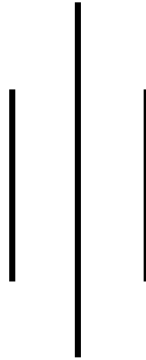


**ANALYSIS OF NON-PERFORMING ASSETS OF COMMERCIAL
BANKS OF NEPAL**
**(A Comparative Study on non-performing Assets of Nabil Bank Ltd. and
Himalayan Bank Ltd.)**



By

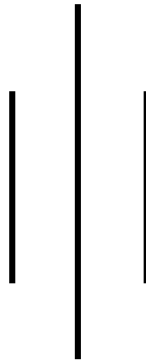
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A Thesis Submitted to:

Office of the Dean

Faculty of management

Tribhuvan University

In partial fulfillment of the requirement for the Degree of Master
of Business Studies (M.B.S)

Kathmandu, Nepal.

August 2010

RECOMMENDATION

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DECLARATION

I hereby declare that the work reported in this entitled" **Analysis of non-performing Assets of Commercial Bank of Nepal**" submitted to office the Dean, faculty of management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the Master's Degree in Business study (M.B.S) under the requirement for the master's Degree in Business study.(M.B.S) under the supervision of Prof. Dr K.D.manandhar of shanker Dev Campus.

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LIST OF ABBREVIATIONS

NPA:	Non-Performing Assets
NRB:	Nepal Rastra Banks
NABIL:	Nepal Arab Banks limited.
HBL:	Himalayan Bank Limited
ATMs:	Automatic Teller Machines
CD:	Credit Deposit
MOF:	Ministry of Finance
SEBON:	Security Exchange Board of Nepal.
ROE:	Return on Equity
ROA:	Return on Assets
CAR:	Capital Adequacy Ratio
NBL:	Nepal Bank Limited
RBB:	Rastriya Banijya Bank.
NPL:	Non-Performing Loan
T.A:	Total Assets
T.L:	Total Loan
C.V:	Coefficient of Variation
S.D:	Standard Deviation

CHAPTER-I

INTRODUCTION

1.1 Background of the Study

Financial intermediaries are vital in the economic prosperity of the nation. There are different types of financial intermediaries or financial institutions such as Commercial Banks, Development Banks, Finance Companies, Cooperatives, etc. Among all those institutions, the commercial banks are the key players in the economy of the country. Economic liberalization of Government has encouraged the establishment and Growth of financial institutions in Nepal.

Banks are the backbone of a country's economy. Commercial banks are like financial department stores that provide a number of services to the people. There are numerous services to the people. There are numerous services provided by commercial banks like accepting deposit, providing financial securities, granting loan, money exchanges, financial consultancy, fund transfer, etc. Commercial banks work as intermediaries between the two sectors of the economy; The Surplus sector and the Deficit sector.

The Surplus sector includes the people who are middle and lower class people who save money that is not enough to invest or start a new business. Generally they are employees and labors. They generally do not want to take risk.

The Deficit sector comprises the business people who always seek money to invest in the business. They are investor rather than saver. They are risk taker.

The commercial bank collects money in small amount from the surplus sector and gives to the deficit sector. While collecting money from surplus sector bank gives the guarantee of repayment of money as well as certain amount as interest. On the other hand while giving money to the deficit sector as a loan, it will charge certain percent as interest which is greater than the paid to saver.

The mushrooming growth of the banks has led them towards cutthroat competition. On the other hand economic condition of the country is not growing. The less opportunity for getting avenues for loan flotation has compelled the banks to finance without being choosy. Quality of the loans and advances could not be maintained to the desirable level if there is no choice whether to finance or not once the loan is given it is supposed that the repayment of interest or principal shall have to be served without any hindrance. The resources could not be considered utilized properly when the loans provided to the clients not be regular and if there is cumulative overdue outstanding. There may be various reasons behind the loans that turn irregular from regular one. The main reason may economic situation of the country which has global and far reaching impact. The smooth operation of the commercial banks is possible only when the economy of the country functions well. Satisfactory level of return on investment is the prerequisite for the financial sector to be groomed. The other contributing factors that turn the good loan into bad are attitude of the borrower, types and quality of security taken and legal hurdles created by the borrower when the recovery action is started. Once the distributed loan is not returned timely by clients and becomes overdue than it is known as NPA for the banks. Reduction of NPA has always been a significant problem for every commercial banks and proper attention for the management of the NPA under top priority. Due to various hurdles on way of management of NPA, commercial banks are now losing their profitability and struggling for their existence.

Operation of the banking institution has been regulated by the international norms, relevant acts, regulation, Memorandum of Association (MOA), Article of Association (AOA), institution given at the time of getting intent and Directives issued by Central Bank from time to time. Likewise the expectation of the stakeholder should also be taken into consideration. All banking institutions are supposed to confine their activities within that periphery.

BY taking the overview of financial institutions providing banking facility in Nepal there are 27 commercial Banks, 78 Development Banks, 16 micro-credit Development Banks, 78 Finance companies, 16 Co-operatives societies (licensed by NRB for limited transaction).

Table No.1.1
List of Commercial Banks in Nepal.

Class A: Commercial Banks				
S.No.	Names	Operation Date (A.D.)	Head Office	Paid up Capital (Rs. In Million)
1	Nepal Bank Limited	1937/11/15	Kathmandu	380.4
2	Rastriya Banijya Bank	1966/01/23	Kathmandu	1172.30
3	Agriculture Development Bank Ltd.	1968/01/02	Kathmandu	10777.50
4	Nabil Bank Limited	1984/07/16	Kathmandu	1449.10
5	Nepal Investment Bank Limited	1986/02/27	Kathmandu	2409.10
6	Standard Chartered Bank Nepal Limited.	1987/01/30	Kathmandu	1398.50
7	Himalayan Bank Limited	1993/01/18	Kathmandu	1600.00
8	Nepal SBI Bank Limited	1993/07/07	Kathmandu	1653.60
9	Nepal Bangladesh Bank Limited	1994/06/05	Kathmandu	1860.30
10	Everest Bank Limited	1994/10/18	Kathmandu	1030.50
11	Bank of Kathmandu Limited	1995/03/12	Kathmandu	1182.20
12	Nepal Credit and Commerce Bank Limited	1996/10/14	Siddharthanagar, Rupandehi	1399.60
13	Lumbini Bank Limited	1998/07/17	Narayangadh, Chitawan	1294.50
14	Nepal Industrial & Commercial Bank Limited	1998/07/21	Biaratnagar, Morang	1311.50
15	Machhapuchhre Bank Limited	2000/10/03	Pokhara, Kaski	1479.10
16	Kumari Bank Limited	2001/04/03	Kathmandu	1304.90
17	Laxmi Bank Limited	2002/04/03	Birgunj, Parsa	1613.50
18	Siddhartha Bank Limited	2002/12/24	Kathmandu	1230.00

19	Global Bank Ltd.	2007/01/02	Birgunj, Parsa	1325.10
20	Citizens Bank International Ltd.	2007/06/21	Kathmandu	1196.00
21	Prime Commercial Bank Ltd	2007/09/24	Kathmandu	1263.70
22	Sunrise Bank Ltd.	2007/10/12	Kathmandu	1419.70
23	Bank of Asia Nepal Ltd.	2007/10/12	Kathmandu	1105.30
24	DCBL Bank Ltd.	2008/05/25	Kamaladi, Kathmandu	1740.4
25	NMB Bank Ltd.	2008/06/05	Babarmahal, Kathmandu	1430.00
26	Kist Bank Ltd.	2009/05/07	Anamnagar, Kathmandu	2000.0
27	Janata Bank Nepal Ltd.	2010/04/05	New Baneshwor, Kathmandu	1400.0

1.2 Profile of Selected Banks

In this study, two commercial banks are selected. Brief profile of those banks is presented below.

These profiles are related to the establishment, objectives and facilities granted by the concerned banks.

NABIL Bank Limited (NABIL)

NABIL is newly named of previous Arab Bank Limited NABIL, which is the first joint venture bank of Nepal was established in 1984 A.D. under the company Act, 1964 A.D. It is joint venture with the United Arab Emirates Bank.

The bank has been functioning with a total network of 36 branches across the country. The head office of bank is Kamalidi and other are branches which are, Kantipath, Balaju, New Road, Jorpati, Thamel, Maharajgunj, Kuleshwor, Maitidevi, Chabhil, Credit Card Counter at Tribhuvan International Airport and Thamel, Birgunj, Pokhara, Parsa, Butwal, Biratnagar, Itahari, Dang, Bhairawaha, Nepalgunj, Dharan, Narayangadh, Lalitpur, Bhaktapur, Baglung, Tulsipur, Ghorahi, Dhagadhi, Mahendranagar, Damak and Birtamod.

Nabil Bank provides a fully range of commercial banking through its 19 points of representation across the kingdom and over 170 reputed correspondent banks across the globe. Operation of the bank including day to day operations and risk management are managed by highly qualified and experienced management team. The publication of the Financial Times, London, has honored the NABIL as "Bank of the year 2004"

Various facilities (Products & Services) have been provided by NABIL. It provides loan, Bills discounting facility under suppliers Credit, Export loan, Hire Purchase, Project finance, Consortium/ Syndication loan, Mortgage loan, loan Against Deposit and Government Security, Housing Finance, Auto Finance, Nabil Property and Personal finance.

NABIL receives deposit by Current, Call, Time, Normal Savings, Lok Bachat, Nabil Bachat, Student Saving, BAL Bachat, Jestha Bachat, Jestha Muddhati, Retirement Fund, Provident Fund.

It also serves for Trade Finance (Import LC, Export LC, Forward contract, Bid Bond etc).

Remittance facilities (Swift transfer, Western union, E-Remittance (Qatar Doha), Travelers cheque, Bank transfer etc), Card & ATMs, E-Banking, Clean Bills etc. And other facilities are U.S. visa fee, Safe Deposit Locker, Balance certificate, Advance Payment Certificates. Its current share capital Rs. 96,57,47,000 & Total Assets Rs 43,86,73,97,504.

Himalayan Bank Limited (HBL)

Himalayan Bank was established in 1993 in joint venture with Habib Bank Limited of Pakistan. Himalayan Bank is also the first commercial bank of Nepal with most of share held by private sector of Nepal. Despite the cut throat competition in the Nepalese Banking Sector, Himalayan Bank has been able to maintain a lead in the Primary banking activities - loan & Deposits.

Legacy of Himalayan lives on in a institution that's known throughout Nepal for its innovative approaches to sale/ merchandising products and customer services such as Premium Saving Account, HBL Proprietary Card and millionaire Deposit scheme, ATMs and Tele-banking. ATMs and Tele-banking were the first customer service products, which are first introduced by Himalayan bank in Nepal. It is currently supplying its service through 32 branches. All branches of HBL are integrated in to Globes, the single banking software where the bank has made substantial investments. This has helped the Bank Provide service like ' Any Branch Banking Facility, Internet Banking and SMS Banking'.

HBL very recently introduced several new Product and Services such as millionaire Deposit Scheme, Small Business Enterprises Loan, Prepaid Visa Card, International Travel Quota, and Credit Card etc. HBL has developed exclusive and proprietary online money transfer- Hima Remit Tm. HBL is the biggest inward remittance handling Bank in Nepal.

