

**DETERMINANTS OF PROFITABILITY OF
COMMERCIAL BANKS IN NEPAL**

A Thesis

Submitted

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Exam Roll No: 1094/17

Class Roll No: 102

Registration No: 7-2-503-13-2012

Submitted in partial fulfillment of the requirement for the degree of

Master of Business Studies (MBS) Semester

In the

Faculty of Management

Tribhuvan University

Kathmandu, Nepal

March, 2020

CERTIFICATION OF AUTHORSHIP

I certify that the work in this thesis has not previously been submitted for a degree nor has it been submitted as part of requirements for a degree except as fully acknowledged within the text.

I also certify that the thesis has been written by me. Any help that I have received in my research work and the preparation of the thesis itself has been acknowledged. In addition, I certify that all information sources and literature used are indicated in the reference section of the thesis.

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Ashmita Khadka

March, 2019

APPROVAL SHEET

We, the undersigned, have examined the thesis entitled DETERMINANTS OF PROFITABILITY OF COMMERCIAL BANKS IN NEPAL presented by Ashmita Khadka candidate for the degree of Master of Business Studies (MBS) and conducted the viva voce examination of the candidate. We hereby certify that the thesis is worthy of acceptance.

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RECOMMENDATION LETTER

It is certified that thesis entitled “DETERMINANTS OF PROFITABILITY OF COMMERCIAL BANKS IN NEPAL” submitted by Ashmita Khadka is an original piece of research work carried out by the candidate under my supervision. Literary presentation is satisfactory and the thesis is in a form suitable for publication. Work evinces the capacity of the candidate for critical examination and independent judgment. Candidate has put in at least 60 days after registering the proposal. The thesis is forwarded for examination.

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ACKNOWLEDGEMENTS

This thesis is prepared and submitted to Office of the Dean, Faculty of Management as partial fulfillment of the requirement of the Master's of Business studies (MBS). Firstly I would like to express my gratitude to my thesis supervisor Associate Prof. Jagat Timalina for his kind supervisions and guidance. Also, I would like to thank my husband Nabin Raj Thapa and parents who headed me towards the light of education and path of truth. Due to their non-stopping guidance, co-operation and support I have been able to come out with this thesis.

Lastly, I want to thank my friends, college staffs, library staffs for their cooperation and all those who supported as well as inspired me to complete this thesis.

Ashmita Khadka

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ABBREVIATIONS

CAR	Capital Adequacy Ratio
DW	Durbin-Watson
EBL	Everst Bank Limited
FY	Fiscal Year
GDP	Gross Domestic Product
GON	Government of Nepal
i.e	That is
LOA	Loan and advance
LR	Liquidity ratio
MBS	Master of Business Studies
MOF	Ministry of Finance
Nabil	Nabil Bank Limited
NBL	Nepal Bank Limited
NEPSE	Nepal stock exchange
NPLR	Nonperforming loan ratio
NSBI	Nepal SBI Bank Limited
OLS	Ordinary Least Square
RR	Reserve requirement
SPSS	Social Sciences Computer software

VD Volume of deposit

ABSTRACTS

The paper has been built of aim of determining *profitability of commercial bank in Nepal*. Initially, the paper starts with the background of the study. The specific purpose of the study is to analyze the relationship between the bank efficiency and profitability in Nepalese commercial banks has been presented in the second part. The descriptive analytical research design has been adopted to analyze and interpret the population data. The six commercial banks have been review and analyze using SPSS method. The study found that the determinants of commercial banks financial performance in Nepal are Bank efficiency, EPS, ROA, ROE, PE Ratio, investment portfolio and cash Reserve ratio. The study conclude that the major determinants of commercial banks financial performance analysis of Nepal are bank size, liquidity, investment portfolio and cash reserve ratio. This would suggest that banks should ensure efficient and effective supervisory and related service for optimum utilization of resources.

Key Words: EPS, ROA, ROE, NPM

CHAPTER I

INTRODUCTION

1.1 Background of the study

Financial institutions are intermediaries are the transfer of financial resources among the participants in the financial system. The main participants in the financial system are individuals, businesses, financial intermediaries, and governments. In the context of financial intermediaries that carry out indirect financing, commercial banks occupy an important place (Gittman and Jochnk, 2010). Commercial Banks play an important role in the economic development of the countries. For instance, they allocate resource and channel funds from savers to investors continuously. They do so, if they get necessary earnings to cover their operational cost they incur. That is to say, for sustainable intermediation function, banks need to be gainful. Beyond the intermediation functions, the performance of banks has critical implications for economic growth of countries. Good financial performance rewards the shareholders for their investment. On the other hand, Poor banking performance can lead to banking failure and crisis which have negative repercussions on the economic growth (Grywinski, 2015).

A profitable commercial bank can withstand negative stocks and contribute to the stability of the financial system in the country. Moreover, the profitability of the banking sector of any country is important because the financial system of a country is largely based on banking system (Ali et al. 2011).The Banking sector considered to be an important source of financing for most businesses. Therefore, the profitability of commercial bank is so important which is determined by several internal and external factors or microeconomic and macroeconomic variables.

Bank profits are necessary to attract new capital to make possible the expansion and improvement of banking services. If the return of existing capital is not comparable to the returns on other investments, in the long run capital will be attracted to other economic pursuits. An important function of profits in banking is to provide reserves

for contingencies and losses that may occur incidentally to the business of banking. Finally, profits in banking, just as in other business, act as a stimulant to management to expand and improve the business, reduce costs, and improve services (Reed et. al., 2016).

Several methods may be used to measure bank profitability, all of which have some advantages and shortcomings. Profitability is generally measured using accounting ratios with the commonly used profitability ratio being ROA. ROA determines the amount of the profit earned per selling of assets. This reflects the efficiency with which the bank's managers use bank's investment resources or assets in generation of income. ROA simply connect the management efficiency and depicts how effective and efficiently the bank management operate as they employ the organization's assets into the earnings. A high ROA ratio is a clear indicator a good performance or profitability of a banking entity (Varshney and Swaroop, 2015).

Another commonly used measure of profitability is rate of return on equity (ROE). It tells how well an institution is doing in an accounting sense. This gives ideas to the stockholders about how well their investment has been utilized to give them return on their money. During the last two decades the banking sector has experienced worldwide major transformations in its operating environment. Both external and internal factors have affected in its structure and performance. Despite the increased trend toward bank disintermediation observed in many countries, the role of banks remains central in the financing economic activity in general and different segments of the market in particular. A second and profitable banking sector is better able to withstand negative stocks and contribute to the stability of the financial system. Therefore, the determinants of bank profitability performance have attracted the interest of academic research as well as of bank management, financial markets and bank supervisors.

Nepalese banking sector consists of 27 scheduled commercial banks; including 22 domestic banks, 6 foreign owned banks at the mid July 2019. Nepal Rastra Bank is the Central Bank of the country and has authority to regulate and supervise all banking companies operating in Nepal. Commercial banks need to be aware of all

those factors (internal and external) that affect their profitability performance. Whereas, internal factors related to profit and loss account shows that how competent bank's management is in creating revenues and controlling costs. Even though a lot of literatures are developed to examine the determinants of banks profitability performance, those studies show different and even contradictory results. Furthermore, Since Nepalese banking sector has shown a rapid progress in terms of number of banks, total assets and capital, widening their branch network, increasing their outreach to remote areas and continuously reporting profits of different magnitude, the examination of the determinants of profitability performance is very necessary.

1.2 Statement of the problem and research questions

Banking is a rapidly growing industry and Nepalese banking has experienced drastic and comprehensive reforms. The reform has achieved phased success, while challenges remain. Apparently, there is need for an in-depth and comprehensive study to provide performance and efficiency assessment of the Nepalese commercial banking industry (Gupta, 2004). Bank performance is the capacity of the bank to generate sustainable profitability. Bank's financial performance depends upon internal and external connectivity and capacity of the bank so that banking organization must identify determinants of profitability before introducing strategy for implementing task.

Profitability is the basic aim of establishing business and banks are not exceptions. So to identify profit determinants provide an opportunity to know which variable's influencing banks profit, management can concentrate their attention on it at the time decision making to adjust the factors. Besides, banks bankruptcies can link systematic crunch. Economic sector that has well established banking setup can also subsidize to the solidity of the financial system within boundaries of the countries. The financial crisis of 2007–09 reflected the importance of bank profitability for national economy as well as global economy, showing the need to keep it under surveillance all the time. Poor bank performance has a negative repercussion on economic growth and development. Poor bank performance can lead to failures and crises. Banking crisis

could entail financial crisis which in turn brings the economic meltdown as happened in the United States in 2007. That is why governments regulate the banking sector through their central banks to foster a sound and healthy banking system which avoid banking crisis and protects the depositors and the economy. Thus, to avoid the crisis; a full attention was given to bank performance (Chopra, 2015).

It through their research were able to find interconnection between bank-specific factors and macroeconomic indicators in the Latvian commercial banks for period 2006–2011. The authors conducted a survey of scientific literature and analyzed the profitability indicators of commercial banks using descriptive statistics, data correlation and regression analysis. On the basis of the results obtained, the authors have concluded that profitability has had a positive effect on operational efficiency, portfolio composition and management, while it has had a negative effect on the capital and credit risks (Saunders and Cornet, 2010).

The financial performance of the bank is affected by the function of internal and external factors. Internal factors refer to the indicators derived from the financial statements of banks (balance sheet and income statement) and therefore can be regarded as specific factor of banks' profitability. External factors are variables that are not related to the management of the bank, but they reflect the economic and regulatory environment that affect indirectly in the operation and profitability of the banks. Internal factors such as bank efficiency, credit risk, Non-performing loan that are affect the bank profitability. But actually what are the factors that really affect the bank's profitability in case of Nepal is the subject matter of study (Richard, 2015).

It depicted that there is a 22% increase in people who used to use banks for savings, deposits, investments and loans but they do not now use banks which may be a lost contribution to banks. The survey identified the obstacles to access finance as; the perception that loans are irrelevant, hard to get or too difficult to repay, lack of enough money to save and lack of knowledge on banking services and products. This study evaluates the determinants of profitability for Tanzanian banks using the bank-specific factors and macro-economic factors (Baxeley, 2007).

Profitability in commercial banks is determined by the ability of the banks to retain capital, absorb loan losses, support future growth of assets and provide return to investors. The largest source of income to these banks is the interest income which is earned through lending activities less interest paid on deposits and debt. Bank of has set some standard measures of profitability such as: Return on equity (ROE) which directly reflects corporate competitiveness strength and sustainable growth. It is an important indicator to show the attractiveness of the equity to the investors. The other one is Return on Assets (ROA), which effectively reflects corporate profitability and it, can be used to evaluate the performance of management in the utilization of the assets.

1. What are the indicators of profit in commercial bank of Nepal?
2. How do determinants of profit play role to increase performance in Nepalese commercial banks?
3. How do non-performing loan affect the profitability of Nepalese commercial banks?
4. What are the relationship between bank efficiency and profitability in Nepalese commercial banks?

