. In Northern Province three districts out of five districts were selected namely Vavuniya, Killinochi and Mullitivu in the first stage for this study. In the second stage, from the chosen districts, two co-operative societies out of six large Cooperatives societies in each district were selected as sample. For the confidential purpose, the names of the 6 cooperative societies selected for this study have not been disclosed. Instead, Co-op 1 to Co-op 6 has been used to indicate them.

## 6. ANALYSIS

The quantitative and qualitative (content) analysis were used to analyze the chosen cooperatives in terms of their operational performance, financial status, sources of funding for investment, utilization of fixed assets, human resource management, and financial performance. The analyses were carried out only for the co-operatives who have provided the access to their documents.

**Operational Performance**

Operational performances of the Co-op are analyzed with the help of the information provided by the cooperatives together with the data collected. The productivity of the cooperatives is very low in terms of their output against the huge inputs. This is supported by the ratio analysis too. With regard to marketing, most of the cooperatives are lack in marketing practices so they are losing existing customers (attrition rate is very high) and they face challenges in acquiring new customers.

**Economic status of the cooperatives**

The societies have multiple resources and perform varieties of activities. The activities and their financial performance during the period 2009/10 to 2012/13 are given in Table 1

It was found that the cooperatives involve lot of potential and relevant activities. However, the most of the cooperatives are running at losses as revealed by the above table. It raises the question why they are not taking preventive action to overcome the losses.

**Investment and Sources of Funding**

Many organizations supported the cooperatives activities. The related information is collected from the annual reports, previous records and from discussion with General Managers, Presidents of the societies and Chief Development Officer of Co-operative Department of the region. The total supports (cash and equipments) of Rs. 67.96 million, Rs.52.97 Million, Rs.41.64 million, Rs. 11.40 Million, Rs.38.69 Million, and Rs. 18.87 Million have been received by the six societies respectively since 2010.

The table 2 shows that after the war, lot of agencies supported the cooperatives to revive the industry. However, very poor returns are reported in their annual reports. It raises the questions on the sustainability of the investment employed.

**Fixed Assets (movable and immovable)**

The fixed assets are presented in the Table 1.3 for the period 2009/10 to 2012/13. It was noted that some assets were valuated Rs. 1.00 for which the documents were destroyed during the civil war. .

At present, though the assets are reported in financial reports, there are no documents for most of the co-operatives to verify the values of the assets. It was observed that proper inventory books are not maintained to record the movement of the assets.

In the meantime, valuable movable and immovable assets were given through funding agencies but they were not added with the fixed assets in most of the societies and have not been depreciated in terms of the co-operative regulations.

Further, it was found that different rates for depreciating their assets were used. There are standard rates available to depreciate the fixed assets. For instance, the depreciation rates for Land and building and Vehicles are 5% and 25% respectively. However, higher rates were used which resulted huge losses in their financial reports.

**Human Resource Management**

Some of the cooperatives provide financial benefits to their employees. Around 25% of the basic salaries are given as bonus whenever they earn profit from the particular business. Except a very few co-operatives, the employees of the other cooperatives were not motivated through any form of benefits to achieve the target of the societies. It was observed from the records and discussions that the employees are paid only basic salaries and they are not getting any other financial benefits or allowances. They are dissatisfied with their salaries and not ready to continue their works. Due to these, most of the societies are facing difficulties in retaining (qualified and experienced) staff.

Further, it was observed that the existing staffs have lack of training. Most of the staff is un-skilled including top management and they do not have knowledge on the essence of co-operative and its functions. Some employees are not qualified for the post but cooperatives are keeping them because they cannot find suitable employees with this salary.

**Financial performance**

Financial performances of cooperatives are judged in terms of its liquidity position, efficiency of its activities and its profitability. Financial performance is measured using ratios which are calculated based on the actual figures available from the financial statements.

**Liquidity Status**

Liquidity means the ability of the organization to meet its current obligations through its current assets. There are basically two ratios, namely current ratio and quick ratio, available to measure the liquidity of any organization.

**Current ratio**

The results show the bad liquidity position of the all cooperatives except one co-operative (co-op 5) throughout the four year period.