The mission of HBL to become a **Leading Bank of the country** by providing Premium products and service the customer. Thus ensuring attractive and substantial returns to the stakeholders of the Bank. The mission of HBL is to become preferred Provider of quality financial services in the country. There are two components in the mission of the Bank, **Preferred Provider and quality financial Services.**

The objectives are to become the Bank of first choice is the main objective of the Bank. HBL is providing loan/credit facilities such as overdraft loans, demand loans, time loans, trust receipt loans, fixed term, project financing, revolving cash credit, packing credit, post shipment, personal loan, loan against fixed deposit, counter guarantee, letter of credit, bid bond, performance bond, advance payment guarantee, hire purchase loan, housing loan. and other facilities provided by HBL are funds transfer, HBL credit card facilities, letter of credit service, SMS banking, etc. Its current share capital is Rs1, 216,215,000 and Total Assets is Rs. 39,320,322,069.

1.3 Focus of Study

The research is based on the impact of NPA on profitability of commercial banks. Currently some Nepalese commercial banks are facing huge amount of Non Performing Assets. Banks should minimize NPA level to achieve their financial goal.

Government owned banks have huge amount of NPA level with comparison to private banks. This research also focused causes impact and remedies of burning problem of NPA level with

the help of secondary data analysis. In the same way the study will also be focused on non performing assets regarding made in the past five years of two sample banks.

1.4 Statement Problem

The commercial banks give loans to the deprived sectors and the loan receiver is entitled to pay the interest and the principal amount on time. But in practice all loans are not recovered as per the sanction or within the expiry of repayment period. The study has identified the following research question.

- a. Is the NPA level of commercial banks lies within the international standard?
- b. Is there any significance difference between the NPAs of commercial banks of Nepal?
- c. What are the causes of NPA?
- d. What is the trend of NPA of commercial banks?
- e. What are the methods to control NPA?
- f. What is the overall impact of NPA on the profitability of the bank?

1.5 Objectives of the Study

The general objective of this research is to analyze the NPA and the loan and advances of the commercial banks of Nepal. The specific objectives of this research are as follows.

-) To examine the highlight the trend and level of Non Performing Assets of the Commercial banks of Nepal.
-) To evaluate the relationship between the ratio of income and the Non Performing Assets to the Loan and Advances.
-) To analyze the impacts of Non Performing Assets to the bank.
-) To provide the necessary suggestion and recommendations on the basis of analysis.

1.6 Significance of the Study

Loan is the main area of the commercial bank. It plays the significant impact on commercial banks profitability and goodwill. But most worry factor in banking sector is the total management of loan. if management and economic condition is not good the commercial banks are facing high level of NPA.

Nepal Government has just enacted the debt recovery act approved the long waited regulation on debt recovery to speed up the financial reforms in the financial sector.

The proposed of the study will make comparison between the NPA of commercial banks of Nepal and International standard. It will also check the NPA level between the commercial banks.

This study would be important as it provides theoretical as well as conceptual framework of different aspects of Non Performing Assets (NPA).

1.7 Limitation of the Study

Every study has its limitations. The main limitation of the study is that, this study is mainly based on secondary data, published books, unpublished reports, and annual reports of the selected banks and so on. Errors are inevitable but we have to give full effort to minimize them. We have to do many things staying within many types of limitations and boundaries.

The study has been subject to the following limitations.

-) The study is based on data and information provided by commercial banks and published in the report of NRB.
-) The study has been secondary data.
-) The research is based on data and information of only five fiscal years.
-) The figures are rounded for nearest rupee.
-) The research has been done for only two sample commercial banks therefore the result of this study cannot be generalized.

1.8 Organization of the Study

The research work has been divided into five chapters, namely:

Chapter I: Introduction

The first chapter includes various aspects of this study like background of the study, statement of the problem, focus of the study, objectives of the study, significance of the study, limitation of the study and organization of the study, brief profile of selected banks.

Chapter II: Review of Literature

The second chapter deals with the review of available literature. In this chapter both conceptual and theoretical review is done. It includes reviews of books, banking journals, websites etc.

Chapter III: Research Methodology

The third chapter will explain the research methodology used in the study, which includes research design, source of data, method of data analysis with different statistical and financial tool used in the study. It provides guidelines and gives a road map to analyze the collected data.

Chapter IV: Data Presentation and Analysis

This chapter covers analysis, presentation and interpretation of the acquired data, which was collected through the designed methodology. Data are presented in tabular, graphic or in an equation form to achieve pre-stated objective. This chapter provides a shape to facilitate the analysis of relevant data in an attractive way.

Chapter V: Summary, Conclusion and Recommendations

The fifth or final chapter includes summary, conclusion and recommendation that can be useful for academicians as well as for practitioners.

CHAPTER-II

REVIEW OF LITERATURE

Review of literature is a basic requirement for any research. Review of literature means reviewing research studies or other relevant proposition in the related area of the study so that all the past studies, their conclusions and deficiencies may be know and further research can be conducted. It is an integral and mandatory process in research works. The review of literature helps the researcher to avoid repetition in the same task or dead end task in the area. This part of the study will be directed to examine and review some of the related books, articles published in various news papers, economic journals, newsletters, related business magazines and websites. In short there is a significant important of review of literature:

-) To identify the problem
-) To determine the methodology for research work
-) To draw the scope of studies
-) To avoid unintentional replication of previous studies
-) To interpret the significance of researcher results in a precise manner

This chapter is related to examine and review some related to books, articles, published and unpublished different economic journals, bulletins, magazines, newspapers and web sites. This chapter has been divided into the following parts.

- i. Conceptual framework.
- ii. Review of related studies
 -) Review of thesis
 -) Review of articles and journals.
- iii. Research gap

2.1 Financial Institution

Financial institutions are the organizations that issue financial claims against themselves and use the proceeds to purchase to purchase primarily the financial assets of others. They are financial intermediaries through which savers can indirectly provide funds to borrowers.

They actively participate in the money market and the capital market, as both suppliers and demanders of funds. They act as the bridge between the savers and users of the fund. In other words, they collect the scattered deposits and give loans or invest to maximize their wealth.

Financial institutions refer to any institution established with the objective of providing loan to agriculture, cooperative, industry or any other specific economic sector, or of accepting deposit from the general public. The term also refers to any other institution called financial institution by NG by publishing a notice in Nepal Gazette. However, the term does not signify commercial bank, (NRB Act, 2012).

Financial institutions are interposed between the ultimate borrowers and lenders to acquire the primary securities of the borrowers and provide other securities for the portfolio of the lenders – Gurely, J.N. and Shaw E.S.

In a broad sense, financial institutions include all the institutions engaged in the business of financial intermediation between depositors and borrowers and borrowers. These financial institutions can be classified into (Dahal and Dahal, 1992:168).

a) Banking Financial Institutions

Banks are the financial intermediaries with which people are most familiar. A primary job of banks is to take in deposits from people who want to save and use these deposits to make loans to people who want to borrow. Banks pay depositors interest on their deposits and charge borrowers slightly higher interest on their loans. The difference between these rates of interest covers the banks cost and returns some profit to the owners of the banks.

Besides being financial intermediaries, banks play a second important role in the economy; they facilitate purchases of goods and services by allowing people to write checks against their deposits. In other words, banks help create a special asset that people can use as a medium of exchange. A medium of exchange is a n item that people can easily use to engage in transactions. A bank's role in providing a medium of exchange distinguishes it from any other financial institutions. Stocks and bonds, like bank deposits, are a possible store of value for the wealth that people have accumulated in past saving, but access to this wealth is not as easy, cheap, and immediate as just writing a check. (Mankiw, 2000:557)

This institution offers the public both deposit and credit services, as well as a growing list of newer and more innovative services, such as investment advice, security underwriting, and financial planning (Rose, 2001: 82). They devote most of their resources to meeting the financial needs of business firms. However, banks have significantly expanded their offerings of financial services to consumers and units of government. It includes Commercial banks, Development Banks, etc.

b) Non Banking Financial Institutions

These institutions began primarily to reach small savers and help these customers achieve home ownership and other personal goals. Non Banking Financial institutions include Finance companies, Cooperatives, Credit Unions, Saving banks, money market funds, Postal Saving, Insurance companies, Welfare Fund, etc.

2.2 Commercial Banking at A Glance

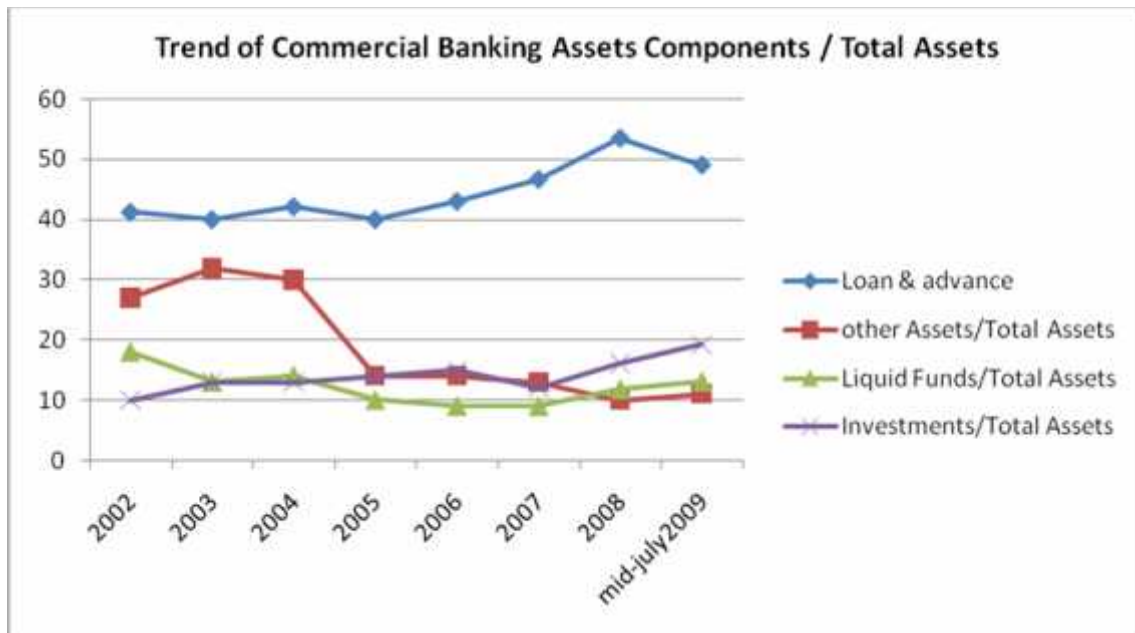
(NRB, Banking and Financial Statistics, 2009).

The number of commercial bank branches operating in the country reached to 752 in mid-July 2009. Of the total bank branches more than 50.39 percent i.e. 379 bank branches are concentrated in the central region. In the eastern, western, mid- western region 147, 135, 57 and 34 bank branches are in operation respectively.

An increment in the number and business of commercial bank contributed to impressive growth in the size of total assets i.e.; sources of fund. The total sources of fund of commercial bank increased by higher rate of 43.30 percent in mid-July 2009 compared to 15.15 percent in the same period of the previous year. At end of the mid-July 2009, the total sources of fund of the commercial banks reached to Rs. 812165.9 million. It was Rs. 566736.0 million in mid July 2008. Loan and advances, the major components of assets, decreased to 49.02 percent in Mid-- July 2009 from 53.45 percent in Mid-July 2008. Similarly, investment and liquid funds, other components of assets, registered the 16.11 percent and 13.05 percent respectively. In the preceding year, the respective shares were 19.23 percent and 11.80 percent.