1.3 Purpose of study

The main objective of this study is to identify the major determinants of profitability performance in Nepalese commercial banks. The specific purpose of the study is:

1. To examine the incidents of profit in commercial banks of Nepal.
2. To assess the determinants of profit play role to increase performance of Nepalese commercial banks.
3. To analyze the non-performing loan affect the probability of commercial banks.
4. To analyze the relationship between bank efficiency and profitability in Nepalese commercial banks.

1.4 Hypothesis

H1: There is significant impact between credit risk and bank profitability.

H2: There is significant impact between non-performing loan and banks profitability.

H3: There is significant impact between bank efficiency and profitability of banks.

1.5 Significance of the study

This study which deals with the determinants of profitability performance of commercial banks in Nepal is beneficial for different stakeholders such as for the academic researcher, Government, investor, customer, Banks managers and executives and for other researchers.

For the researcher, the finding of this study initiate for further research. Moreover, this study initiate the commercial banks managers and executives to give due emphasis on the management of identified variables and provides them with understanding of activities that enhance their banks profitability performance.

The policymaker like government, Ministry of Finance (MOF), Nepal RastraBank (NRB), the finding of this study is also provide insights and more reliable guide to monitoring the impact of bank specific and macroeconomic variables on profitability performance of Nepalese commercial banks.

This study will help businesses understand which economic and financial factors are critical to track and analyze in order to attain operational success. Recognizing the drivers of ROA and ROE will help new investors analyze financial statements and make informed equity investment decisions. The findings will also be of importance to literature, as it will add on to the existing literature on profitability and financial performance of banking industry.

Finally, the finding of the study is used as a reference by other researchers; thus, it can minimize the literature gap in the area of the study especially in Nepal.

1.6 Limitations of the study

This study is include internal and external factors for identifying what the factors indeed affects to profitability performance of commercial banks, still it has its own restrictions which are as follows:

1. A total of twenty seven commercial banks operate presently in Nepal, only six commercial banks are taken as the sample. So finding of the study can not be generalized.
2. There are many variables that affect the profitability performance of the bank but this study cover only two variables such as Bank efficiency, Credit risk and Non-performing loan.
3. There are many variables that used to measure the performance of bank but this study covers ROA (Return on Asset) and ROE (Return on equity).
4. This study is based on secondary data; reliability of the result is based on the reliability of data available from the annual report.
5. The study only uses the quantitative technique approach and focuses on the description of the outputs from SPSS, so other qualitative aspects regarding determinants of profitability performance are not considered.

1.7 Organization of the study

This report of the study entitled “Determinants of profitability performance of commercial banks in Nepal” is organized into five chapters. They are Introduction, Literature Review, Methodology, Results and conclusions.

Chapter 1: Introduction

This chapter includes overview of the entire work of thesis. It includes background of the study, statement of the problem, research question, research hypotheses, purpose of the study, Significance of the study and limitation of the study. It explains the determinants of profitability of commercial banks in Nepal.

Chapter 2: Literature review

This chapter includes reviews of relevant and pertinent research conduct till date by other researches and makes an attempt to relate this research with them. It presents summary and finding of previous researches carried out by other researches. Furthermore, it presents the research gap in the field of study.

Chapter 3: Methodology

This chapter explains in detail the method and procedures applied in conducting research: sampling, data collection, data analysis, tools and techniques used.

Chapter 4: Results

This chapter consists of systematic presentation and analysis of financial statement employing financial and statistical tools. It also includes the major findings.

Chapter 5: Conclusions

This chapter presents the summary of the findings obtained from data analysis in the previous chapter. The findings are interpreted and given meaning to derive solid conclusions and implication of the study. It also provides recommendations to the stakeholder of the research subject.

CHAPTER-II

REVIEW OF LITERATURE

In this chapter the overall concept and view of 'financial Performance' will be streamlined by making comprehensive review of relevant literature related to this study which would enable us to know the comparative strength and weakness of the chosen banks and the opportunities /threats they possess in the dynamic environment. The review of literature is arranged in the following order:

2.1 Theoretical review

Financial analysis is the process of determining the significant operating and financial characteristics of a firm from accounting data and the financial statement. The goal of such analysis is to determine the efficiency and the performance of the firm management, as reflected in the financial reports and records. The analysis is attempting to measure the firm liquidity, profitability and other indicators that describes the business is conducted in a rational and orderly way or not. The theoretical review contributes to a better understanding of the concept and the meaning of major profitability performance determinants in Nepalese commercial banks and its impact on profitability performance of commercial banks. Concept and the meaning about these factors from different sources are linked together to formulate a meaningful and magnificent material in this section.

2.1.1 Determinants of profitability

Profitability is the ability of a business to earn a profit. Profit is what is left of the revenue a business generates after it pays all expenses directly related to the generation of the revenue. Profitability determines whether a business stays in business (Cheney and Mosses, 2001).

Like all business, for banks profit is earning money than what they pay in expenses. The major portion of a bank's profit comes from the fees that it charges for its services

and the interest that it earns on its assets. Its major expense is interest paid on its liabilities (Chareles,2009).

The major assets of bank of a bank are its loans to individuals, businesses, and other organizations and the securities that it holds, while its major liabilities are its deposits and the money that it borrows, either from other banks or by selling commercial paper in the money market (Bhalla, 2009).

Banks increase profit by using leverage, which helped precipitate the credit crisis that occurred in 2007 to 2009. Profit can be measured as a return on assets and return on equity. Because of leverage, banks earn a much larger return on equity than they do on assets (Benerjee, 2004).

The variables which influences on profitability achievement of business are the determinants of profitability. From the related literature reviews it is known that there are bank specific variables, industrial based variables and macroeconomic variables effecting on achieving the profit goal of banks which are also known as internal and external variables (Crossee, 2006).

Internal factors are individual bank characteristics which affects the banks performance. These factors are basically influenced by internal decisions of management and the board. The external factors are sector-wide or country-wide factors which are beyond the control of the organization and affect the profitability of banks. The overall profitability performance of the banks in Nepal in the last two decade has been improving. However, this doesn't mean that all banks are profitable, there are banks declaring losses. Studies have shown that bank specific and macroeconomic factors affect the performance of commercial banks (Francis, 2008).

Internal factors/ bank specific factors

The internal determinants of banks profitability are normally consisting of factors that are within the control of commercial banks. They are the factors which affects the revenue and the cost of the banks. Some studies classified them into two categories namely the financial statement variables and non-financial variables. The financial statement variables includes factor that are directly related to the bank's balance sheet

and income statement. While, the non-financial statement variables include factors like the number of branches of a particular bank, location, size of the bank and human resource capacity etc (Ivmy, 2013).

Credit risk ratio

This ratio is calculated to find out how successfully the selected banks are utilizing their total collections or deposits on loan and advances for the purpose of earning profit. Greater ratio shows the better utilization of total deposits. This ratio can be obtained dividing loan and advances by total deposits, which can be shown as,

$$\text{Credi Risk Ratio} = \frac{\text{Total Loan and Advances}}{\text{Total Deposits}}$$

Non performing loan

This ratio indicates the ratio between the non- performing assets and total assets. Higher NPA to total assets implies ratio implies the bad effect in banks performance and it decreases the profitability of the banks and lower ratio implies the better performance of the bank and it increases the profitability of banks. This ratio can be calculated as follows:

$$\text{NPA to Total Assets} = \frac{\text{Total Non Performing Assets}}{\text{Total Assets}}$$

Bank efficiency ratio

This ratio is a measure of banks overheads as a percentage of its revenue. It is a quick and easy measure of banks ability to turn resources into revenue. The lower the ratio, is batter(50% is generally regarded as the maximum optimal ratio). An increase in the efficiency ratio indicates either increasing costs or decreasing revenues. This ratio can be computed by using following formula:

$$\text{Bank Efficiency Ratio} = \frac{E}{\text{Revenue}}$$

2.1.2 Profit measures of commercial banks

Profit is the ultimate goal of commercial banks. All the strategies designed and activities performed thereof are meant to realize this grand objective. However, this does not mean that commercial banks have no other goals. Commercial banks could

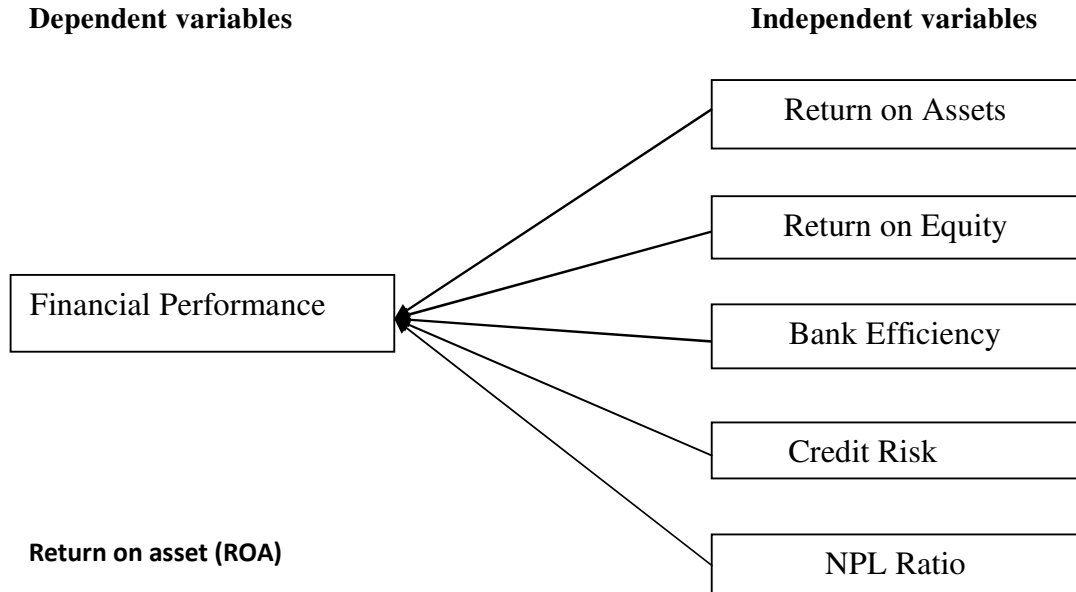
also have additional social and economic goals. However, the intention of this study is related to the first objective, profitability. To measure the profitability of commercial banks there are variety of ratios used of which Return on Asset, Return on Equity and Net Interest Margin are the major ones (Bedi and Mardikar, 2013).

In most of the study, the profitability is measured in the form of ratios which are normally reported y commercial banks annual reports. It claims that the use profitability ratios are not influence by changes in price levels. And it is said to e most appropriate way of measuring profitability as one make use of time series analysis. This is because the real value of profits can not be affected by the varying inflation rates. According to Rasiah (2010) for one to realize how well a bank is performing it is much more useful to consider return on assets (ROA) and return on equity (ROE) (Mishkin, 2017).

Profitability can be measured in terms of assets, income or equity. In the literature, more reliance has been placed on the Return on assets (ROA) to measure bank profitability. Yet, other possible measures to reflect profitability of banks are return on equity (ROE), profit margin, interest rate margin and bank stock prices. Specific indicators of the banks, such as return on assets (ROA) and return on equity (ROE), demonstrate how successfully the banks maintain their profitability. For instance, Fitch (2012) stressed that exactly ROA is one of the main indicators determining profitability of a bank. The measures of banks profitability performance are explained briefly as follows.