**Quick ratio**

Current ratios and quick ratios are almost the same for the co-op 1. This is because the stocks at the end of the period were not reported and not included in the current assets for most the years. In Co-op 2, this ratio indicates little healthy situation in liquidity whereas in Co-op 3, there were no healthy liquidity position during 2010/11 and 2011/12. In Co-op 4, the results show a very bad liquidity position in 2010. However, it reached at the satisfactory level in 2011. The results show increasing trend in the ratio for Co-op 5. However, the liquidity position in 2011 and 2012 were not satisfactory. Too much of working capital may indicate the inefficiency in cash management. I In 2009/2010, the ratio was satisfactory indicating better position than other years for Co-op 6.

**Activity ratios**

**Stock turnover ratio**

In Co-op 1, this ratio was very high in 2009/10 indicating the efficiency of the activities. It was more than 1000 times during 2009/10. However, it drastically dropped to 132 times in the following year and reached to merely 3 times during 2012/13. The results show the inefficiency of the society in generating income through its varieties of activities.

In Co-op 3, the comparison of these two ratios shows that the efficiency of the society in generating income has gone down during the whole period.

In Co-op 4, this ratio is high in 2011 compared to 2010 indicating the efficiency of the activities. The results show the efficiency of the society in generating income through its varieties of activities.

A mixed performance is observed in Co-op 5. . The ratio was 17.83 times 2011 indicating a high performance. However, a very little performance is reported in 2012 compared to 2013 showing a frustrating performance where as the stock turnover ratio was slightly high compared to the year 2009/10 in the year in Co-op 6. It started declining in the rest of the years indicating the inefficiency in the operating activities.

**Total assets turnover ratio**

In Co-op 1, though there was a very slight improvement in 2010/11 compared to 2009/10, this ratio dropped drastically in the following years. The ratio which was 1.04 in 2010/2011 dropped to 0.11 in 2012/2013 though the total assets of the Rs. 30.78 million in 2010/2011 has increased to the level of Rs. 56.9 Million in 2012/2013. It reveals negative trend instead of positive. In Co-op 3, The results show that the usage of assets in generating income has increased for Co-op 3 during the period. In Co-op 4, the results show that the performance and utilization of assets have been decreasing. For instance the ratio which was 5.50 in 2010 dropped to 4.64 in 2011 though the total assets of the Rs. 27.62 million in 2010 has increased to the level of Rs 49.01 Million in 2011. In Co-op 5, this ratio is also revealing a mixed performance. The performance in 2012 is almost nil (0.05 times). However, there is a improvement in 2013. In Co-op 6, though there was a very slight improvement in 2010/11 compared to 2009/10, this ratio dropped in the following years. The ratio which was 4.18 times 2010/2011 dropped to 3.32 times in 2012/2013 though the total assets of the Rs. 189 million in 2010/2011 has increased to the level of Rs. 299n million in 2012/2013. It reveals negative trend instead of positive ( Table 3).

**Fixed assets turnover ratio**

In co-op 1, though this s ratio was very high during 2009/10, compared to the following years, , it started declining from 3.16 times in 2010/2011 to 0.24 times (almost 0 times) in 2012/2013 though the fixed assets has risen with the growth rate of 161% during these periods.

In Co-op 3, as noticed in the ratio of total assets, this ratio is also revealing the same trend. This ratio has increased from 11 times to 44 times during the period indicating efficient usage of fixed assets.

In Co-op 4, after removing current assets from Total assets, the results show increasing trend in the ratios. Though fixed assets declined by Rs. 2.3 millions in 2011. This shows the efficiency in usage of fixed assets. In Co-op 5, as seen in Total assets turnover ratio, the results show a fluctuating trend in generating income in the union.

In Co-op 6, it also shows a mixed performance of the fixed assets. Though the fixed assets increased by Rs. 6

million in 2010/11 compared to 2009/10, the ratio has declined instead of increasing. The situation was worse in the following year. The ratio was 7 times though the fixed assets increased by Rs. 16 millions. However, a complete reverse situation was observed in 2012/13. The ratio increased by 4 times more compared to 2011/12 though the fixed assets decreased by around Rs. 11 millions.

**Profitability**

Profit is a yard-stick to measure the management efficiency. It is the management responsibility to use the capital employed and the fixed assets efficiently to generate adequate profit to satisfy many stakeholders. Profitability is the ability of the organization to generate profit.