Figure 2.1

Trend of Commercial Banking Assets Components / Total Assets



Source: NRB, Banking & Financial Statistics, 2009.

In the Mid-July 2009, the loans and advances increased at lower rate of 31.44 percent compare to 32.30 percent in Mid-July 2008. By the end of mid-July 2009, the total outstanding amount of loans and advances of commercial banks reached to Rs 398143.0 million. It was Rs 9960.7 million in Mid-July 2008.

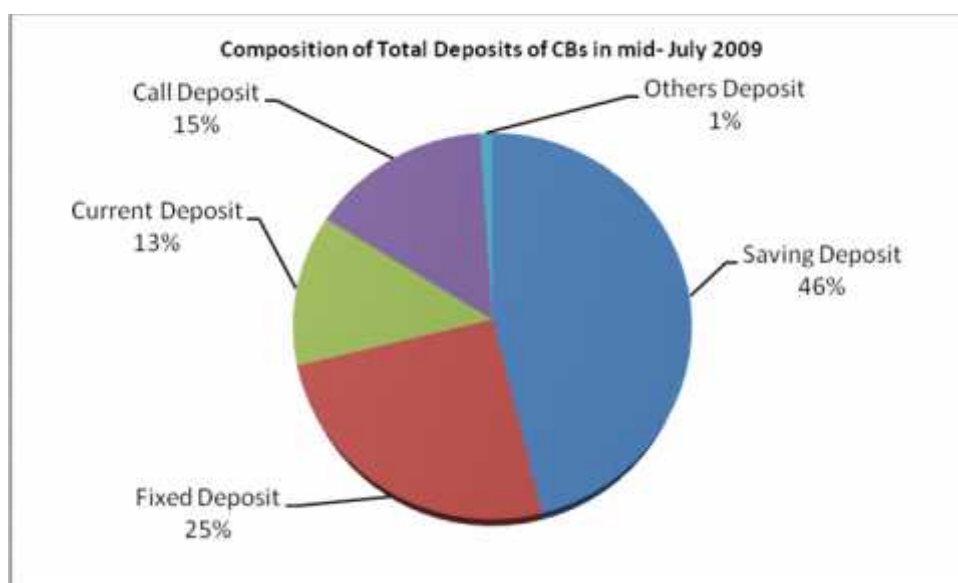
The composition of liabilities of commercial banks shows that, the deposit has occupied the dominant share of 69.40 percent followed by capital fund 3.74 percent and borrowings 2.26 percent in the Mid-July 2009. The respective shares of deposit, capital fund and borrowings in the previous year were 75.18 percent, 1.76 percent and 2.54 percent respectively.

In the Mid - July 2009, total deposit of commercial bank increased by 32.28 percent compare to 26.25 percent growth in the Mid - July 2008. In Mid - July 2009, it reached to Rs 563604.5 million from Rs 426080.3 in mid - July 2008. On an average 10.98 percent annual growth rate was observed during the 2001 2009 period. Among the component of deposit, current deposit increased with rate of 27.74 percent compare to 24.56 percent in lat year. Similarly, saving deposit and fixed deposit increased by 22.92 percent and 34.82 percent respectively.

Of the components total deposit, saving deposits, fixed deposit, current deposit and call deposit are 46.12 percent, 25.06 percent, 12.71 percent and 15.11 percent. In the last year the respective share of saving, fixed, current and call deposit were 49.63 percent, 24.59 percent, 13.16 percent and 11.62 percent.

Figure 2.2

Composition of Total Deposits of Commercial Banks



Source: NRB, Banking & Financial Statistics, 2009

The total investment of commercial banks in mid- July 2009 increased by 61.31 percent and reached to Rs 130856.9 million from Rs 108954.8 million in mid - July 2008. Similarly liquid fund increased by 58.49 percent and amount to Rs 105989.0 million.

The sector wise loans and advances of the commercial banks in mid-July 2009 reached to Rs 396858.0 million. Out of these ,the production sector constituted the highest share of 21.93 percent followed by the other sector 18.34 percent, wholesale& retailer 17.06 percent, construction 11.23 percent and finance, insurance & fixed assets by 9.73 percent. Similarly, service industries comprise 6.35 percent, transportation, communication & public services by 4.54 percent and agriculture by 3.34 percent in the same year.

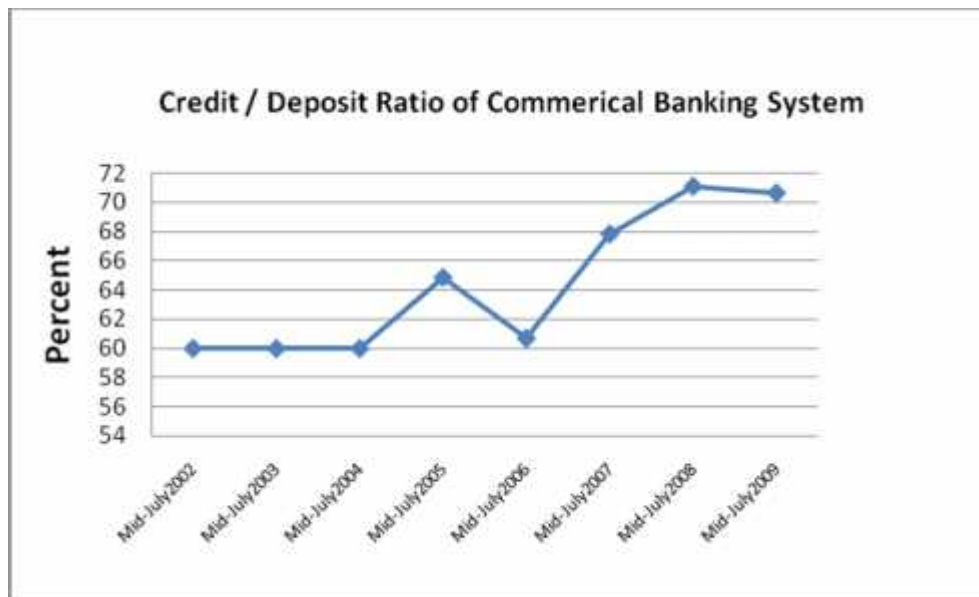
The outstanding of deprived sector credit of commercial banks in the mid-July 2009 increased by higher rate of 76.36 percent and reached to Rs 13565.1 million. It was Rs 7691, 40 million in mid-July 2008. The ratio of deprived sector credit to total outstanding of

product wise loans & advance stood at 2.96 percent in the current fiscal period. Last year it was 2, 82 percent.

Credit deposit ratio of commercial banking system did not undergo a noteworthy change during 2002-2009 mid- July. It was 2002 to 2004 remained consist around 60 percent. It was increased to 64.86 percent in mid July 2005. It declines to 60.7 percent in mid July 2006 and it increase 67.84 percent in mid July 2007, 71.09 percent in mid July 2008 and decreased 70.64 percent in mid July 2009.

Figure 2.3

Credit / Deposit Ratio of Commercial Banking System



Source: NRB, Banking & Financial Statistics, 2009.

In mid- July 2009, the credit to deposit ratio of the commercial banks remained decreased by 0.45 percent from 71.09 percent to 70.64 percent in mid- July 2009.

The non-performing loan of commercial banks declined significantly to 3.53 percent in mid- July 2009 from 6.08 percent in the mid- July 2008. The total amount of NPA remained to Rs. 13574.6 million from Rs. 18648.5 million in mid- July 2008.

2.3 Financial Markets

The term financial markets refer to the network of borrowers and lenders of funds within the economy and to the general market place through which borrowers and lenders are brought together. There is the need for infrastructure since it is typically provided by the arrangements for trading in securities. It is the mechanism created to facilitate the exchange of financial assets.

Investments are made in assets. Assets, generally, are of two types, Real Assets (Land, Building, Factories, Vehicles, etc) and Financial Assets (Stocks, Bonds, T-Bills, etc). These two types of investment are not competitive but complementary. The markets where financial assets are traded are called Financial Markets.

Financial markets can be classified on different basis as given below.

2.3.1 Primary and Secondary Market

This classification is on the basis of securities traded. Primary market refers to the market where new securities are issued for the first time to raise funds. Securities traded in the primary market for the very first time referred to as Initial Public Offering (IPO).

Secondary market refers to the market where existing or already outstanding securities are traded among investors. NEPSE is an example of secondary market.

2.3.2 Money and Capital Market.

On the basis of life span of securities, financial markets are classified as money and capital market. Money market refer to the market where short term highly liquid debt securities are traded. A money market typically involves financial assets that have a life span of one year or less. Money market instruments include short term of deposit marketable, liquid and low-risk securities. It includes T-Bill, negotiable certificate (CDs), Bankers, acceptances, Commercial Papers, etc.

Capital markets are the markets meant for long term securities. Capital markets typically involve financial assets that have life spans of greater than one year.

2.3.3 Loan and Security Market

Another way of classifying financial market is to divide them into market for loans and market for securities.

Market for loan is negotiated face to face directly between the borrower and lender. Securities market is impersonal or open market where buyers and sellers of securities are unknown to

each other. Trading is done through the help of the brokers or dealers.(Shrestha and Bhandari, 2004)

2.4 Types of Loan

A loan-unlike equity-is a fixed payment contract, irrespective of whether there is profit or not. Yet businesses fail and the contractual payments are not honored. If the loan is secured through collateral, the bank can seize and sell the collateral, but in many countries that involves legalities and delays.

Loans and advances are the primary assets of the commercial banks. Most of banks fund are used to acquire earning assets, which provide the bulk of revenue and enable them to cover expenses, including the cost of capital. There are various types of bank loans, according to the way in which the interest payments are calculated. Banks loans may be classified as, (Shrestha and Bhandari, 2004: 263-266).

2.4.1 Amortized Loans

Amortized loan refers to the determination of the equal annual loan payments necessary to provide a lender with a specified interest return and repay the loan principal over a specified period, so the loan takes the form of an annuity.

In the amortized loans system, first step is to calculate installments to be paid for every period. Suppose the loan amount is Rs. L , the rate of interest is K percent per period, and the number of payments is n , then the installment payment can be calculated as follows.

2.5 Loan Management

Loan and advances dominate the asset side of the balance sheet of any bank. Similarly, earnings from such loans and advances occupy a major space in income statement of the bank. Lending can be said to be the *raison d'etre* of a bank. However, it is very important to be reminded that most of the bank failures in the world are due to shrinkage in the value of loan and advances. Hence, loan is known as risky assets. Risk of non-repayment of loan is known as credit risk or default risk. (Bhandari, 2003: 114).

Performing loans have multiple benefits to the society while non performing loans erode even existing capital. Considering the importance of lending to the individual bank and also to the society it serves, it is imperative that the bank meticulously plans its credit operations. Sound credit policy, whose objectives are as follows, is a foundation in this direction.

- i. To have performing assets.
- ii. To contribute to economic development.
- iii. To give guidance to lending officials.
- iv. To establish a standard for control.

The established credit policy normally speaks about the following components.

2.5.1 Loan Volume

The policy should contain the credit deposit ratio (CD ratio) the bank wishes to maintain. CD ratio is very much influenced by the behavior of banks liabilities. The higher the volatile deposit and volatile borrowings lower the volume of loan and vice versa. Moreover, the bank should fix the amount of loan it wishes to give a single borrower. Limit should not be more than the one set by regulatory authorities. In Nepal, a bank can give maximum loan to a borrower as follows.