Conceptual framework

This portion of the thesis displays the impact among the variables presented in the framework are selected after studying and having depth knowledge on the determinants of profitability of commercial banks through various related literature reviews. The study have been though mostly had used bank specific and profitability variable for study purpose. The most common variable among those study were capital adequacy, non-performing loan and operational efficiency. The conceptual framework diagram for this study is represented in the following figure.



Return on asset (ROA)

The ROA reflects the ability of a bank’s management to generate profits from the bank’s assets. It shows the profits earned per birr of assets and indicates how effectively the bank’s assets are managed to generate revenues, although it might be biased due to off-balance sheet activities. This is probably the most important single ratio in comparing the efficiency and operating performance of banks as it indicates the returns generated from the assets that bank owns (Tan et al. 2012). It measures the ability of the bank management to generate income by utilizing company assets at their disposal. In other words, it shows how efficiently the resources of the company are used to generate the income. It further indicates the efficiency of the management of a company in generating net income from all the resources of the institution (Khrawish, 2011). Wen (2010), state that a higher ROA shows that the company is more efficient in using its resources.

Return on assets (ROA) is the ratio of Net Income after Taxes divided by Total Assets. The ROA signifies managerial efficiency in other words it depicts how effective and efficient the management of banks has been as they seek to transform assets into earnings. And the higher ratio indicates the higher performance of the banks. It is a useful tool for comparing profitability of one bank with other or the whole commercial banking system (Khan and Jain, 2015).

Return on equity (ROE)

Return on equity is the return to shareholders on their equity. This means that, return on equity reflects the capability of a bank in utilizing its equity to generate profits (Tan et al. 2012). According to Dietrich et al. (2009), banks with a lower leverage ratio (higher equity) report a higher ROA, but a lower ROE. However, the ROE disregards the higher risk that is associated with a higher leverage. Even if ROE is commonly used in different studies, it is not the best measure of profitability. ROE is a financial ratio that refers to how much profit a company earned compared to the total amount of shareholder equity invested or found on the balance sheet. ROE is what the shareholders look in return for their investment. A business that has a high return on equity is more likely to be one that is capable of generating cash internally. Thus, the higher the ROE the better the company is in terms of profit generation. It is further explained by Khrawish (2011) that ROE is the ratio of Net Income after Taxes divided by Total Equity Capital. It represents the rate of return earned on the funds invested in the bank by its stockholders. ROE reflects how effectively a bank management is using shareholder's funds. Thus, it can be deduced from the above statement that the better the ROE the more effective the management in utilizing the shareholders capital.

The ROE is said to measure the rate of return on the bank's shareholders equity and it is calculated by dividing banks net income after tax by total equity capital which includes common and preferred stock, surplus, undivided profits, and capital reserve (Khubchandani, 2017).

Bank efficiency

Banks' technical efficiency is defined as the difference between observed. Quantity of input and output variables with respect to optimal quantity of input and output variables. An efficient bank can achieve a maximum value of one in comparison to an inefficient bank, which can reduce to the level of zero.

These measures of profitability gives an indication of what the banks earns on the shareholder's investment. According to it many researcher have presented ROA as an appropriate measure of bank profitability. Among them who argued that bank

profitability is best measured by ROA in the sense that, ROA cannot be distorted by high equity multiplier? However, it also claims that ROA tend to be lower for financial intermediaries, most banks heavily utilized financial leverage to increase their ROE to competitive levels.

Credit risk

Credit risk is the possibility of a loss resulting from a borrower's failure to repay a loan or meet contractual obligations. Traditionally, it refers to the risk that a lender may not receive the owed principal and interest, which results in an interruption of cash flows and increased costs for collection. Excess cash flows may be written to provide additional cover for credit risk. Although it's impossible to know exactly who will default on obligations, properly assessing and managing credit risk can lessen the severity of a loss. Interest payments from the borrower or issuer of a debt obligation are a lender's or investor's reward for assuming credit risk (Pandey, 2011).

NPL ratio

When a borrower has not made regular payments for at least 90 days, the loan is considered a nonperforming loan, or NPL. The nonperforming loan ratio, better known as the NPL ratio, is the ratio of the amount of nonperforming loans in a bank's loan portfolio to the total amount of outstanding loans the bank holds (Thapa, 2017)..

2.2 Review of previous studies

Rayamajhi (2015) entitled with “Liquidity Management of Commercial Banks in Nepal with reference to Bank of Kathmandu (BOK), Nepal Industrial and Commercial Bank (NIC), HBL and NABIL”,

Objectives:

- Examining & analyzing the liquidity position and its management in Nepalese commercial banks.
- The efficient deposit utilization in investment of NABIL is good, BOK is poor and NIC and HBL are moderate and so on.

Major Findings:

- The liquidity position of NIC is strong, HBL is poor and BOK, and NABIL are moderate in terms of cash and bank balance to current deposit ratio,

- The liquidity position of NIC and BOK are proportionately better than NABIL and HBL in terms of short-term investment to total investment ratio,
- Mr. Paudel recommended that all the commercial banks should maintain the strong liquidity position.
- For liquidity commercial bank should focus on short term deposit as well as current deposit.

Kafle (2016) entitle with "Liquidity Position of Commercial Banks of Nepal With reference to BOK, HBL, Standard Chartered Bank (SCB), Nepal Bank Limited (NBL), NIB and HBL"

Objectives:

- Examining the relationship between liquidity and profitability.
- Saving and fixed deposits are in higher proportion as the major sources of funds for each bank,

Major Findings:

- The banks under study are maintaining very high level of liquidity than the rate imposed by the NRB,
- There is positive correlation between change in deposit and change in total liquid fund of the banks and so on.
- That performance of stated banks are quite satisfactory and they should find new investment sector for long lasting profitability

Adhikari (2017) entitle with "Liquidity and Profitability Position of Commercial Banks of Nepal" which included SCBL, NABIL, HBL, HBL; NIBL.

Objectives:

- Main objective of the research is to examine the liquidity and profitability position of the commercial banks of Nepal.
- The average net profit made by SCBL is highest. In terms of net profit margin SCBL is most efficient.

Major Findings:

- The liquid asset of SCBL is highest among the above mentioned banks.

- In terms of cash reserve ratio liquidity position of NIBL is most satisfactory.

Recommendations:

- According to the thesis it would be better if HBL increases the liquid assets considering the short-term liabilities requirement.
- NABIL and HBL should be careful enough while maintaining CRR and thus should not jeopardize the credibility of the bank.
- Lastly she suggests that banks should reengineer the portfolio of its investment to achieve higher higher profit.

Shrestha (2018) entitle with “Liquidity Management of Commercial Banks in Nepal with reference to Bank of Kathmandu (BOK), Nepal Industrial and Commercial Bank (NIC), HBL and NABIL”,

Objectives:

- Examining & analyzing the liquidity position and its management in Nepalese commercial banks.
- The efficient deposit utilization in investment of NABIL is good, BOK is poor and NIC and HBL are moderate and so on.

Major Findings:

- The liquidity position of NIC is strong, HBL is poor and BOK, HBL and NABIL are moderate in terms of cash and bank balance to current deposit ratio,
- The liquidity position of HBL, NIC and BOK are proportionately better than NABIL and HBL in terms of short-term investment to total investment ratio,
- Mr. Paudel recommended that all the commercial banks should maintain the strong liquidity position.
- For liquidity commercial bank should focus on short term deposit as well as current deposit.

Parajuli (2019) entitle with “Liquidity and Profitability Position of Commercial Banks of Nepal” which included SCBL, NABIL, HBL and NIBL.

Objectives:

- Main objective of the research is to examine the liquidity and profitability position of the commercial banks of Nepal.
- The average net profit made by SCBL is highest. In terms of net profit margin SCBL is most efficient.

Major Findings:

- The liquid asset of SCBL is highest among the above mentioned banks.
- In terms of cash reserve ratio liquidity position of NIBL is most satisfactory.

Recommendations:

- According to the thesis it would be better if HBL increases the liquid assets considering the short-term liabilities requirement.
- NABIL and HBL should be careful enough while maintaining CRR and thus should not jeopardize the credibility of the bank.
- Lastly she suggests that banks should reengineer the portfolio of its investment to achieve higher higher profit.

2.3 Research gap

In the researches done so far it is known which bank is better performing than which one. Also the comparative study of the liquidity position has been done. The study done so far studies about either the commercial banks but this study does the comparative study of as many as commercial banks possible. In studies done earlier either liquidity position or the profitability position and financial performance analysis of studied, but this study compares the investment policy of several banks in Nepal. In researches done so far, most of them focus on the limited number of banks or limited number of variables that measures liquidity or profitability. But this study has gathered as many as banks possible. Also, this study has gathered as many as variables and ratios to study and measure liquidity and profitability of the banks under study. This research is an original one should be the foundation for the future researchers to know about the pattern of sample banks.

Therefore, this research is broader and is aimed to analyze the impact of profitability and liquidity by analyzing their trends and using hypothesis to draw the effective conclusion.

- Nevertheless, the analysis performed and conclusion drawn regarding the Liquidity Position of Nepalese Commercial Banks; there is considerable place for arguing on its accuracy and reliability.
- In reviewing previous researches, I have found that they have not discussed much about the financial sectors decentralization towards the rural areas, where there is real need in those areas financial activities should be undertaken which I had referred here in my study.
- By undertaking the policy of decentralization of financial sectors, then there will be much more healthy competition between existing financial institutions than in the present situation.

CHAPTER III

METHODOLOGY

This chapter deals with research methodology of the study. To solve the research problem and fulfill the objectives of the study, detail discuss about research design, population and sample, sources of data & data analysis tools has been made. To accomplish the goal, the study follows the research methodology described in this chapter.

3.1 Research design

The descriptive and analytical research designs has been used for achieve the objectives. The descriptive research design has been adapted to undertake fact finding operation searching for adequate information in the context of determinants of lending behavior of commercial bank in Nepal. This study has also used correlation research design to establish the directions, magnitudes and forms of the observed relationship between different dependent and independent variables (Adhikari, 2016).

3.2 Population and sample

There are 27 commercial banks in Nepal. Among them six commercial banks have taken sample for judgmental sampling. The convenience sampling method was used in choosing the banks for the study. Moreover, in selecting the 6 banks out of 27 commercial bank for the study, due care is given to include banks such as: joint venture, domestic, best performer, average performer and comparatively week performer in the sample. The banks selected for the study are six sample banks. This study assumes that the study population has been fairly represented by the selected sample.

3.3 Data collection procedure

As explained in previous chapters, the main sources of secondary data are the reports of the Banks published in their respective annual general meetings and web site of the relevant banks. In addition to that some of the relevant data are also collected from the

non- bank financial statistics published by the non- bank regulation department of Nepal Rastra Bank.