**Gross profit ratio**

In Co-op 1, the results show an increasing trend in generating gross profit since 2010/11, though it dropped from 12 % in 2009/10 to 6.31% in 2010/11.

In Co-op 2, only around 3% of gross profit is earned out of 100% of net sales in 2012/2013 which is inadequate. In Co-op 3, the gross profit ratio has gone down though the assets utilization has been increased as observed in total assets and fixed assets ratios. In Co-op 4, the results show decreasing trend in earning profits from the activities. In Co-op 5, the results show that the gross profit ratio is also highly fluctuating.

In Co-op 6, the results show that the gross profit ratio is highly fluctuating from 3.50% to 9.94% during the four year period.

**Net profit ratio**

In Co-op 1, this shows a highly mix results indicating the inefficiency of the management. The ratio was almost 0 % in 2011/12. In the meantime, a huge loss was reported in 2012/13 compared to the net sales in that year which is very unrealistic situation. In Co-op 2, in figures, out of Rs. 1194 millions of sales, only Rs. 4 millions of net profit is earned by the MPCS in 2012/13 which is very unrealistic situation. In Co-op 3, this ratio reveals a disappointing performance. Out of the sales of Rs. 647.5 millions, only Rs. 2.3 millions of profits is earned during 2011/12. In Co-op 4, this result shows the inefficiency of the management. The ratio was 4 % in 2010 and the net sales were increased by Rs. 75.6 millions in 2011. In Co-op 5, the results show the total inefficiency of the management. It has negative values indicating net loss to the entity. As noticed earlier, 2012 is the worse period for the union.

In Co-op 6, the results show negative ratios for the last three years indicating net loss to the MPCS. It was positive only in the financial year of 2009/2010.

**Return on capital employed (ROCE) ratio**

In Co-op 1, except 2009/2010, it is observed a negative relationship between net profit and capital employed, instead of positive relationship.

In Co-op 3, the results show that the financial performance of the MPCS has increased to a level of around 18 % profit earned through the capital employed.

In Co-op 4, in 2010 Rs 100 of capital employed earned Rs 64.69 but in 2011 every Rs. 100 of capital employed, Rs. 133.34 of net loss is reported in 2011 which is very unrealistic. In Co-op 5, millions of capitals are employed at the increasing trend but it is noted the revenues generated through these capital employed are at the decreasing trend. In Co-op 6, except 2009/2010, it is observed a negative relationship between net profit and capital employed, instead of positive relationship.

**Return on assets ratio**

In Co-op 1, as noted in the ratios of return on capital employed, these ratios also reveal the same scenarios.

In Co-op 2, in table, Rs. 181 million of assets are employed in the business. However, only around Rs. 5 millions of profits are earned through various activities.

In Co-op 3, though this ratio increased from -2 % to 3%, the percentage earning generated through the total assets employed is very less.

In Co-op 4, as noted in return on capital employed, mismanagement of the society is once again proofed by the poor ROA ratio.

In Co-op 5, as noted in return on capital employed, the result reveals that mismanagement of the assets.

In Co-op 6, as noted in the ratios of return on capital employed, these ratios also reveal the same scenarios.

## 6. FINDINGS

In most of the cooperatives, there were no transparencies in handling money. Some of the cooperatives, quotations for buying movable and immovable assets were not obtained from the relevant authorities. Many loans were obtained from the bank against the fixed deposits of the union. Though the decisions were taken in the meetings even with a few members, approvals from relevant co-operative authorities were not obtained.

Some of the cooperatives, most of the payments for day-to-day activities were done in improper ways. Most of the funds provided by NGOs were not property spent by the societies. It was found that records for the Inventory were not maintained for fixed assets.

Almost all the payments were made without the prior approval of the ACCD of the co-operative body. In all cooperatives a petty cash system was not maintained. It was observed that the liquidity position of most of the cooperatives was at a critical level.

It was found inefficient management practices especially with regard to asset management (physical resources). It was revealed that there is no marketing plan at all to their business activities.

The employees, except some society's basic salaries are paid without any other financial benefits or allowances. Further, it was observed that the existing staffs have lack of training.

As a whole, the business activities carried out by most of the societies are not satisfactory.

## 7. RECOMMENDATIONS

Payments should be made as per the co-operative regulations and should be authorized/approved by board of directors and Asst. Cooperative commissioner. Quotations for fixed assets and construction should be obtained as per co-operative regulations. The proper procedure on calling quotations and opening them should be followed.