Funded credit:	25% of banks core capital
Non-Funded credit:	50% of banks core capital

2.5.2 Loan Mix

The bank gives loan to various sectors. This is necessary for the long term survival of the bank. Even if any sector is doing very well, the bank does not put its total money in that sector. If the bank concentrates its lending only in one sector, failure of the sector may cause bankruptcy of the bank. Even if two individual borrowing units of two sectors have the same level of risk, the portfolio risk is minimized due to diversification. There is a practice of fixing maximum amount of loan bank wants to give in one sector. Normally, the ceiling is fixed in relation to core capital of the bank. As per NRB, if a bank wishes to have credit

exposure(funded + non-funded) in any sector more than 100% of its core capital, the same should be approved by the Board of Directors and should be notified to NRB.

Similarly, the policy should have reference to short term and long term loan mix. This is very much affected by the nature of banks deposits mix and interest rate movement in the market. The bank having short term maturing liabilities go for regular amortizing and self liquidating loans through, normally, the long term gives higher rate of return. However in the scenario of rising interest rate, bank can make more money by having loan portfolio maturing in the short term.

2.5.3 Pricing

The policy should have reference to the pricing of loan services. Profitability in loan is calculated as follows.

$$P = I - O - C - D$$

Where,

P = Profitability, I = Interest, O = Operating expenses, C = Cost of fund, D = Expected default loss.

There is a practice of fixing prime lending rate. Based, on the risk, percentage is added in the prime lending rate. The higher the risk, the higher will be the rate. Being a custodian of public money, the bank however should not take risk beyond a certain level irrespective of how high the lending is. The policy should speak whether the banks adopts fixed or floating mixed type of interest rate in its portfolio. The policy should speak about compensating balance (the balance the borrower is required to maintain at the bank as a condition of the loan) and commitment fee.

Credit policy should positively react to interest rate structure in the market. Flexibility required. However, no concession beyond certain level of interest rate on the borrowers threat that they would shop around.

2.5.4 Lending Authority

This is one of the very critical aspects of loan management. Misuse of lending authority puts the bank at a risk. Some banks adopt centralized while some banks adopt decentralized approach regarding lending authority. Under centralized approach, lending authority is not given to branch staff. Under decentralized approach, a certain limit is given to forward to Head Office for approval.

2.5.5 Risk Analysis

The policy should have reference to the acceptable character of the borrower. Though it should not be like a straitjacket, the policy should specify the acceptable liquidity, leverage, coverage, efficiency and profitability ratios so that there can be consistency in the risks perceived by all lending officials.

2.5.6 Loan Classification and Provisioning

Though all loans are good at the time of disbursement, with the passage of time, they show the sign of problem. Based on the health of loan, the loan should be classified and provided accordingly. Provisioning is made as cushion against possible losses and to reflect the true picture of banks assets. Hence, there is a practice of showing net loan (total loan-loan loss provision) in the financial statements instead of gross loan. The bank should comply with statutory regulation relating to loan classification and provisioning.

NRB regulation on classification and provisioning is as follows.

<u>Type</u>	<u>Criteria</u>	<u>Provision</u>
<u>Requirement</u>		
Pass	Principal overdue up to 3 months	1%
Substandard	Principal overdue up to 6 months	25%
Doubtful	Principal overdue up to 1 Year	50%
Bad	Principal overdue above 1 Year	100%

Pass loan is called nonperforming and others are called `Non-Performing Assets`. Provision requirement in case of loan given against personal guarantee only is additional 20% for pass, substandard and Doubtful loans. Provision for restructured, rescheduled and swapped loan is 12.5% only.

For better management of loan portfolio, the management can have more classifications and can have more stringent criteria than the one fixed by regulating authorities.

2.5.7 Statutory Directives

Management should devise the policy keeping mind the statutory directives. Lending function of a bank is heavily influenced by the directives because the quality of bank's loan portfolio has to do more with risk and safety than any other banking operation.

Credit facility helps create jobs and income to thousands of people directly and indirectly thereby raising their living standard. Hence, regulatory authorities make efforts to ensure there is no discrimination to any community or any individual on the ground of race, sex, religion, age, education level etc. In USA, the community Reinvestment Act 1977 requires the banks to meet the credit needs of individuals and businesses in their territories. Similarly, Equal Credit Opportunity Act 1974 bars the banks from denying credit facilities to any individual because of their sex, religion, race, age etc.

More regulation of NRB relating lending activities of the banks are as follows.

- Single borrower limit.
- Sectoral limit.
- Directive Credit (priority sector and deprived sector limit).
- No loan to restricted areas.
- No loan to directives/employees/shareholders holding more than 1% share of the bank.
- Interest rate deviation.

2.5.8 Quality of Lending Officials

Experience, knowledge, adaptability etc of lending officers should be considered while formulating the policy.

Considering all above facts, the credit policy should be carefully established, communicated properly to the lending officers and implemented effectively by the lending officers. The credit policy of the bank is established by the board of directors based on the recommendation of Chief Executive Officer or senior loan officer.

2.6 Loan Approval Process

Loan is approved by the approving authority only after being convinced that the loan will be rapid together with interest. There are many processes involved to approve the loan which are as follows (Dahal & Dahal, 1992:121).

2.6.1 Application

A borrower is normally required to submit an application to the bank along with required documents:- Project Proposal, historical financial statements and documents pertaining to company's legal existence.

2.6.2 The Credit Analysis

Followings steps are taken to analyze/ appraise loan application:

Historical Analysis

Historical analysis refers to analysis of past financial statements and business risk. The former is quantitative while the latter is qualitative analysis. The financial analysis exhibit the financial performance of the management and business risk analysis helps to the major risk factors (supply, production, demand, collection, management) observed in the past and how management mitigated them. The underlying purpose of historical analysis is to know the major factors in borrower's present condition and past performance which foreshadows borrower's likely success or failure in repaying the debt in future.

There is a practice of analyzing 5Cs of Credit (Character, capacity, Condition, Capital, and Collateral) by the financial institutions.

Character

It refers to the personal traits (ethics, honesty and integrity) of borrowers which is very important for lending decision. Serious purpose, truthfulness in answering the queries, responsibility and seriousness in making all the efforts to repay loan make up what a lending official call the character. No further credit analysis is made if the lending official feels the borrower lacks character.

Capacity

Capacity is being used in two senses.

1. Legal Capacity to borrow money.
2. Capacity to generate enough income to repay loan or through liquidation of assets.

Condition

Condition refers to the general economic condition beyond the control of the borrower that affects the business of the borrower. This is basically security, political and other social conditions under which the business has to operate. Loan is given to the borrower if lending officials feels general condition is favorable for that type of business.

Collateral

Loan is given if the banker is satisfied that the borrower can repay money from the cash flow cash flow generated from operating activities. However, the bank wants to ensure that their loan is repaid even in case of default. In such cases, the banker asks for additional securities. Collateral can be fixed in nature land, building, machinery or working capital like inventories and account receivables.

Capital

Capital refers to the net worth of the borrower. This is covered under capacity above while analyzing the leverage ratio. Leverage ratio will be high if the borrower has low capital. A bank gives loan only when it finds leverage ratio acceptable to it or if the borrower has enough capital.

2.6.3 Forecast and Risk Rating System

Based on the findings of historical analysis, and in light of present and foreseeable future environment, the analyst has to forecast impending major risks. The analyst should also highlight to what extent inherent risks will be mitigated and how unmitigated risks can be covered.

Analysis of credit information attempts to answer the question “How risky would it be to lend to this applicant?”. Most commercial loans are risky to some degree. Up to a certain risk level, a lender may justify granting a particular loan and attempt to compensate for the relatively high risk by charging a high rate of interest and adequate securities. Above a certain risk level, loans will not be granted. Thus, it can be said that credit analysis: (1)

determines which loans will be made and which will not and (2) provides a ranking from low risk to high risk for those loans that are made, thus helping determine the rates of interest to be charged and the value of securities to be obtained.

2.6.4 Return

The amount of loan has got inherent cost as it is obtained from either shareholder or depositor or creditor. The analysis should be made to calculate total return (interest, fee and commission) and compare whether it meets banks standard.

2.6.5 Liquidation

The analyst should ascertain banks ability to recover loan in case of liquidation of the borrower. If liquidation analysis reveals insufficient security, additional security may be asked for.

2.7 Action Guidelines According to State of Loan

On different states of loan different actions should be taken. (Dahal & Dahal, 1992; 55)

2.7.1 Pass Loan

Provide “good” service, retain customer. Consider new facilities.

2.7.2 Indicative of Sub- Standard

-) Obtain legal review of all documentation.
-) No new facilities.
-) Frequent contact to gain more information/monitor problems.
-) Suggest ways to strengthen company and protect bank.
-) Consider inter-creditor agreement.

2.7.3 Substandard

-) Service not at issue, move immediately to strengthen Banks position.
-) Seek reduction in facilities and/or increase in security, restructure debt if advantageous to Bank.
-) Take “hard- line” with management, demand specific plan to improve situation.
-) Look for ways to improve management, control management, etc.

2.7.4 Doubtful

-) No interest taken to profit.
-) Look for ways to avoid losses.
-) Take legal action now, sell security if advantageous to bank, force management to repay/ finance.
-) Monitor weekly, track performance, control all assets and liabilities, if possible.

2.7.5 Bad

-) Loss inevitable, take provision to cover loss and all costs of liquidation.
-) Look for ways to minimize losses, study timing of sales.
-) Be creative, but remember time value of money.

These are general guidelines for managing loans and advances according to its state.

2.8 Financial Performance and Financial Institution

Financial soundness is a situation where depositor’s funds are safe in a stable banking system. The financial soundness of a financial institution may be strong or unsatisfactory varying from bank to another. External factors such as deregulation; lack of information among customers; homogeneity of the bank business, connection among banks do cause bank failure. Some useful measures of financial performance which is the alternative term as financial soundness are coined into what is referred to as CAMEL. The acronym ‘CAMEL’ refers to the five components of a bank’s condition that are stressed: Capital adequacy, Assets quality, Management, Earnings, and Liquidity. A sixth component, a bank’s Sensitivity to

market risk, was added in 1997; hence the acronym was changed to CAMELS.(Note: that the bulk of the academic literature is based on pre-1997 data and is thus based on CAMEL ratings.)Ratings are assigned for each component in addition to the overall rating of a bank's financial condition. The ratings are assigned on a scale from 1 to 5. (Bhandari, 2003: 127).

Capital Adequacy

This ultimately determines how well financial institutions can cope with shocks to their balance sheets. The bank monitors the adequacy of its capital using ratios established by The Bank for International Settlements. Capital adequacy in commercial banks is measured in relation to the relative risk weights assigned to the different category of assets held both on and off the balance items.

Assets Quality

The solvency of financial institutions typically is at risk when their assets become impaired, so it is important to monitor indicators of the quality of their assets in terms of overexposure to specific risks trends in non-performing loans, and the health and profitability of bank borrowers especially the corporate sector. Credit risk is inherent in lending, which is the major banking business. It arises when a borrower defaults on the loan repayment agreement. A financial institution whose borrowers default on their loan repayments may face cash flow problems, which eventually affect its liquidity position. Ultimately, this negatively impacts on the profitability and capital through extra specific provisions for bad debts.