3.4 Sources of data

After defining the research design, how the work comes to define the sources of relevant data for the research study. Generally, Secondary data are sources of this study. On the other hand secondary data are those data that are collected by someone else or used already & made available to other in the form of published statistics such as annual reports, periodicals, newspapers, magazines etc. once a primary data is used; it loses its originality & becomes secondary. This study is mainly depends on the use of secondary data that consists of annual reports of the concerned bank. However besides the annual reports various other sources of data have also been used for the purpose of the study plan documents, newspaper, magazine, economic journals, NRB reports etc.

3.5 Methods of analysis

To achieve the objectives of the study, various financial, statistical and accounting tools have been used in this study. The analysis of data will be done according to pattern of data available. With the available tools and resources, analytical statistical tools such as Karl Person's coefficient of correlation and simple regression are adopted in this study. The various calculated results obtained through financial, accounting and statistic tools are tabulated under different heading. Then they are compared with each other to interpret the results.

3.5.1 Financial tools

There are various financial tools to measure the performance of an organization. The following financial tools have been used for the analysis:

a) Ratio analysis

The relationship between two accounting figures expressed mathematically is known as a financial ratio. Ratio analysis is used to compare a firm's financial performance and status to that of other firms or to itself over time. From the help of ratio analysis,

qualitative judgment can be done regarding financial performance of the firm. In this study, following ratios are calculated and analyzed.

i) Net Profit to total deposit ratio

This ratio measures percentage of profit with the bank to make immediate payment to the depositors. This ratio is computed by dividing cash and bank balance by total deposit. This can be presented as follows:

$$\text{Net Profit to Deposit Ratio} = \frac{\text{Net Profit}}{\text{Total Deposits}}$$

ii) Return on loan and advances ratio

Return on loan and advances ratio shows how efficiently the banks have utilized their resources to earn good return from provided loan and advances. This ratio is computed dividing net profit (loss) by the total amount of loan and advances and can be mentioned as,

$$\text{Return on Loan and Advances Ratio} = \frac{\text{Net Profit (Loss)}}{\text{Loan and Advances}}$$

iii) Net profit to total investment

Net profit to total investment ratio calculates the profitability of banks in comparison to the investment of the organizations. It is calculated by dividing net profit by investments.

$$\text{Net Profit to Total Investment} = \frac{\text{Net profit}}{\text{Total Deposits}}$$

iv) Return on total assets (ROA)

Return on total assets or simply return on assets, measures the productivity of the assets. It is measured in terms of relationship between net profit and assets. "This ratio judges the effectiveness in using the total fund supplied by the owners and creditors. Higher ratio shows the higher return on the assets used in the business thereby, indicating effective use of the resources available and vice-versa. ROA is calculated as under;

$$\text{Return on assets (ROA)} = \frac{\text{Net income}}{\text{Total assets}}$$

v) Return on Equity Ratio (ROE)

Since, shareholders are entitled to the residual profits; ROE shows the relationship between net income and shareholders' fund. This ratio indicates the firm's ability of generating net income per rupee of shareholders' fund. The main objective of computing this ratio is to analyze how effectively the funds supplied by shareholders' have been utilized. This ratio is of great interest to the present as well as the future prospective shareholders and also of great concern to management which has the responsibility of maximizing the owners' welfare. This ratio can be computed by

using following formula:

$$\text{ROE} = \frac{\text{Net income}}{\text{Shareholder's equity}} \times 100\%$$

vi) Credit risk ratio

This ratio is calculated to find out how successfully the selected banks are utilizing their total collections or deposits on loan and advances for the purpose of earning profit. Greater ratio shows the better utilization of total deposits. This ratio can be obtained dividing loan and advances by total deposits, which can be shown as,

$$\text{Credi Risk Ratio} = \frac{\text{Total Loan and Advances}}{\text{Total Deposits}}$$

viii) Non performing loan

This ratio indicates the ratio between the non-performing assets and total assets. Higher NPA to total assets implies ratio implies the bad effect in banks performance and it decreases the profitability of the banks and lower ratio implies the better performance of the bank and it increases the profitability of banks. This ratio can be calculated as follows:

$$\text{NPA to Total Assets} = \frac{\text{Total Non Performing Assets}}{\text{Total Assets}}$$

ix) Bank efficiency ratio

This ratio is a measure of banks overheads as a percentage of its revenue. It is a quick and easy measure of banks ability to turn resources into revenue. The lower the ratio, is batter(50% is generally regarded as the maximum optimal ratio). An increase in the efficiency ratio indicates either increasing costs or decreasing revenues. This ratio can be computed by using following formula:

$$\text{Bank Efficiency Ratio} = \frac{E}{\text{Revenue}}$$

(Without including interest expenses)

3.5.2 Statistical tools

Various statistical tools related to this study are drawn out to make the conclusion more reliable according to the available financial data. For this following statistical tools are used;

a) Arithmetic mean

The average value is a single value within the range of the data that is used to present all of the values in the series. Since an average is somewhere within the range of the data, it is called a measure of central value. Arithmetic mean is more popular to denote particular type of average. It is obtained by dividing sum of obtain observations by the number of item which is present as follows:

$$\bar{X} = \frac{\sum x}{n}$$

Where,

\bar{X} = Arithmetic Mean

$\sum x$ = Summation for total observation

n = Number of items

b) Standard deviation

Standard deviation is the most important and widely used measure of studying dispersion. It is also known as root mean square deviation. It is also denoted by the small Greek Letter σ (sigma). The standard deviation measures the absolute dispersion of a distribution. Hence, standard deviation is extremely useful in judging the representative of the mean. Symbolically,

$$\sigma = \frac{\sqrt{\sum d^2}}{n}$$

Where,

σ = Standard deviation

$\sum d^2$ = sum of squares of the deviation measured from arithmetic average

n = Number of items

c) Coefficient of variation

The coefficient of variation is the corresponding relative measures of dispersion, comparable across distribution, which is defined as the ratio of the standard deviation to the mean expressed in resulting percentage. It is used in problems where we want to compare the variability of two or more than two series. The series for which the coefficient of variation is greater is said to be more variable or conversely less consistent, less uniform, less stable or less homogeneous and vice-versa.

We can denote this by following formula,

$$CV = \frac{\sigma}{x} * 100$$

Where,

CV = Coefficient of variation

σ = Standard Deviation

x = Mean / Average

d) Correlation analysis

Correlations the statistical tool that we can use to describe the degree to which one variable is linearly related to another. The coefficient of correlation measures the degree of relationship between two sets of figures. Among the various methods of finding out coefficient of correlation, Karl Pearson's method is applied in the study. The result of coefficient of correlation is always between +1 and -1. When r = +1, it means there is perfect relationship between two variables and vice-versa. When r = 0, it means there is no relationship between two variables. The Pearson's formula is:

$$r = \frac{n\sum xy - \sum x \cdot \sum y}{\sqrt{n\sum x^2 - (\sum x)^2} \cdot \sqrt{n\sum y^2 - (\sum y)^2}}$$

Where,

r = coefficient of correlation

x = independent variable

y = dependent variable

n = no. of periods

e) Probable error of the co-efficient of correlation

After the calculation of Co-efficient of correlation the next thing is to find out the extent to which it is dependable. For this purpose the probable error of the coefficient of correlation is calculated. If the probable error is added to and subtracted from the co-efficient of correlation it would be giving two such limits within which we can reasonably expect the value of co-efficient of correlation to vary.

The formula for finding out the probable error of the Karl Pearson's co-efficient of correlation is:

$$P. E.(r) = 0.6745 * \frac{1-r^2}{\sqrt{n}}$$

Where,

P. E. (r) = Probable error of co-efficient of correlation

r = co-efficient of correlation

n = Number of pairs of observations

In order to conclude whether the co-efficient of correlation is significant or not. The following points should be kept in mind

- If the co-efficient of correlations is less than its probable error, it is not at all significant.
- If the co-efficient of correlations is more than six times of probable error, it is definitely significant.
- If the probable error is not much and the co-efficient of correlation is 0.5 or more it is generally to be significant.

f) Coefficient of determination

The Co-efficient of determination is the measure of degree of linear association or correlation between two variables, one of which happens to be independent and the other being dependent variable. In other words, co-efficient of determination measures the percentage of total variation in dependent variable explained by independent variable. The co-efficient of determination can have a value ranging from zero to one. A value of one can occur only if the unexplained variation is zero which simply means that all the data points in the scatter diagram fall exactly on the regression line. Co-efficient of determination is the square of the Co-efficient of correlation.

Symbolically,

$$R^2 = (r)^2$$

Where,

R² = Co-efficient of Determination

r = Co-efficient of correlation

g) Regression analysis

Regression is the statistical tool which is used to determine the statistical relationship between two or more variables and to make estimation or prediction of one variable on the basis of the other variables. In other words, regression is that statistical tool with the help of which the unknown value of one variable can be estimated or predicted on the basis of known value of the other variable. Assuming that the two variables are closely related we can estimate the value of the one variable from the given value of another. For example, if we know that production and sales are closely related, we can find out the quantity of production required to achieve a given amount of sales. Thus regression determines the average probable change in one variable based on a certain amount of change in another. In symbolically, it is defined as:

- $\sum e^2 = \sum (Y - \hat{Y})^2$
- This is called the least square if
- $\sum e^2 = \sum (Y - \hat{Y})^2 = 0$ which best fits all the data.
- taking the first derivative of this expression with respect to "a" and "b" gives two equations which are called the normal equations.
- i.e. = $\frac{\partial \sum (Y - \hat{Y})^2}{\partial a} = \text{minimum}$ and $\frac{\partial \sum (Y - \hat{Y})^2}{\partial b} = 0$
- gives,
- $\sum Y = na + b\sum X$ $\sum XY = a\sum X + b\sum X^2$

The regression model is used in the analysis. The economic model for this study is given as:

$$Y = b_0 + bX_{it} + E_{it}$$

Where,

Y is dependent variable, b_0 is the constant, b_{it} the coefficient of explanatory variables, X_{it} is the explanatory variable and E_{it} is error term.

By using the prescribed economic model, the impact of these internal indicators and external economic factors on performance of commercial banks will be estimated with the following regression equation.

$$ROA_{it} = b_0 + b_1 \text{Bank Efficiency}_{it} + b_2 \text{NPLR}_{it} + b_3 \text{Credit Risk}_{it} + e_{it}$$

$$ROE_{it} = b_0 + b_1 \text{Bank Efficiency}_{it} + b_2 \text{NPLR}_{it} + b_3 \text{Credit Risk}_{it} + e_{it}$$

Subscript I refers to firm I, subscript t refers to time/ year

Where,

ROA = Return on assets

ROE = Return on equity

CR_{it} = Credit Risk Ratio of i^{th} bank in year t

$NPLR_{it}$ = Non-performing loan ratio of i^{th} bank in year t

Bank Efficiency $_{it}$ = Bank Efficiency ratio of i^{th} bank in year t

b_0 = The intercept

b_1, b_2, b_3, b = the slope which represent the degree with which bank performance

CHAPTER IV

RESULTS

4.1 Profitability position of selected banks

The relationship between two accounting figure expressed mathematically, is known as a financial ratio or simply a ratio. An accounting figure conveys meaning when it is related to some relevant information. Here profitability ratios are calculated and evaluated in terms of the relationship between net profit and assets.