Inventory book for movable and immovable assets should be maintained. A petty cash system should be implemented immediately and source documents should be obtained for each and every transaction to avoid malpractices.

Store / stock ledger should be maintained with the details of purchasing, selling and the balance and should be authorized and approved for daily activities. Cooperatives should have a benchmark rate of return for each and every activity and it should not continue any activities with continuous loss.

The union should implement a scheme of financial benefits for the activities they have. Targets may be determined and the employees should be motivated to achieve the targets. A marketing plan for each and every activity should be developed so that all the activities can be carried out in a proper manner and any deficiency can be noted immediately.

## 8. CONCLUSION

The co-operative society and its development is important to the economic development in this region and the country. Only the co-operative can support the development of the individual member and the livelihood of the community. Especially, in the northern part of Sri Lanka after the civil war, role of the co-operative society is very important for utilizing the natural resources thereby generating employment opportunities, which may lead to fulfill the industry gap.

Therefore, the board of directors and management should work efficiently and effectively using the resources available to achieve the vision of the co-operative societies so that the members of the cooperatives can be benefitted through the potential and relevant activities already available. .

**Acknowledgment**

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**Table 1** Economic status of cooperatives

| Institutions | Profit or (loss) in Rs. | | | |
|---|---|---|---|---|
| | **2009/2010** | **2010/2011** | **2011/2012** | **2012/2013** |
| Co-op 1 | 1,011,154.41 | (721,194.96) | (1397024.43) | (3,965,053.05) |
| Co-op 2 | - | - | - | 4,708,544.65 |
| Co-op 3 | - | (1200488.49) | 2274228.16 | - |
| Co-op 4 | - | 6,147,955.53 | (6,342,042.04) | - |
| Co-op 5 | - | (432,879.49) | (934,524.63) | (3,946,974.90) |
| Co-op 6 | 4625788.95 | (7015843.39 | (6182961.73) | (4093915.83) |

**Table 2** Investment and support projects

| Orgn, | Investment and support project in Rs. | | | | |
|---|---|---|---|---|---|
| | **2009/2010** | **2010/2011** | **2011/2012** | **2012/2013** | **Total** |
| Co-op 1 | 3,238,339.00 | 9,349,500.00 | 8,900,000.00 | 12,005,016.00 | **67,961,240.00** |
| Co-op 2 | 9,630,319.65 | 10,543,945.43 | 10,512,684.76 | 22,289,338.05 | **52,976,287.89** |
| Co-op 3 | - | - | 22,248,767.50 | 19,400,000.00 | **41,648,767.50** |
| Co-op 4 | - | 2,500,000.00 | 8,900,000.00 | - | **11,400,000.00** |
| Co-op 5 | - | - | 2,939,589.92 | 35,756,000.00 | **38,695,589.92** |
| Co-op 6 | - | 11463000.00 | - | 7414605.55 | **18,877,605.55** |

**Table 3** Inventory of fixed assets (Movable and Immovable)

| Orgn. | Assets Type | Investment and support project in Rs. | | | |
|---|---|---|---|---|---|
| | | **2009/2010** | **2010/2011** | **2011/2012** | **2012/2013** |
| Co-op 1 | Movable | 17.00 | 6,632,359.00 | 4,788,816.75 | 8,631,335.71 |
| | Immovable | 451,008.00 | 3,514,004.61 | 7,123,234.62 | 18,151,138.42 |
| Co-op 2 | Movable | - | - | - | 2,716,791.00 |
| | Immovable | - | - | - | 34664839.66 |
| Co-op 3 | Movable | 8755078.15 | 7060976.74 | 7982616.62 | - |
| | Immovable | | 178422696.46 | 639609682.28 | - |
| Co-op 4 | Movable | 2665051.05 | 2197398.43 | - | - |
| | Immovable | 8089695.64 | 6229596.80 | - | - |
| Co-op 5 | Movable | - | 75366.00 | 8954.00 | 5970.00 |
| | Immovable | - | 842591.90 | 1450675.95 | 1585213.06 |
| Co-op 6 | Movable | 10251463.00 | 7909597.25 | 13417775.54 | 1298040.00 |
| | Immovable | 6072700.88 | 14186188.59 | 24986524.41 | 25967345.02 |