Earnings

This continued viability of a bank depends on its ability to earn an adequate return on its assets and capital. Good earnings performance enables a bank to fund its expansion, remain competitive in the market and replenish and /or increase its capital. A number of authors have urged that, banks that must survive need: Higher Return on Assets (ROA)., better return on net worth/ Equity (ROE), sound capital base i.e. the Capital Adequacy Ratio(CAR), adaptation pf corporate governance ensuring transparency to stakeholders that is equity holders, regulators and the public.

Liquidity

Initially solvent financial institutions may be driven toward closure by poor management of short-term liquidity. Indicators should cover funding sources and capture large maturity mismatches. An unmatched position potentially enhances profitability but also increases the risk of losses. The “M” represents Management, given that this paper is hinged on financial performance, the management component is not considered in the measure.

Generally, literature on corporate governance comprises attributes such as financial transparency, disclosure and trust among others and it is revealed that financial transparency and disclosure enhance trust between the stakeholders and organizations like commercial banks. Capital Adequacy, Earnings and Liquidity are the key dimensions of measuring financial performance in Commercial Banks. In summary, this literature forms an underpinning for the establishment of the association between corporate governance and financial performance.

2.9 RISK

Risk is defined as the variability of the returns of a period. The deviation between the expected and actual return brings variability in the return and the variability is termed as risk. The higher the deviation between expected and actual return, the higher will be the risk. Risk is the uncertainty of returns and if there is certainty there is no risk at all. Risk and return in investment go together and without risk no more return can be expected.

2.9.1 Source of Risk

Various factors contribute to investment uncertainty that contribute to investment risk are as follows: (Bhattarai, 2006: 107)

2.9.1.1 Liquidity Risk

Liquidity risk is associated with uncertainty created by the inability to sell the investment quickly for cash. The return variability will increase if price discounts and sales commission

are to be given in order to liquidate assets in time. The less liquidity, the greater will be the risk. So, two factors- price and time are associated with liquidity.

2.9.1.2 Interest Rate Risk

It is the potential variability of a return caused by changes in the market interest rates. Market interest rate influences the value of an asset and hence its return. If the market interest rate rises, the value of an asset will decrease. A higher interest rate means a higher discount rate and a higher discount rate causes a lower present value of any asset.

2.9.1.3 Default Risk

Default risk is related to the probability that some or all of the initial investment will not be returned. The degree of default risk is closely related to the financial condition of the company issuing and the security is rank in claims on assets in the event of a default or bankruptcy.

2.9.1.4 Callability Risk

Some securities are issued with a call provision i.e. a company may call back the securities issued before their maturity. The callability risk is the portion of securities total variability of return that derives from the possibility that the issue may be called.

2.9.1.5. Convertibility Risk

Convertibility risk is that portion of the total variability of return from a convertible bond or convertible preferred stock that reflects the possibility that the investment may be converted into the issuer's common stock at a time or under terms harmful to the investor's best interests.

2.9.1.6 Bull-Bear Market Risk

The various market forces make securities price upward and downward. The upward trend of market price (Bull Market) and downward trend of market price (Bear Market) create a long lasting source of investment risk.

2.9.1.7 Industry Risk

Industry risk is that portion of an investment's total variability of return caused by events that affect the products and firms that make up and down to the industry. Some of the factors which affect all the firms in an industry may be the industry's life cycle, international tariffs or quotas, industry-related taxes and availability of industry related raw materials.

2.9.1.8 Management Risk

Management errors are difficult to analyze, investors can reduce their risk by buying shares in those corporations in which the executives have the significant equity investment instead of buying shares in the corporation in which executives have no equity investment.

2.9.1.9 Political Risk

Political risk is the portion of assets' total variability of return caused by changes in the political environment (domestic and international as well as the internal changes of the company).

2.9.1.10 Purchasing Power Risk

It is the variability of return an investor suffers because of inflation. Inflation (or a rise in general prices over time) seems to be the normal way of life in most countries today. However, when inflation takes place, financial assets (such as cash, stocks, and bonds) may lose their ability to command the same amount of real goods and services they did in the past. To put this in another way, the real rate of return on financial assets may not adequately compensate the holder of financial assets may not adequately compensate the holder of financial assets for inflation.

2.10 NRB Directives to Commercial Banks Relating To Credit

(NRB, Unified Directives, 2006)

2.10.1 Directive Credit

Banks have to extend a certain percentage of loan and advances in the deprived and priority. Currently, deprived sector lending should be at least 0.25% to 3 % depending on the banks and priority sector lending at least 12% inclusive of deprived sector lending to their total credit portfolio.

In case of shortfall in any sector, the concerned bank has to pay penalty at the highest lending rate of the bank during the shortfall period which is monitored quarterly.

2.10.2. Single Borrower Limit

Single borrower's limit refers to the maximum credit limits that can be extended to a customer, firm, company or companies of the same group. Such limit is currently as under:

- a. Funded: 25% of Core Capital.
- b. Non-funded: 50% Core Capital.

The bank, where, a single borrower enjoys credit limit more than above should bring it within the limit. If above limit is not observed by a bank, 30% additional risk weight is assigned to such credit portfolio warranting additional capital.

Interest Spread

Weighted interest spread between lending rate and deposit rate should not exceed 5%. Such rate is calculated as under:

$$\text{WALR} = \frac{\text{InterestIncomeForSixMonths}}{\text{AverageInterestEarningAssets}} \times \text{Outstanding on the month - end of 6 months}$$

$$\text{WADR} = \frac{\text{Interest Expenses For Six Months}}{\text{Average Deposit Outstanding on the Month end of 6 months}}$$

WALR= Weighted Average Lending Rate.

WADR= Weighted Average Deposit Rate.

Interest Spread= WALR – WADR.

Interest in move in excess of 5% spread on bi-annual basis (mid January and mid-July) should be retained in the bank as Interest Spread Reserve and no dividend can be given out of this fund. However, this fund is treated as supplementary capital.

Interest Spread limit of 5% was scrapped on 25th July 2002.

Interest Rate

Banks are free to fix interest rate on deposits and loans. Interest rates on all types of deposits and loans should be published in the local newspapers and communicated to NRB minimum on a quarterly basis and immediately when revised. Deviation of 0.50% from the published rate is allowed on all types of loans and deposits.

2.10.3 Loan Classification and Provisioning

A bank is required to classify their loan on the basis of overdue aging schedule and provide on a quarterly basis as follows:

<u>Type</u>	<u>Criteria</u>	<u>Provision Requirement</u>
Pass	Principal overdue up to 3 months	1%.
Substandard	Principal overdue up to 6 months	25%.
Doubtful	Principal overdue up to 1 Year	50%
Bad	Principal overdue up to 1 Year	100%.

Pass loan is called 'performing' and others are called 'Non-Performing Assets'. Provision requirement in case of loan given against personal guarantee only is additional 20% for pass, Substandard and Doubtful loans. Provision for restructured, rescheduled and swapped loan is 12.5%.

Provision for Pass Loan made up to 1.25% of total risk weighted assets is treated as supplementary capital.

Investment portfolio of the bank should be accounted at market value or cost whichever is less. If investment securities have not been listed in the stock market, 100% provision should be made against such an investment and deposited at 'Investment Adjustment Reserve'.

2.10.4 Sectoral Credit Limit

Credit concentration in one sector increases the risk of a bank. Hence, NRB requires banks to monitor its credit portfolio in following ways:

a. Level I: Sector where credit of a bank ranges from 50-100% of core Capital.

Bank has to devise a proper Credit Information System to monitor such credit at least quarterly.

b. Level II: Sector where credit of a bank is above 100% of Core Capital. Board of Directors of the bank should decide annually whether it wants/does not want to have credit exposure more than 100% in any sector. Decision of the Board should notify to Banking Operations Department and Supervision and Inspection Department of NRB.

2.11 Reasons for Loan Becoming Bad

One undesirable side effect of current trend in banking is a relatively high bank failure rate. For most of its history, the banking industry experienced an extremely low failure rate (only about 1 or 2 percent of the banking population each year failed) due to extensive regulation and conservative management. However, the number of bank failures and the average size of failing banks advanced sharply in the 1980s, though the failure rate slowed down in the 1990s.

Some analysts argue that even more important is the increased volatility of economic and financial conditions, especially interest rates and the prices of foreign currencies. This volatility has made bank earnings and stock prices more unstable and forced bankers to devote more time to the control and management of risk.(Rose, 2001:88)

When loans are overdue to repay their specific period then it becomes bad loan. By analyzing various studies, following are some important causes for turning a loan into a bad one.

2.11.1 Lack of Credit Policy and Culture

The credit policy generally guides the institution to disseminate and diversify the loans. It also helps in making the decision for whether or not granting the loan to a certain party. Hence a clear and in written form a credit policy is a must. The bank also must have a credit culture .They must not only focus on their loan but also the customer who is taking the loan. The credit team should know each and every loan taker and should watch from near. The bank now is not only the lender it must also act as the financial advisor also to the customer.

In Nepal only few financial Institutions have a clear-cut credit policy. At the same time credit policy should also be strictly adhered to.

2.11.2 Undue Influence/Pressure

One of the major factors contributing in Banks Non Performing assets is the undue Influence exerted by politician, bureaucrats, board members and senior executives of the bank itself. This is the reasons most of the state owned commercial banks and some private banks have large NPA.

2.11.3 Cut Throat Competition

The number of commercial banks is growing rapidly. It is nearly saturated. But the market size is very small and the economic situation is not improving. In such situation, the commercial banks have very less option to invest. Due to this, there is unfair competition exercised by the banks to attract the customer. In such situation, NPA may increase due to sanctioning the loan without studying and analyzing the client properly.

2.11.4 KYC-Know Your Customer

If we don't know our customer-in terms of his capacity, managerial ability, past tract Record, market reputation, and business he is involved and lends him, then the loan extended to Such a customer may be booked as a "Bad loan" co-instant, it is disturbed.

2.11.5 Lack of Vision

The success of any organization lies on the ability to think and have long term vision. Creativity is very essential thing for the managers to drive the whole organization to success. The managers should be able to create new products. In Nepal, there is a culture of copying others product. Recently almost all commercial banks are catering consumer loan. .Lack of Vision results in investment in those areas which will turn the loan into NPA.

2.11.6 External Factors

There are many external factors that turn a good loan to bad. Economic condition of the country, political situation, technological change, etc. also plays a key role in turning a good loan to bad. We have currently witnesses the closer of the factories in the Terai region of Nepal due to political instability. This closer of the factories, result in inability to repay loan taken by the organization although the business man do not intend to be a defaulter. (Source: National Daily Newspapers and Business Magazines).

2.12 Review of Previous Studies

2.12.1 Review of Earlier Thesis

For the purpose of this study, relevant thesis works regarding several aspects of banking sectors conducted by different intellectuals and students are discussed below:

In the research conducted by **Dirga Narayan Kafle (2005)** on "**Non Performing Loans of Nepalese Commercial Banks**", devised following major findings and suggested following major recommendations to be adopted in order to decrease the level of NPA and increase the efficiency of the commercial banking industry.

Major Findings:

- a. The return on assets (RoA) and return on equity (RoE) of the bank somehow depend upon Non Performing Loan. The bank should reduce its NPL to increase RoA and RoE of the bank.
- b. Management inefficiency is one of major cause behind high level of NPA of Commercial banks.