4.1.1 Return on assets

The following table shows the percentage of net profit to total assets of sample banks:

Table 4.1

Return on Assets

Banks	EBL	HBL	BOKL	NIBL	NSBI	NCCB
2013/14	2.25	1.3	1.12	2.3	1.19	0.49
2014/15	1.85	1.34	1.26	1.9	1.51	1.12
2015/16	1.61	1.94	1.51	2	1.8	1.26
2016/17	1.72	2.19	1.89	2.1	1.7	1.51
2017/18	1.97	1.67	1.47	2.1	1.53	1.89
Mean	1.867	1.653	1.427	2.076	1.531	1.146
S.D	0.221	0.343	0.262	0.133	0.208	0.463
CV	11.839	20.730	18.342	6.391	13.592	40.412

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

Table 4.1 shows that average ROA of sample banks are 1.867, 1.653, 1.427, 2.076, 1.531 and 1.146 respectively and lowest coefficient variation of NIBL is 6.391 which mean NIBL is more consistent than other sample banks. In this way average ROA of NIBL is 2.076 higher than other banks.

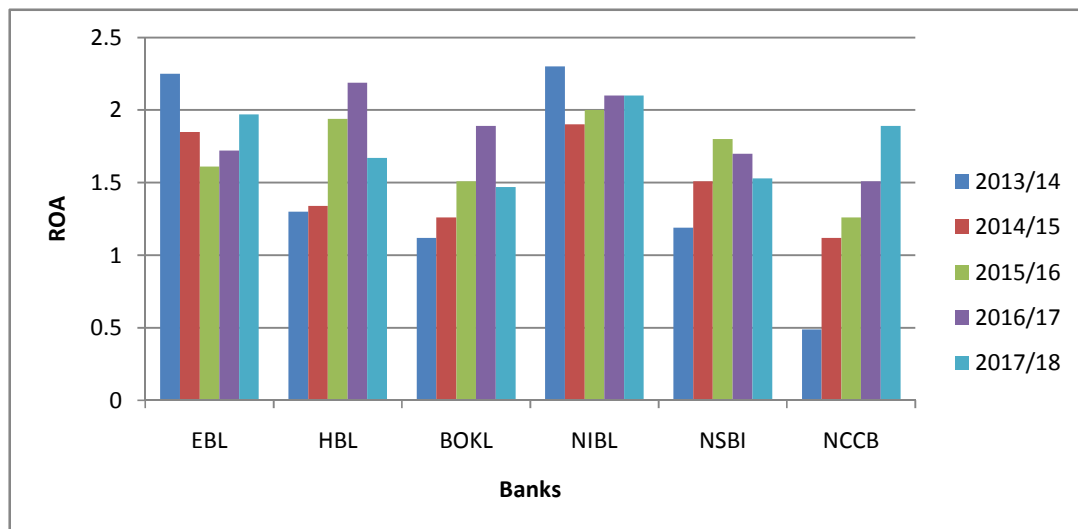


Figure 4.1: Return on Assets

Figure 4.1 shows that average ROA of Nepal SBI Bank Limited is 1.19 ratio which is the higher and lower is 0.49 of NCCB in 2012/13. Total average of NIBL is higher than other and lower is NCCB. In this way standard deviation of NCCB is higher than others. In overall NIBL bank is better performance and NCCB is slightly weak than among sample banks.

4.1.2 Return on equity

This ratio can be obtained dividing net profit by no of shareholder equity. Ratios and statistical calculations are given as under:

$$\text{Net profit to Total Deposit} = \frac{\text{Net profit}}{\text{Total Deposit}}$$

Total No of Shares

Table 4.2

Return on Equity

Banks	EBL	HBL	BOKL	NIBL	NSBI	NCCB
2013/14	26.63	26.15	13.66	27.8	20.31	5.3
2014/15	27.2	23.08	16.65	28.1	22.85	14.05
2015/16	28.88	42.89	21.96	31	21.51	16.15
2016/17	25.82	40.93	21.96	28.1	22.16	18.12
2017/18	22.77	26.15	14.81	46.1	20.41	19.28
Mean	26.180	30.797	17.464	31.572	21.425	13.325
S.D	2.013	8.321	3.522	7.037	0.985	4.970
CV	7.689	27.019	20.166	22.290	4.596	37.295

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

Table 4.2 shows that average return on equity of EBL, HBL, BOKL, NIBL, NSBI & NCCB is 26.180, 30.797, 17.464, 31.572, 21.425 and 13.325 respectively and average ROE of NIBL is higher than other which value is 31.572. CV of NSBI is lower than other selected banks which mean NSBI is more consistency than other banks.

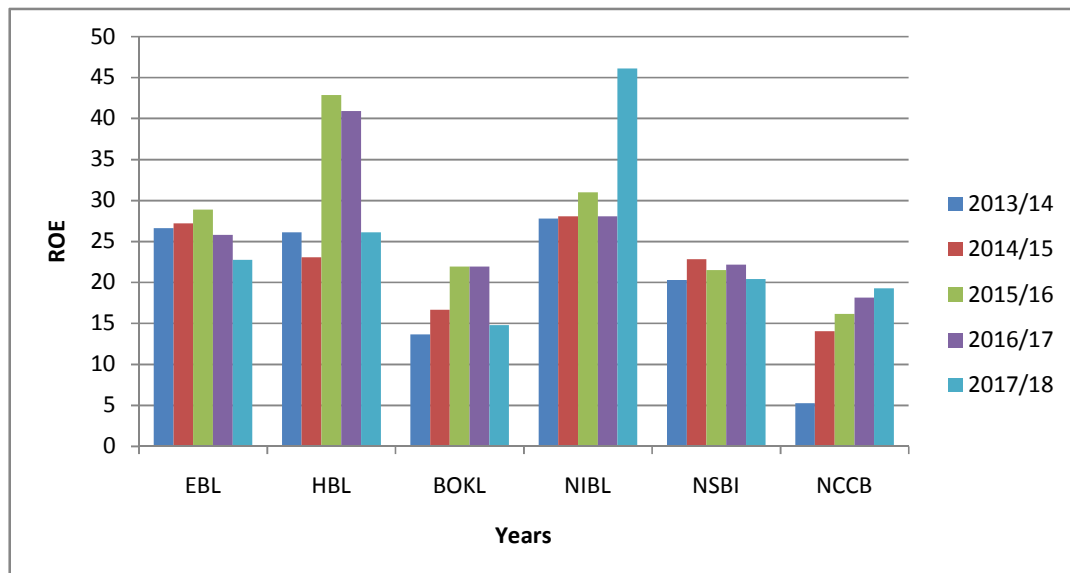


Figure 4.2: Return on Equity

Figure 4.2 shows that average mean of NIBL is higher than other selected banks. CV of NSBI is lower than other selected banks which mean NSBI is more consistency than other banks.

4.1.3 Net profit to total deposits ratio

This ratio can be obtained dividing net profit by total deposits. Ratios and statistical calculations are given as under:

$$\text{Net profit to Total Deposit} = \frac{\text{Net profit}}{\text{Total Deposits}}$$

Table 4.3

Comparative Net Profit to Total Deposit Ratios

Years	SBI	EBL	HBL	NCCB	NIBL	BOKL
2013/14	0.0129	0.0255	0.0318	0.0489	0.0013	0.0012
2014/15	0.0168	0.025	0.0341	0.0503	0.0087	0.0088
2015/16	0.0189	0.0189	0.0292	0.0198	0.0065	0.0025
2016/17	0.0204	0.0185	0.0266	0.0242	0.026	0.0045
2017/18	0.0184	0.0241	0.0309	0.0316	0.042	0.0054
Mean	0.017	0.022	0.030	0.033	0.010	0.004
S.D	0.003	0.003	0.003	0.013	0.015	0.003
CV	14.835	13.780	8.280	38.385	157.195	71.781

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

Table 4.2 shows that net profit to total deposit ratio of SBI, EBL, HBL, NCCB and NIBL are in fluctuating trend during the seven years study period. EBL has not invested its total working fund in shares and debentures in the year 2011/12. SBI, EBL, HBL, NCCB and HBL have the CV of 8.28% which is lowest than other sample banks and NIBL has highest CV during the study period. This means HBL is more consistent bank than other banks.

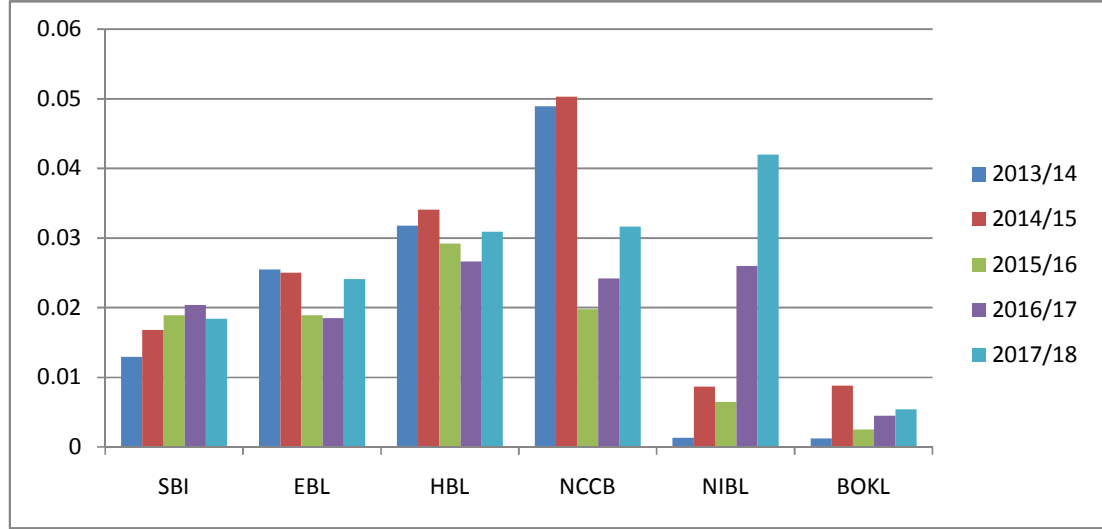


Figure 4.3: Comparative Net Profit to Total Deposit Ratios

Table 4.3 and Figure 4.3 show that The Coefficient of variation shows more stable ratio of HBL than SBI, EBL, NCCB and NIBL and NIBL has 9.03 and 36.75 Net Profit to Total Deposit Ratios respectively. The ratio of comparative investment on shares and debentures to total working fund ratios of Nepal SBI Bank Limited is 0.0174, 0.0095, 0.0129, 0.0168, 0.0189, 0.0204 and 0.0184 respectively between fiscal year 2011/12 and 2017/18. Similarly the ratio of comparative investment on shares and debentures to total working fund ratios of HBL Bank Limited is 0.0214, 0.3100, 0.0318, 0.0341, 0.2292, 0.0266 and 0.0309 respectively from fiscal year 2011/12 to 2017/18. Likewise, the ratio of comparative investment on shares and debentures to total working fund ratios of the Everest Bank Limited is 0.02703, 0.0218, 0.0255, 0.025, 0.0189, 0.0185 and 0.0241 respectively from fiscal year 2011/12 to 2017/18. In similarly NCCB and NIBL has Net Profit to Total Deposit Ratios are 0.0843, 0.0099, 0.989, 0.0503, 0.0198, 0.0242, 0.0316 and 0.0078 as well as 0.0030, 0.0013, 0.0087, 0.0065, (0.026) and (0.042) respectively.

4.1.4 Return on loan & advances ratio

This ratio is computed dividing net profit (loss) by the total amount of loan and advances and can be mentioned as,

Return on Loan & Advances = $\frac{\text{Net Profit}}{\text{Loan \& Advances}}$

Loan & Advances

Table 4.4

Comparative Return on Loan and Advances Ratios

Years	SBI	EBL	HBL	NCCB	NIBL	BOKL
2013/14	0.0265	0.0339	0.0436	0.029	0.0022	0.0587
2014/15	0.0259	0.0326	0.047	0.064	0.0154	0.097
2015/16	0.0245	0.0289	0.0364	0.0256	0.0099	0.0985
2016/17	0.0284	0.0255	0.0386	0.0029	0.0372	0.0541
2017/18	0.0238	0.0297	0.0408	0.0362	0.0554	0.0543
Mean	0.026	0.030	0.041	0.022	0.015	0.070
S.D	0.002	0.003	0.004	0.020	0.020	0.021
CV	6.244	9.835	9.057	90.061	132.709	29.648

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

Table 4.3 shows that Return on Loan and Advances Ratios of Nepal SBI bank has 0.0346, 0.0193, 0.0265, 0.0259, 0.0245, 0.0284 and 0.0238 and EBL is 0.0358, 0.0304, 0.0339, 0.0326, 0.0289, 0.0255 and 0.0297 is respectively. In this way HBL bank is 0.0279, 0.0409, 0.0436, 0.0470, 0.0364, 0.0386 and 0.0408 respectively. NCCB is 0.959, 0.136, 0.029, 0.064, 0.256, 0.029 and 0.0362 respectively. NIBL is 0.0196, 0.0061, 0.0022, 0.0154, 0.0099, (0.0372) and (0.0554) respectively.

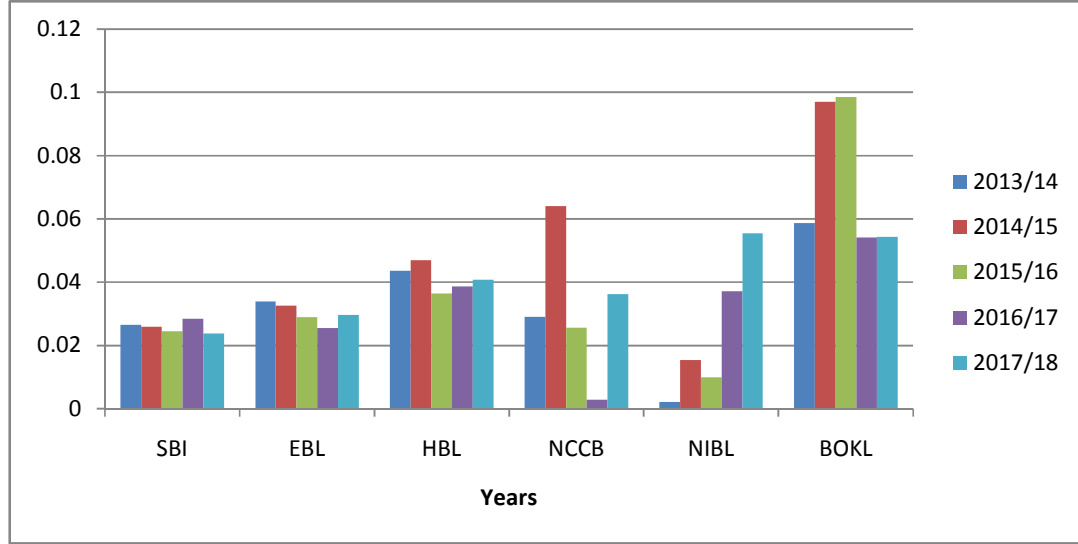


Figure 4.4: Comparative Return on Loan and Advances Ratios

Figure 4.3 shows that the return on loan and advances of SBI, EBL, HBL, NCCB and NIBL has the ratio of fluctuating trend. During the study period, HBL has the highest ratio of 5.61% than that of SBI, EBL, NCCB and NIBL i.e. 3.22% and 2.87% respectively. In average NCCB has the highest mean ratio of 9.81 % where as SBI, EBL, NCCB and NIBL has the mean ratio of 2.74% and 2.20%. Coefficient of variation indicates that EBL has no more variance between seven years study period than SBI and HBL.

4.1.5 Net profit to investment ratio

Table 4.5

Net Profit to Investment Ratio

Years	SBI	EBL	HBL	NCCB	NIBL	BOKL
2013/14	0.0295	0.1588	0.1236	0.2501	0.0073	0.0584
2014/15	0.0516	0.2382	0.1407	0.5402	0.0299	0.2567
2015/16	0.1049	0.1042	0.0769	0.1957	0.0299	0.2987
2016/17	0.069	0.9507	0.0804	0.2106	0.1776	0.3261
2017/18	0.0717	0.1916	0.112	0.3016	0.3263	0.2987
Mean	0.060	0.235	0.104	0.279	0.052	0.213
S.D	0.025	0.314	0.025	0.126	0.122	0.097
CV	41.316	133.592	23.795	45.129	235.220	45.693

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

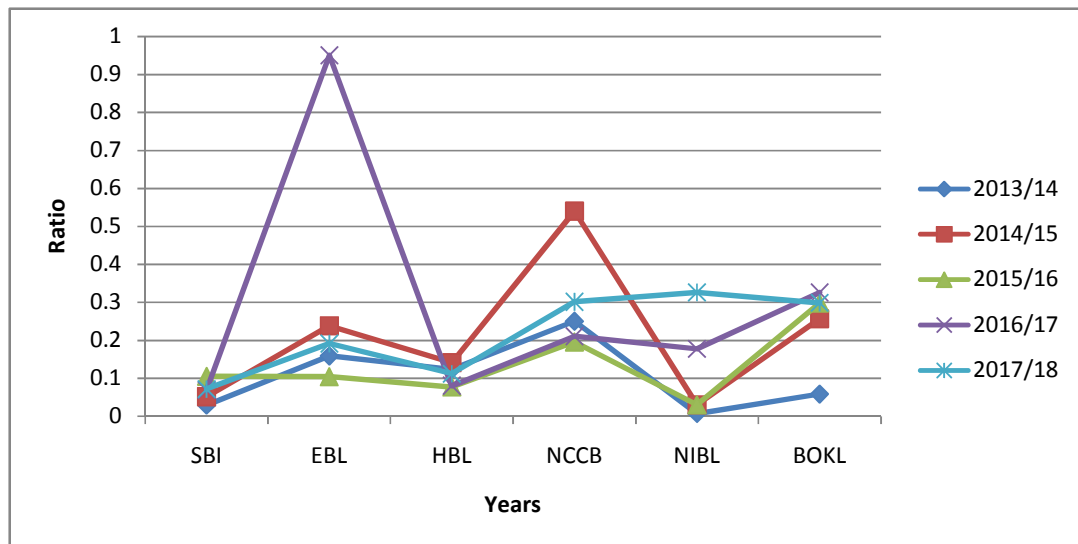


Figure 4.5: Net Profit to Investment Ratio

Table 4.5 shows that SBI has average net profit to investment ratio is 24.61 percent and Net profit to investment ratio of 38.24 of Everest Bank Limited. Similarly, the ratios of NCCB are 98.12, 124, 25.01, 54.02, 19.57, 21.06 and 30.16 from fiscal year 2011/12 to 2017/18. Similarly, the ratios of Nepal Bank Limited are 5.59, 2.01, 0.73, 2.99, (17.76) and (32.63) from fiscal year 2011/12 to 2017/18. The ratios of the Nepal SBI Bank Limited are 3.91, 2.06, 2.95, 5.16, 10.49, 6.9 and 7.17 respectively between fiscal year 2011/12 and 2017/18. Similarly, the ratios of HBL Bank Limited are 8.17, 11.37, 12.36, 14.07, 7.69, 8.04 and 11.20 respectively. The ratio of EBL is 14.35, 13.86, 15.88, 23.82, 10.42, 6.90, and 7.17 respectively from fiscal year 2011/12 to 2017/18. The mean ratio of SBI is lower than that of EBL and NIBL i.e. 24.61 % < 27.66 % < 38.24%. It means that SBI has maintained the lower net profit to investment ratio which means it operates with lower risk for higher profit.

4.1.6 Bank efficiency

Table 4.6

Bank Efficiency

Banks	EBL	HBL	BOKL	NIBL	NSBI	NCCB
2013/14	70.25	55.12	52.72	76.44	556.45	62.76
2014/15	58.92	54.72	55.35	74.78	53.65	64.35
2015/16	69.1	63.95	60.85	77.11	59.65	59.56
2016/17	66.8	41.14	66.47	70.86	54.58	64.49
2017/18	63.02	37.33	43.53	67.55	39.92	56.65
Mean	65.483	49.468	55.227	73.257	82.750	61.486
S.D	4.161	9.809	7.741	3.621	201.906	3.030
CV	6.355	19.829	14.016	4.943	243.996	4.929

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

Table 4.6 shows that Bank efficiency ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 65.618, 50.452, 55.784 and 73.348 respectively. Average Bank Efficiency, SD of NIBL is higher than other sample banks which value is 73.348 and 3.6213 is respectively. CV of NIBL is lower than other so NIBL is more consistency than other sample banks.

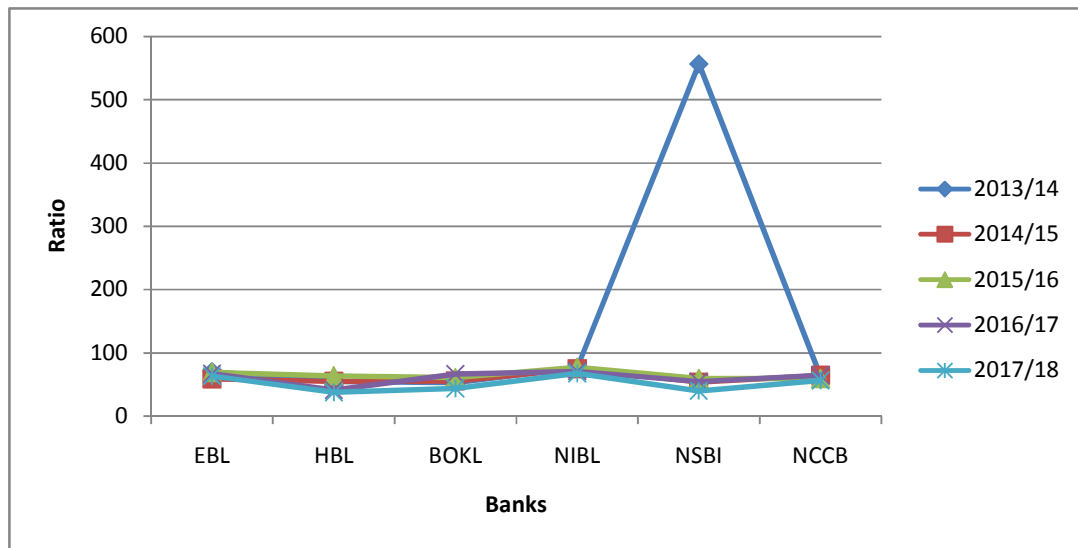


Figure 4.6: Bank Efficiency

Table 4.6 shows that Bank efficiency ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 65.618, 50.452, 55.784 and 73.348 respectively. Average Bank Efficiency, SD of NIBL is higher than other sample banks which value is 73.348 and 3.6213 is respectively. CV of NIBL is lower than other so NIBL is more consistency than other sample banks.