Major Recommendations:

- a. Those banks having high level of NPL should take immediate action. The bank should dispose off the collateral taken from the borrower and recover principal and interest amount.
- b. Corporate structure of the banks play key role in the effective loan management. There should be separate department for credit appraisal, documentation, disbursement, relationship maintenance and inspections.
- c. Maintenance efficiency should be enhanced. Hence necessary trainings should be given to the managers and staffs.

Niranjan Shrestha (2007) in his research, “**Non Performing Assets of Commercial Banks**” made following major findings and advised following major recommendations:

Major Findings:

- a. The result shows significant difference in NPA of commercial banks and international standard of 4%.
- b. High degree of negative correlation exists between NPA with RoA and RoE. The banks should reduce their level of NPA to increase RoA, RoE and profitability.
- c. Management in efficiency is one of the major causes behind high level of NPA of commercial banks.

Major Recommendations:

- a) Follow the regulation of Nepal Rastra Bank
- b) Those banks having high level of NPA should take immediate action. The bank should dispose off the collateral taken from the borrower and recover principal and interest amount.
- c) Formation of assets Management Company is necessary.

In the study of **Rajesh Bhandary** (2004) titled “Analysis of Non Performing Assets of Commercial Banks of Nepal”, he found following major findings and suggested following major recommendations.

Major Findings:

- a. There is negative correlation exists between NPA with ROA and ROE.
- b. The external factors are major contributing for the growth of NPA in any banks. Political and economic situation of the country and borrower related factors were found most crucial in the conversion of good loans into bad.
- c. Lack of asset management company, Execution of the court proceedings and cumbersome legal procedure and economic recession and political instability are major problems associated with the management of NPA.

Major Recommendations:

- a. Formulation of NPA management committee and reviewing of its performance on monthly basis may bring the colour in the management of NPA.
- b. Approaching to loan recovery tribunal for dispose off bad loans from loan portfolio.
- c. All banks should make initiative towards the establishment of Asset Management Company so that bad loans of the banks could be removed from the Balance Sheet.

2.12.2 Review of Related Journals and Articles

Narayan Sapkota (2004) in his article published on 19thMay 2004 in Rajdhani National Daily entitled "Portion of NPA in Commercial Banks – High in Public, Low in Private", has highlighted the fact of NPA as being less in private banks in comparison to public banks. He has mentioned that the NPA of two big nationalized banks (NBL and RBB) was about 60% and the loans were in very serious situation. He further added that in order to improve this situation and to make healthy banking environment, financial reform program had been brought; as its consequences, the management of these two big banks was handed to foreign company on a contract but the ratio of NPL was not reduced.

While most of the privately owned banks had NPA within international standard, some had it above that standard. As per international standard 5% NPA was acceptable during 2004. He

also mentioned the average NPA of the Nepalese banking sector to be 30% which is very high. (Source previous thesis.)

Pradhan, (2058), in his article “NPA Some Suggestions to Tackle Them” found that unless the growth of NPA is kept in control, it has the potential to cause systematic crisis. He has mentioned that a dream of globalization led to huge investment which unfortunately could not be utilize properly due to hesitant liberalization policies. Large corporate misused the credits and delayed payments and contributed indirectly for enhancing NPA ratio. He further argues that lack of vision in appraisal of proposal while loan sanctioning, reviewing or enhancing credit limits, absence of risk management policy of financing, concentration of credit in few group of parties and sector, lack of initiatives to take timely action against willful defaulters, indecision on existing out of bad loans for fear of investigation agencies like special police CIAA, public accounts committee of the parliament have also contributed in whatsoever measures to the worsening situation on NPA front. He further pointed out that most crucial reason for the increase in the NPA is the shabby and defaulter friendly legal system. Suggesting the remedy of NPA, he adds that administrative system should be strengthened. Legal reforms should be made and assets Reconstruction Company should be formed.

Professor **Bishwambher Pyakuryal** (2001) has stated in his article entitled 'Our Economy is in a Volatile Stage' that the banks have not able to collect their overdue due to the increasing cumulative NPAs in Nepalese commercial banks. There is no additional demand of the investment due to the higher risk and present uncertainty. According to his article, revenue collection was negative and regular expenditure was higher than the revenue during that time which indicated volatility of the economy. Even before the declaration of emergency, the government didn't have surplus revenue to pay for the remuneration and benefits of retired civil servants. Up to 65% of the country's development expenditure was being financed by foreign aid. He also predicted that if Nepal couldn't meet the regular expenditure through its revenue, it would be very difficult to convince the donor community. This could push the society toward what is called a 'mass unrest society.' He also added the need to establish some kind of Asset Management Company to take over the non-performing assets (NPAs) of the government-owned banks.

2.13 Research Gap

There is a certain gap between the present researches. Previous researchers are done in this topic called " Non-Performing Assets". Previously many researches were done by using secondary data. The information of this very research is also based on secondary data as well as primary data, but many effective tools and techniques are used to get the desired result as per the objectives of this study. To analyze the facts financial tools as well as statistical tools were used to desired objectives of the study. Financial tools includes ratio analysis and the statistical tools include mean, standard deviation, coefficient of variation, correlation of coefficient analysis and also include trend analysis.

CHAPTER-III

RESEARCH METHODOLOGY

3.1 Background

Research is a systematic inquiry of any particular topic and methodology is the method of doing research in well manner and human nature's get satisfied with the same thing that regularly takes place for a long time. They are always curious to learn, understand or investigate when some particular things happens or happened. Why did the things happen or do they happen? How did they happen or how do they happen? They are not satisfied till they solve the question and develop the form of their beliefs or judgment about those particular phenomena. For this they gather the information and analyze them to achieve their goal. The method that applies during this knowledge gaining research is known as research methodology means the analysis of specific topic by using a proper method. In other words, research methodology is a systematic study of the research problem that solves them with some logical evidence. The population and sample, source and data collection techniques, and data analysis tools and the hypothesis to be tested, which are associated with the study, have been discussed in this chapter.

3.2 Research Design

“Research design is a plan, structure and strategies of investigation conceived so as to obtain answer to research question and control variance. The plan mean now researcher investigator collect the data structure in term controlling the data in term of money and time.” We can say that the research design is specification of methods and procedures for acquiring the information needed. It is the plan, structure and strategy of investigation conceived so as to obtain answer to research question and to control; variances. It is the overall operational pattern of framework of the projects that stipulates what information is to be collected from which sources by what purpose.

The main objective of research design is to make analysis in non-performing assets of commercial banks in Nepal and provide valuable recommendation. In other words, this research is aimed at studying the non-performing assets of commercial banks. This will follow analytical and descriptive research design. And it also analyzes the composition of trend of non-performing assets, loan recovery and profitability condition of commercial

banks. The design for this research is made by financial statistical tools. So it can be also called roadmap for Research study or blueprint of the study. The Research Design is the overall operational pattern of frameworks of the project that stipulates what information is to be collected, from which source, by what procedures, how to conduct analysis, etc. The research design of this study is analytical as well as descriptive. This study is the evaluation of Non Performing Assets (NPA) of commercial banks of Nepal.

3.3 Population and Sample

The term ‘population’ for research means all the member of any well defined class of people, event or object. It means that the entire group of people, events or things of interest that a researcher wished to investigate. A representative part of population selected from it with the objection of investigation its propertied is called sample. For purpose of study, the random sampling had been used to analysis about total member number and inters group number.

The commercial banking industry is the population of this research. Currently there is all together 27 commercial banks operating in Nepal and out of them, two banks are taken as sample for this study. Since profitability is a factor related to NPA of banks, it was taken as the basis for taking sample. Profitability was linked with the market share value of the banks. Some of the banks in the sample have high market share value whereas some have low value. This variation was taken into consideration in order to make the study representative to the extent possible to the commercial banking industry of Nepal.

3.4 Types and Sources Of Data

For the purpose of analysis in this research, manly the secondary data will be used. The facts and figures provided by the banks will be taken into consideration. But some data which are not published will be directly collected from the bank. The bank professionals will also be interrogated wherever needed.

The main source of data is the annual reports published by the banks. The statistical reports of the NRB are also the main source. Furthermore the publications of Ministry of Finance (MoF), Security Exchange Board of Nepal (SEBON), unpublished thesis and journals,

different web sites, libraries etc. and other data published in the Newspaper and Magazines are also used.

3.5 Data Collection Techniques

In order to collect the data annual report published by the commercial banks and Nepal Rastra Bank (NRB), Economic report and other published statistical are collected. Data from such reports are used in this study and to obtain the additional information, informal talk made with bank personals. Similarly information is collected from Newspapers, Magazines, Web sites, bulletin, booklets and journal published from relative banks.

3.6 Data Analysis Tools

For the fulfillment of the study objectives various financial tools as well as statistical tools have been employed. The description of financial tools as well as statistical tools is described below.

3.6.1 Statistical Tools

The statistical tool is essential to measure the relationship of two or more variable. It is the mathematical technique used to facilitate the analysis and interpretation of the performance of the organization. It helps to compare the performance, strengthen, weakness of the organization. It also helps to present the data, show the relation and deviations or differences of variables of organizations. In this study, the following statistical tools are used:

3.6.1.1 Mean (Average)

Mean is defined as sum of observations divided by their number in the selected sample. It is the popular measure for representing the entire data. It is the average of the data. It is further used in many statistical and financial analysis tools

$$\text{Mean } \bar{X} = \frac{\sum X}{n}$$

Where,

ΣX = Sum of Variable 'X'
 n = No. of observation

3.6.1.2 Correlation Analysis

Correlation coefficient is defined as the association between the dependent variable and independent variable. It is a method of determining the relationship between these two variables. If the two variables are so related change in the value of independent variable cause the change in the dependent variable then it is said to have correlation coefficient (Sunity and Silwal: 325).

The most widely used in practice for calculating correlation coefficient between two variables is "Karl Pearson's correlation coefficient." The correlation coefficient between two variables X and Y, usually denoted by r (X, Y) or r_{xy} or simply r, is a numerical measure of linear relationship between them and is defined as

$$r_{12} = \text{Correlation coefficient between } X_1 \text{ and } X_2$$

$$= \frac{n \Sigma X_1 X_2 - \Sigma X_1 \Sigma X_2}{\sqrt{n \Sigma X_1^2 - (\Sigma X_1)^2} \sqrt{n \Sigma X_2^2 - (\Sigma X_2)^2}}$$

Where,

- r = correlation co-efficient
- n = Total no. of year
- X = Dependent Variable
- Y = Independent Variable

The value of r lies between -1 and + 1 symbolically,

$$-1 \leq r \leq +1$$

The correlation coefficient is systematic in two variables, i.e. $r_{xy} = r_{yx}$ (It can be verified by exchanging X and Y in the formula). It is a pure number independent of the unit of measurement.

Interpretation of correlation coefficient

- i. When $r = +1$, there is perfect positive correlation.
- ii. When $r = -1$, there is perfect negative correlation.
- iii. When $r = 0$, there is no correlation.
- iv. When r lies between 0.7 and 0.999 (-0.7 to -0.999) there is a high degree of positive (or negative) correlation.
- v. When r lies between 0.5 and 0.699 (-0.5 to -0.699) there is a moderate degree of positive (or negative) correlation.
- vi. When r is less than 0.5, there is low degree of correlation.