4.1.7 Credit risk

Credit risk is an investor's risk of loss arising from a borrower who does not make payments as promised. Such an event is called a [default](#). Another term for credit risk is default risk. Investor losses include lost [principal](#) and [interest](#), decreased [cash flow](#), and increased [collection costs](#), which arise in a number of circumstances. Credit risk is the major risk that banks are exposed to during the normal course of lending and credit underwriting.

In other term, the risk associated for nonpayment of interest and principal for credit facilities extended to the clientele is credit risk.

Table 4.7***Credit Risk***

Banks	EBL	HBL	BOKL	NIBL	NSBI	NCCB
2013/14	0.78	0.72	0.8	0.72	0.76	0.79
2014/15	0.67	0.75	0.79	0.75	0.73	0.81
2015/16	0.75	0.8	0.85	0.8	0.79	0.84
2016/17	0.83	0.84	0.88	0.85	0.81	0.87
2017/18	0.76	0.87	0.9	0.88	0.86	0.85
Mean	0.756	0.794	0.843	0.798	0.789	0.832
S.D	0.052	0.055	0.043	0.060	0.044	0.029
CV	6.867	6.971	5.122	7.479	5.613	3.435

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI & NCCB F.Y 2013/14 to 2017/18

Table 4.7 shows that credit risk ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 0.758, 0.796, 0.844 and 0.80 respectively. Average and SD credit risk ratio of EBL is lower than other sample banks which value is 0.758 and 0.051 is respectively. CV of EBL is lower than other so EBL is more consistency than other sample banks.

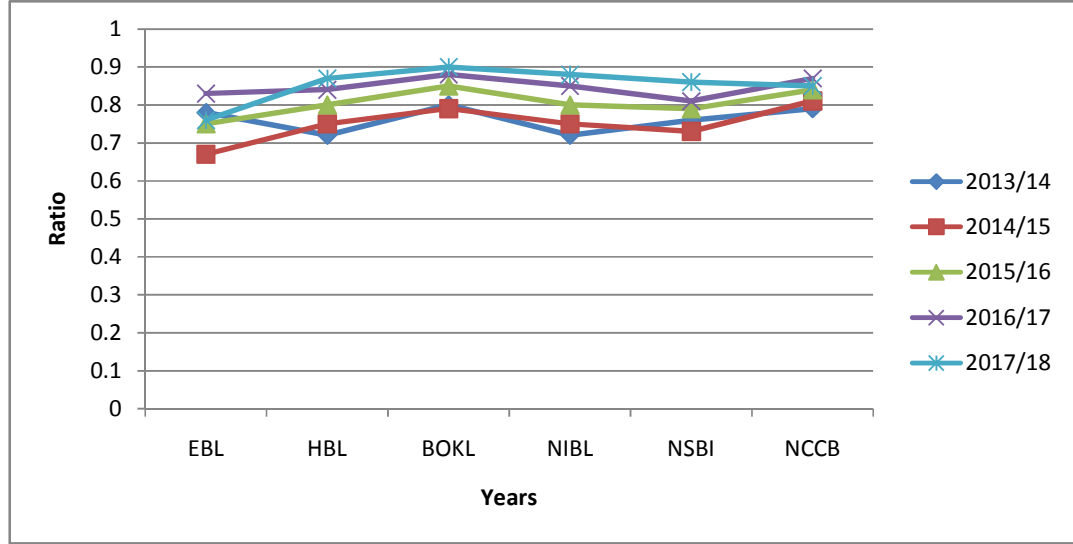


Figure 4.7: Credit Risk

4.1.8 Non-performing loan ratio

Non performing assets to total assets

This ratio indicates the ratio between the non – performing assets and total assets. Higher NPA to total assets implies ratio implies the bad effect in banks performance and it decreases the profitability of the banks and lower ratio implies the better performance of the bank and it increases the profitability of banks. This ratio can be calculated as follows:

Table 4.8

NPL Ratio

Banks	EBL	HBL	BOKL	NIBL	NSBI	NCCB
2013/14	0.97	1.96	1.78	1.77	1.96	3.78
2014/15	0.66	3.22	0.64	1.25	1.08	3.01
2015/16	0.38	1.23	0.55	0.68	0.98	2.52
2016/17	0.25	0.85	0.38	0.83	0.81	2.02
2017/18	0.2	1.4	0.44	1.36	0.65	1.67
Mean	0.414	1.560	0.637	1.112	1.018	2.495
S.D	0.287	0.825	0.519	0.389	0.456	0.744
CV	69.425	52.911	81.460	35.020	44.829	29.820

Source: Annual Report of EBL, HBL, BOKL, NIBL, NSBI &NCCB F.Y 2013/14 to 2017/18

Table 4.8 shows that Non- Performing loan ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 0.492, 0.1.732, 0.758 and 1.178 respectively. Average and SD non performing ratio of NIBL is higher than other sample banks which value is 1.178 and 0.38 is respectively. CV of EBL is lower than other so EBL is more consistency than other sample banks.

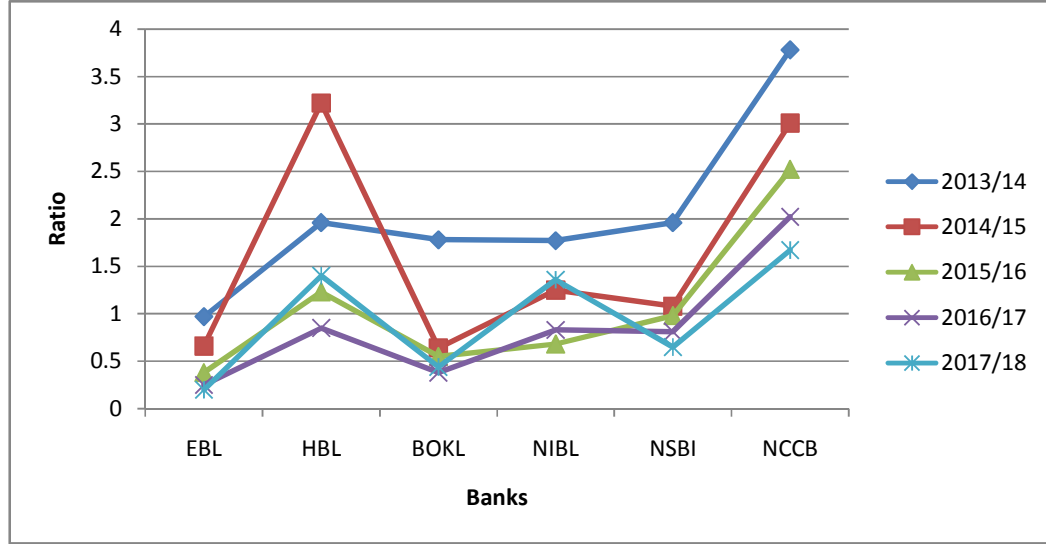


Figure 4.8: Non-Performing Loan ratio

Figure 4.8 shows that non performing loan ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 0.492, 0.1.732, 0.758 and 1.178 respectively. Average and SD non performing ratio of NIBL is higher than other sample banks which value is 1.178 and 0.38 is respectively. CV of EBL is lower than other so EBL is more consistency than other sample banks.

4.2 Descriptive statistics of variables

The summary of the descriptive statistics for all variables used in the study is presented in Table 4.6. The table reports the financial performance analysis of commercial banks in Nepal which are the Loan and Advances, Credit Risk, Bank Efficiency, NPL, Total Deposit, ROE, ROA. The result shows that the mean \pm standard deviation of ROA is 1.775 ± 0.35159 , the mean \pm standard deviation of ROE is 27.03 ± 8.44 , the mean \pm standard deviation of NPL is 1.04 ± 0.73 , the mean \pm standard deviation of Credit Risk is 0.79 ± 0.06 , and the mean \pm standard deviation of Efficiency is 61 ± 11.45 respectively.

Table 4.9***Descriptive Statistics of Variables***

	N	Minimum	Maximum	Mean	Std. Deviation
ROA	20	1.12	2.30	1.7745	.35159
ROE	20	13.66	46.10	27.0320	8.44385
NPL Ratio	20	.20	3.22	1.0404	.73635
Credit Risk	20	.67	.90	.7996	.06344
Efficiency	20	37.33	77.11	61.3002	11.45365
Valid N (listwise)	20				

4.3 Correlation analysis

This tool is used to predict the relationship between deposits and loan & advances, net profit and outsider assets and deposits and Investment. Under this study, Karl' Pearson's coefficient is being used. In order to assess the nature of the correlation between the dependent and the independent variables and to ascertain whether or not multi co linearity exists as a result of the correlation among variables, Pearson correlation coefficients were calculated and have been shown as correlation matrix in Table 4.6. The results indicate that bank financial performance indicator (ROA) is significantly positively correlated with bank size and cash reserve ratio. The result indicates that these two variables may significantly affect financial performance analysis of Nepalese commercial banks. The result further implies that large size bank with enough cash reserve can provide more loans and advances to their clients.

Table 4.10

Correlation Coefficients of Study Variables

Correlations

Variable	Correlation	ROA	ROE	NPL Ratio	Credit Risk	Efficiency
ROA	Pearson Correlation	1				
	Sig. (2-tailed)					
	N	20				
ROE	Pearson Correlation	.637**	1			
	Sig. (2-tailed)	.003				
	N	20	20			
NPL Ratio	Pearson Correlation	-.247	.057	1		
	Sig. (2-tailed)	.293	.812			
	N	20	20	20		
Credit Risk	Pearson Correlation	.042	.053	-.288	1	
	Sig. (2-tailed)	.860	.826	.219		
	N	20	20	20	20	
Efficiency	Pearson Correlation	.475*	.217	-.145	-.281	1
	Sig. (2-tailed)	.034	.358	.541	.231	
	N	20	20	20	20	20

** . Correlation is significant at the 0.01 level (2-tailed).

* . Correlation is significant at the 0.05 level (2-tailed).

The main result of a correlation is called the correlation coefficient. It ranges from the -1 to +1. The closer r is to +1 or -1, the more closely the two variables are related.

If r is close to 0, it means there is no relationship between the variables. If r is positive, it means that as one variable gets larger the other gets larger. If r is negative it means that as one variable gets larger the other gets smaller (often called as inverse correlation).