3.6.1.3 Analysis of Variance (ANOVA)

Analysis of Variance often abbreviated ANOVA is a powerful statistical tool for tests of significance to evaluate difference among the parameters of several groups. It is specially designed to test whether the means of more than two quantitative populations are equal. It consists of classifying and cross classifying statistical results and testing whether the means of a specified classification differ significantly. (Azaya B.Sthapit, P R Joshi,Hiranya Gautam & P M Dongol)

There are two types of ANOVA; One way ANOVA and Two ways ANOVA.

In one factor ANOVA only one factor is considered at a time and we may conduct the experiment through a number of sample studies. The main objectives of one way ANOVA is to analyze difference among the group means by considering one factor (one variable). Through an analysis of the variation in the data, both among and within the several groups, we are able to draw conclusions about possible difference in group means.

F-test statistics:

$$F = \frac{S_1^2}{S_2^2} \text{ With d.f is } (n_2-1, n_1-1)$$

Where,

$$S_1^2 = \frac{1}{n_1} \sum_{i=1}^{n_1} x_i^2 - \frac{(\sum_{i=1}^{n_1} x_i)^2}{n_1}$$

$$S_2^2 = \frac{1}{n_2} \sum_{i=1}^{n_2} X_i^2 - \frac{(\sum_{i=1}^{n_2} X_i)^2}{n_2}$$

3.6.2 Financial Tools

“Financial analysis is the process of identifying the financial strength and weakness of the firm by properly establishing relationship between the item of balance sheet and profit & loss account.” (Pandey, 2000: 108) while adopting financial tools, a ratio is used as benchmark for evaluating the financial position and performance of any firm. “Financial analysis is the use of financial statement to analyze a company’s financial position and performance and to assess future financial performance,” (Wild, Subramanyam and Halsey, 2003: 13)

3.6.2.1 Technical (Trend) Analysis

In this analysis the past trend is analyzed of any data and future movement is predicted. Technical analysis presents the past data in the charts and predicts the patterns of future. It shows where the organization is going in that particular matter of analysis. In the technical analysis different charts and picture are used which makes it simple to understand. It is used to analyze the data as well as to present the data. (Francis, 1998: 98)

3.6.2.2 Ratio Analysis

Ratio analysis is the most effective tool of financial analysis. It is the widely used tool in financial analysis. A ratio simply shows the relationship between the two variables or one another. It presents the relative strengths and weakness of any firms or organization and financial performance of the organization. It summaries the financial figurer and make quantitative judgment about the financial performances and positions. The relationship between two accounting figures expressed mathematically is known as financial ratio

(Pandey, 2000:108). To make analysis, we can use various ratios. But only those ratios have been calculated which are related to the subject matter.

a. Net Profit to Loan and Advances = $\frac{Net\ Profit}{Loan\ \&\ Advances} \times 100\%$

b. NPA to Loan and Advances = $\frac{NPA}{Loan\ \&\ Advances} \times 100\%$

It is the percentage of Non Performing Loan and Advances. It shows how much of the total loan and advances are not performing well.

Return on Equity

This ratio assesses the effectiveness of the management with respect to both its operating and financing decisions. (Pradhan, 2004: 59)

c. ROE = $\frac{NetIncome}{CommonEquity} \times 100\%$

Return on total Assets (ROA)

This ratio measures the return on total assets after interest and taxes

d. ROA = $\frac{NetIncome}{TotalAssets} \times 100\%$

These three net Profit Ratio, ROA and ROE are used to check the profitability of the firm. It measures the efficiency and effectiveness of the firm's management.

3.7 Test of Hypothesis

As per objective of the study, following hypothesis are formulated

Hypothesis 1

There is no significant different between the NPA level of commercial banks of Nepal and international Standard of 5%.

Hypothesis 2

There is no significant difference between the NPAs of commercial banks of Nepal.

CHAPTER-IV

DATA PRESENTATION AND ANALYSIS.

4.1 Analysis and presentation of NPA.

In this chapter, efforts have been made to present and analyze the collected data. This is the main part of the research. It is the body of the report. Data collected from various sources were classified and tabulated as requirement of the study and in accordance to the nature of the data. Different statistical and financial tools are used to analyze the data collected under the study. To make easier and clearer to the understanding of the study, data are presented in the table and figures also.

In the category of loan. Pass loan is called performing assets and other i.e. substandard doubtful and loss loan are called Non-Performing Assets.

Data for five fiscal years have been presented starting from 2004/5 to 2008/9 to study and analyze the level of NPA. In this chapter conclusion is drawn regarding position of NPA of sample bank. Various factors contributing for NPA, impact of NPA on profitability and other suggestive measure for the management and mitigation of NPA's. To study about NPA ratio, Analysis, trend Analysis Correlation analysis and opinion survey analysis is done.

4.2 Analysis and Presentation of NPA

An NPA is defined as an asset non-contributing to the income of the bank. NPA Analysis is one of the major aspects of this study that analyzes the level of NPA of Nabil Bank Ltd and Himalayan Bank Ltd. While analyzing the NPA two categories of NPA are analyzed, one is Gross NPA and other is Net NPA.

4.2.1 Analysis of Gross NPA

Gross NPA is the total of those loans and advances which are due for more than 90 days. More specifically they are the sum total of loans and advances categorized as substandard,

doubtful and loss according to NRB directives. Since the NPAs are the part of the bank's assets, they are analyzed with respect to total assets and total loan

Table 4.1

Gross NPA Level of HBL

(Rs in millions)

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Total Assets	27418.16	29460.39	33519.14	36175.53	39320.33			
Total Loan	12424.52	14642.56	16997.99	19497.52	24793.16			
Total NPA	1000.77	1040.29	642.35	477.23	551.31	Mean	S.D	C.V
NPA As% of T.A	3.65	3.53	1.91	1.31	1.40	2.36	1.02	43.22
NPA As% of T.L	7.10	3.77	2.45	2.44	2.22	3.6	1.83	50.83

Source: Annual Report of HimalayaBankLimited

During the study period, Gross NPA with respect to total assets of HBL is ranges from 3.65 to 1.31 with average mean, standard deviation and C.V. of 2.36, 1.02, and 43.22 respectively. These statistical figures impel us to conclude that gross NPA with respect to total assets of Himalayan Bank Limited is in decreasing trend but in 2008/9 slightly increase than 2007/8.

Similarly, gross NPA with respect to total loan of HBL are ranges from 7.10 to 2.22with average mean, S.D. and C.V. of 3.6, 1.83, and 50.83 respectively. These statistical figures impel us to conclude that gross NPA with respect to total loan of Himalayan bank is in decreasing trend during the study period. In conclusion, we found that HBL's average NPA ratio as a % of total loan is 3.60% which is under the criteria of NRB's directives issuing for commercial banks for managing NPA.

Table 4.2

Total Assets, Total Loan and Total NPA of HBL

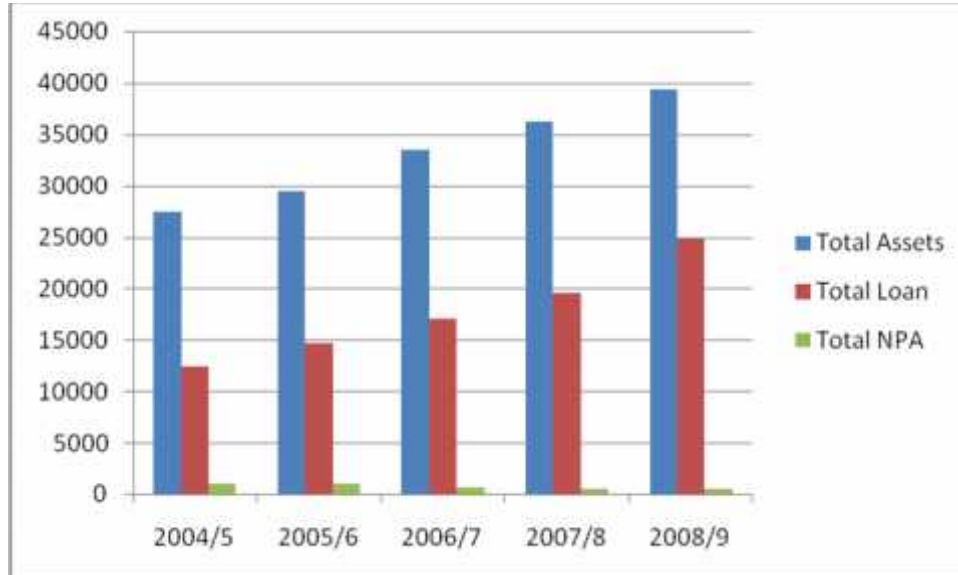
(Rs. in millions)

Fiscal Year	Total Assets	Total Loan	Total NPA
2004/5	27418.16	12424.52	1000.77
2005/6	29460.39	14642.56	1040.29
2006/7	33519.14	16997.99	642.35
2007/8	36175.53	19497.52	477.23
2008/9	39320.33	24793.16	551.31

Source: Annual Report of Himalayan Bank Limited

Figure 4.1

Total Assets, Total Loan, and Total NPA of HBL



From the above table and figure, we depict that total assets of the bank are in increasing trend. Likewise, total loan of the bank also is in increasing trend and non-performing assets of the bank is in fluctuating trend.

Table 4.3**Gross NPA Level of NABIL****(Rs.In million)**

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Total Assets	17186.33	22329.27	27253.39	37132.76	43867.40			
Total Loan	10586.17	13278.78	15903	21365.05	27589.93			
Total NPA	244.50	183.25	178.11	170.40	220.72	Mean	S.D	C.V
NPA As % of T.A	1.42	0.82	0.65	0.45	0.50	0.768	0.351	45.7
NPA As % of T.L	2.31	1.38	1.12	0.79	0.8	1.28	0.56	43.75

Source: Annual Report of NABIL Bank Ltd

During the study period, Gross NPA with respect to total assets of NABIL is ranges from 1.42 to 0.50 with average mean, standard deviation and C.V. of 0.768, 0.351, and 45.7 respectively. These statistical figures impel us to conclude that gross NPA with respect to total assets of Nabil Bank Limited is in decreasing trend but in 2008/9 slightly increase than 2007/8.

Similarly, gross NPA with respect to total loan of NABIL are ranges from 2.31 to 0.79 with average mean, S.D. and C.V. of 1.28, 0.56, and 43.75 respectively. These statistical figures impel us to conclude that gross NPA with respect to total loan of Nabil bank is in decreasing trend during the study period. In conclusion, we found that NABIL"s average NPA ratio as a % of total loan is 1.28 which is under the criteria of NRB"s directives issuing for commercial banks for managing NPA.