While correlation coefficient is normally reported as r = (a values between -1 to =1) squaring them makes then easier to understand. The square of the coefficient (or r square) is equal to the percent of the the variation in one variables that is related to variation in the other. After squaring r ignore the decimal point. An r of 0.5 means 25 percent of the variation is related (0.5 square =0.25). An r value of 0.7 means 49 percent of the variation is related.

There is moderate degree correlation between ROA and ROE Ratio which is statistically significant at 1% level of significance.

There is low degree negative correlation between ROA and NPL Ratio which is statistically insignificant at 5% level of significance.

There is low degree positive correlation between Credit Risk and ROA which is statically insignificant at 5% level of significance.

There is low degree of positive correlation between Bank Efficiency and ROA which is statistically correlation is significant at 5% level of significance.

There is moderate degree of correlation between ROE and NPL which is statistically insignificant at 5% level of significance.

There is moderate degree of correlation between ROE and Credit Risk which is statistically insignificant at 5% level of significance.

There is low degree positive correlation between ROE and Efficiency which is statistically insignificant at 5% level of significance.

There is low degree negative correlation between NPL and Credit Risk which is statistically insignificant at 5% level of significance.

There is low degree negative correlation between NPL and Efficiency which is statistically insignificant at 5% level of significance.

There is low degree negative correlation between Efficiency and Credit Risk which is statistically insignificant at 5% level of significance.

4.4 Major findings

The findings of the study are as follows:

- i. Average ROA of sample banks are 1.867, 1.653, 1.427, 2.076, 1.531 and 1.146 respectively and lowest coefficient variation of NIBL is 6.391 which mean NIBL is more consistent than other sample banks.
- ii. Average return on equity of EBL, HBL, BOKL, NIBL, *NSBI* & *NCCB* is 26.180, 30.797, 17.464, 31.572, 21.425 and 13.325 respectively and average ROE of NIBL is higher than other which value is 31.572. CV of *NSBI* is lower than other selected banks which mean *NSBI* is more consistency than other banks
- iii. It shows that net profit to total deposit ratio of SBI, EBL, HBL, NCCB and NIBL are in fluctuating trend during the seven years study period
- iv. EBL has not invested its total working fund in shares and debentures in the year 2011/12. SBI, EBL, HBL, NCCB and HBL have the CV of 8.28% which is lowest than other sample banks and NIBL has highest CV during the study period.
- v. Table 4.3 shows that Return on Loan and Advances Ratios of Nepal SBI bank has 0.0346, 0.0193, 0.0265, 0.0259, 0.0245, 0.0284 and 0.0238 and EBL is 0.0358, 0.0304, 0.0339, 0.0326, 0.0289, 0.0255 and 0.0297 is respectively
- vi. SBI has average net profit to investment ratio is 24.61 percent and Net profit to investment ratio of 38.24 of Everest Bank Limited. Similarly, the ratios of NCCB are 98.12, 124, 25.01, 54.02, 19.57, 21.06 and 30.16 from fiscal year 2011/12 to 2017/18.

- vii. Bank efficiency ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 65.618, 50.452, 55.784 and 73.348 respectively.
- viii. Credit risk ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 0.758, 0.796, 0.844 and 0.80 respectively. Average and SD credit risk ratio of EBL is lower than other sample banks which value is 0.758 and 0.051 is respectively. CV of EBL is lower than other so EBL is more consistency than other sample banks.
- ix. Non- Performing loan ratio of Everest Bank Limited, Himalayan Bank Limited, Bank of Kathmandu Limited and Nepal Investment Bank limited are 0.492, 0.1.732, 0.758 and 1.178 respectively. Average and SD non performing ratio of NIBL is higher than other sample banks which value is 1.178 and 0.38 is respectively. CV of EBL is lower than other so EBL is more consistency than other sample banks.
- x. The coefficient is statically significant at 10 percent level. This positive coefficient is surprising. In general understanding, the result should be negative. But at this point, it should be noted that explanatory power of the variables in the model is not strong. In addition, the level of significance is also weak.
- xi. The results indicate that bank financial policy indicator is significantly positively correlated with bank size and cash reserve ratio. The result indicates that these two variables may significantly affect financial policy of Nepalese commercial banks.
- xii. The result further implies that large size bank with enough cash reserve can provide more loans and advances to their clients. The major determinants of commercial banks' financial performance in Nepal are: bank size, liquidity, investment portfolio, and cash reserve ratio.

CHAPTER V

CONCLUSION

The last chapter of this study is summary, conclusion and recommendations developed from the study of the financial performance analysis of sample banks. Conclusion and recommendation consist of two parts, the first one is conclusion which is drawn from the major findings of this study and the second one is recommendations to the sample banks to solve the problems found on the basis of analysis and conclusion.

5.1 Discussion

Banks, which deal with commercial activities, are known as commercial banks. These financial institutes help to integrate every financial activity of the community. The main objective of a commercial bank is to play a vital role in the development of good trade. Commercial banks are mechanisms of mobilizing funds in returnable resources. They offer financial support to all types of business through providing various types of loans and other financial services. Commercial banks aid the economic development of the nation. Commercial banks pool together the savings of the community and use the funds productively through prudent investments. Integrated and speedy developed of the country is possible only when competitive banking service reach every nooks and corners of the country. Today number of commercial bank are concentrated in only few places because lack of development of infrastructure in remote places. Government must give attention toward remote places.

Rayamajhi (2015) has found that the analysis of liquidity position of these commercial banks shows different position here, the average current ratio of NSBI is great than that of NBB. Therefore, the liquidity position of SBI is in normal position. From the analysis of turnover of these two banks, NBB has better turnover than SBI in terms of loans and advances to total deposit ratio. Thus NBB has better utilization of resources income generating activities than SBI bank. Despite the fluctuating trend in the ratio of cash and bank balance to total deposit

SBI bank is more efficient than NBB in cash management i.e. it is more able to keep more cash balance against its various deposits.

Shrestha (2018) has found the correlation and the signification of their relationship between different ratios related to capital structure and found study was the banks are operating in Nepal as commercial merchant banks. The growth is still going on as so many new banks are coming into existence after this study. It is operating with higher technology and new efficient methods in banking sector. However, this study has been undertaking only three JVB's viz. SCBNL and NBBL to examine and evaluation the financial data. The findings of the study are as JVB's have used high percentage of total debt in raising the assets. The higher ratio constitutes that the outsider's claim in total assets of the bank is owner's claim.

Parajuli (2019) has found the analysis that NBBL has been successfully utilized their total deposits in terms of extending loan and advances for profit generating purpose on compared to NSBI and HBL. But NSBI is also better than HBL. It has concluded that net profit to total assets ratio in case of HBL is found better performance by utilizing overall resources but the generated profit is found lower for the overall resources in three joint venture commercial banks. In this study and previous research findings are difference due to choose the sample of banks, bank performance, return on assets, net profit margin ratio, return on equity, years to be choose the data and annual report financial indicator so the study finding's is different to previous study findings so this study is contradictory.

5.2 Conclusion

This study has investigated the determinants of commercial banks' financial performance analysis of the Nepalese context. The pooled data of four commercial banks for the period 2013/14 to 2017/18 have been analyzed using regression model. The regression results reveal that bank size has significant positive effect on loans and advances whereas liquidity ratio, investment portfolio and cash reserve ratio have significant negative effect on banks' loan advances. This study concludes that the major determinants of commercial banks' financial performance analysis of Nepal are bank size, liquidity, investment portfolio, and cash reserve ratio. There is no doubt that banking plays vital role in the development of a

country. Banking is a system in which an organized institution collects funds and mobilizes the collected funds and resources into various productive sectors. The systematic collection of idle funds and the subsequent mobilization or canalizations has supplemented not only the financial needs of trading, Manufacturing and service industries, but also provided the necessary finances for agricultural sector. Therefore, it can be said that the development in the field of industrialization and commercialization is possible only with the support of banking. Average ROA of Nepal Investment Bank Limited is 2.18 which is the highest and lower

is 1.45 in BOKL . NIBL and EBL is the less CV which means better ROA among sample commercial banks. Average Non Performing Loan Ratios are 0.492, 1.173, 0.758, and 1.178 respectively. The average CV value of the Non Performing Loan ratio of Nepal investment Bank Limited is 33.05 which is lower than other sample banks mean NIBL is better performance than others. Net profit to Investment ratio of NIBL is higher than other sample banks. Average ROE of Nepal Investment Bank Limited is higher than other sample banks and standard deviation of HBL is higher than other bank and coefficient variance of HBL is higher than other sample banks. The coefficient is statically significant at 5 percent level. This positive coefficient is surprising. In general understanding, the result should be negative. But at this point, it should be noted that explanatory power of the variables in the model is not strong. In addition, the level of significance is also weak. The results indicate that bank financial policy indicator is significantly positively correlated with bank size and cash reserve ratio. The result indicates that these two variables may significantly affect financial policy of Nepalese commercial banks. The result further implies that large size bank with enough cash reserve can provide more loans and advances to their clients.

5.3 Implications

On the basis of above reports following implications:

Implication to bank

The research was to investigate the financial performance analysis of the development banks in Nepal. This thesis is therefore paramount for guiding banking sector policy

improvements. The study is a number of policy interventions in development banking industry for improved performance in profitability and factor productivity growth which are among the key measures of bank performance in the sub-region. For bank profitability determinants, the thesis points out to the need for bank managers to gear towards optimum utilization of resources, observe prudent risk management procedures for sound and competitive services for better returns. Results also confirm the importance of bank level as well as macroeconomic factors to the bank total factor productivity growth. This would suggest that banks should ensure efficient and effective supervisory and related service for optimum utilization of resources. This would include equitable investment of resource gains from different investments such as earning bonds and securities banks trade in, prudent resource management to avoid high levels of liquidity risk, increased supervision to avoid high levels of non-performing loan ratios, ensure sound competitive environment and excellence in services to maintain competitive bank total factor productivity growth.

Implications to further scope

A wide survey can be conducted on nationalized, private, foreign and cooperative banks separately to analyze the innovative strategies adopted by the increase deposit, lending which help to increase bank size and other indicators also. A separate study can be conducted in redressed measures in commercial banks. A region wise study on financial performance analysis of development banks in Nepal may be taken up for research. In depth studies on the liquidity, profitability, assets management, credit risk ratio of development banks may be pursued.

Implication to management level

The study strategic and financial results are closely linked, and the performance in one area can impact the other. A high level of financial performance may result from an effective strategy, but good financial results let you pursue strategies that require substantial investments. When you develop effective strategies and implement them so they achieve the desired financial results, they can give you the flexibility to pursue additional strategic initiatives. The financial performance implications, it has to define the goals of your financial and strategic initiatives. To what extent you have reached the financial and strategic targets you set defines the level of performance achieved. If

performance is not uniform, it can check whether poor performance in one area had implications in the other. It is more better in regard to safety that other means of investment. It is very important to know that the increase in large amount on assets as cash and bank balance is not considered good from the profitable point of view of the bank as it doesn't earn any return. It is also a genuine means of utilization of resource. Recently, government has controlled the interest rate to reduce such activities. So it is recommended to increase the ratio, with investing its funds in shares and debentures of different types of other companies in different areas.

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