Table 4.4

Total Assets, Total Loan and Total NPA of NABIL

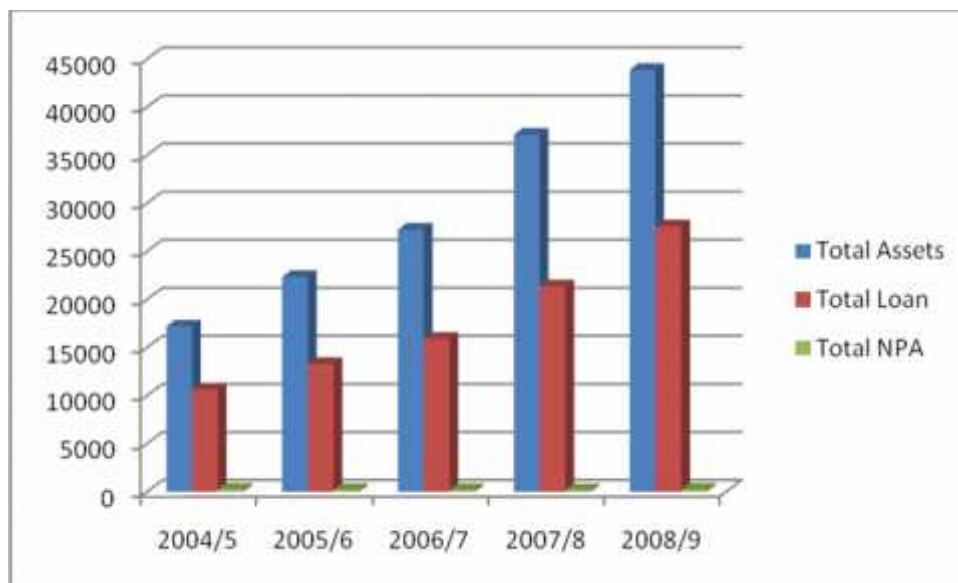
(Rs. in millions)

Fiscal Year	Total Assets	Total Loan	Total NPA
2004/5	17186.33	10586.17	244.50
2005/6	22329.27	13278.78	183.25
2006/7	27253.39	15903	178.11
2007/8	37132.76	21365.05	170.40
2008/9	43867.40	27589.93	220.72

Source: Annual Report of NABIL Bank Ltd

Figure 4.2

Total Assets, Total Loan, and Total NPA of NABIL



From the above table and figure, we depict that total assets of the bank are in increasing trend. Likewise, total loan of the bank also is in increasing trend and non-performing assets of the bank is in fluctuating trend (in 2004/5 to 2007/8 decreasing trend but in 2008/9 slightly increase)

4.2.2 Analysis of Net NPA

Net NPA is the value of loans after subtracting specific provisioning from gross amount of NPA. Net NPA reflects the actual position of bad loan on the total loan portfolio. Net NPA is also analyzed with respect to total assets and total loans.

Table 4.5
Net NPA Level of HBL

(Rs in millions)

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Total Assets	27418.16	29460.39	33519.14	36175.53	39320.33			
Total loan	12424.52	14642.56	16997.99	19497.52	24793.16			
Total NPA	1000.77	1040.29	642.35	477.23	551.31			
Provisioning for NPA	145	90	58	53	59			
Net NPA	855.77	950.29	584.35	424.23	492.31	mean	S.D	C.V
Net NPA as% of T.A	3.12	3.22	1.74	1.17	1.25	2.1	0.89	42.38
Net NPA as% of T.L	6.88	6.49	3.44	2.18	1.98	4.19	2.11	50.36

Source: Annual Report of HBL.

From the above table, it is found that net NPA ratio as percent of total assets of HBL is ranging from 11.25 to 3.12 while expressing net NPA with respect to total loans is ranges from 1.98 to 6.88 during the study period. Average mean, S.D. and C.V. of net NPA with respect to total assets are 2.1, 0.89, and 42.38 respectively. It concludes that during the study period, net NPA ratio as % of total assets is in decreasing trend and net NPA ratio as % of total loans is also in decreasing trend. NPA level of HBL meets the criteria according to NRB's directives.

Table 4.6
Net NPA level of NABIL

(Rs in millions)

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Total Asset	17186.33	22329.27	27253.39	37132.76	43867.40			
Total Loan	10586.17	13278.78	15903	21365.05	27589.93			
Total NPA	244.50	183.25	178.11	170.40	220.72			
Provisioning for NPA	3.77	14.2	64.06	45.72	16.02			
Net NPA	240.73	169.05	114.05	124.68	204.7	Mean	S.D	C.V
Net NPA As% of T.A	1.40	0.76	0.42	0.34	0.47	0.68	0.39	57.35
Net NPA As% of T.L	2.27	1.27	0.72	0.58	0.74	1.12	0.62	55.36

Source: Annual Report of NABIL

Bank

Above table reflects that the net NPA ratio as a percent of total assets ranges from 0.47 to 1.40 and average mean, S.D. and C.V. of Net NPA is 0.68, 0.39 and 57.35 respectively during the study period. While expressing net NPA with respect to total loans it comes within the range of 0.74 to 2.27. Average means, S.D. and C.V. of net NPA with respect to total loan is 1.12, 0.62 and 55.36 respectively. During the study period net NPA ratio of total assets is in decreasing trend except of F/Y 2008/9 and net NPA ratio of total loan is also in decreasing trend except in F/Y 2008/9.

4.2.3 Analysis of NPA with Respect to Loan Loss Provisioning

Loan loss provisioning is a vehicle to adjust in the loss arises from the gone loan. Higher amount of provisioning indicates that the bank is maintaining sufficient cushion for the loss that could be arise in future. Analysis of NPA with respect to provisioning reflects that the position of future loss that could be arising from the further degradation of loan.

Table 4.7**Analysis of NPA with Respect to Loan Loss Provisioning of HBL**
(Rs in millions)**(Rs in**

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Provisioning for Loan Loss	1026.65	1119.39	796.17	682.83	654.92			
Total NPA	1000.77	1040.29	642.35	477.23	551.31	Mean	S.D	C.V
Loan Loss Provisioning as a % of NPA	97.47	92.93	80.68	69.89	84.18	85.03	9.65	11.35

(Source: Annual Report of HBL)

During the study period, amount of loan loss provisioning over the total NPA of HBL is ranging from 69.89 to 97.47. Average Mean, S.D and C.V. of loan loss provisioning to NPA is found that 85.03, 9.65 and 11.35 respectively. This statistical figure impels us to conclude that of total 85.03 of HBL is secured by loan loss provisioning. There is decreasing trend in the growth of Loan loss provisioning with respect to portion of non-performing assets.

Table 4.8**Analysis of NPA with Respect to Loan Loss Provisioning of NABIL.****(In****millions)**

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Provisioning for Loan Loss	360.57	356.24	357.24	394.40	409.07			
Total NPA	244.50	183.25	178.11	170.40	220.72	Mean	S.D	C.V
Loan Loss Provisioning as a % of NPA	67.81	51.44	49.86	43.2	53.95	53.25	8.12	15.25

Source: Annual Report of NABIL Bank

During the study period, amount of loan loss provisioning over the total NPA of NABIL are ranging from 43.2 to 67.81. Average Mean, S.D., C.V. of loan loss provisioning to NPA is found 53.25, 8.12 and 15.25 respectively. These statistical figures impel us to conclude that 53.25% of total NPA of NABIL is secured by loan loss provisioning and there is

increasing trend in the growth of loan loss provisioning with respect to portion of nonperforming assets which they are holding in their portfolio.

4.2.4 Analysis of Net NPA with Respect to Gross NPA.

This is the very important ratio in the analysis of NPA. As net NPA is the amount of loans and advances against which there is no provision maintained. This ratio helps to analyze how much NPA is not protected out of the total NPA by means of provisioning. Higher of this ratio is considered dangerous from the viewpoint of further provisioning in coming future. This is analyzed on the table given below.

Table No. 4.9

Net NPA to Gross NPA Ratio of HBL

(Rs.in million)

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Net NPA	855.77	950.29	584.35	424.23	492.31			
Gross NPA	1000.77	1040.29	642.35	477.23	551.31	Mean	S.D	C.V
Net NPA ratio as % of Gross NPA	85.51	91.35	90.97	88.89	89.30	89.20	2.24	2.51

Source: Annual Report of HBL

From the analysis, part of net NPA out of gross NPA of HBL is ranging from 85.51 to 91.35 during the study period. Average Mean, S.D. and C.V. are 89.20, 2.24 and 2.51 respectively. This statistical figure suggests us to conclude that in average of 89.20% NPA of HBL is not secured by means of provisioning. Net NPA with respect to total NPA are slightly fluctuating during the study period.

Table 4.10**Net NPA to Gross NPA Ratio of NABIL****(In millions)**

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9			
Net NPA	240.33	169.05	114.05	124.68	204.7			
Gross NPA	244.5	183.25	178.11	170.40	220.72	Mean	S.D	C.V
Net NPA Ratio as % of Gross NPA	98.46	92.25	64.03	73.17	92.74	84.13	13.18	15.67

Source: Annual Report of NABIL

Analyzing above table, it is found that of net NPA out of gross NPA of during the study period is ranging from 64.03 to 98.46. Average mean, S.D and C.V of terminology is 84.13, 13.18 and 15.67 respectively. This statistical figure suggests us to conclude that in average 84.13% of NPA of NABIL is not secured by means of provisioning. Net NPA in decreasing trend in 2004/5 to 2007/8 and increasing in 2008/9 during the study period.

4.3 Trend Percentage (Index Number) Analysis.

This analysis is useful to measure the relative change in the value of the variables in any given period is called the "current period" with respect to its value in same fixed period called the " based period". Index number is a tool which is used to study the direction of some particular change in phenomena. To get objectives of research trend percentage analysis of loans, NPA provisioning is done on the following way.

4.3.1 Analysis of Trend Percentage of Total loans.

This analysis is done to find out the direction of growth of loan portfolio. From this analysis, it has tried to find out the growth trend of loan portfolio of sample banks during the period of study. Following table and graph presented below reflects the actual scenario of the subject.

Table 4.11

Trend percentage of Total Loans

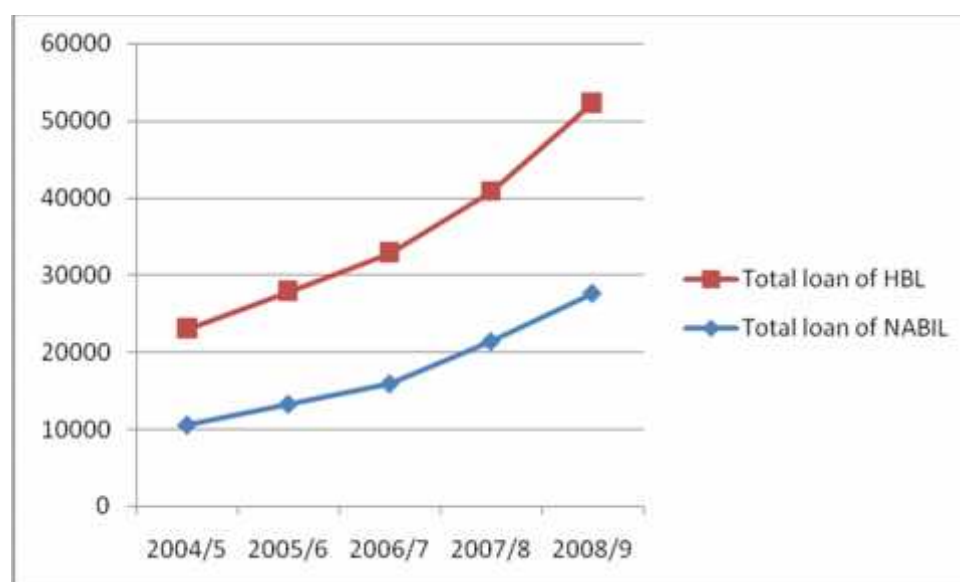
(Rs in millions)

Fiscal Year		2004/5	2005/6	2006/7	2007/8	2008/9
HBL	Total Loans	12424.52	14642.56	16997.99	19497.52	24793.16
	Index Number	100	117.85	136.81	156.93	199.55
NABIL	Total Loans	10586.17	13278.78	15903	21365.05	27589.93
	Index Number	100	125.43	150.22	201.82	260.6

Source: Security Board of Nepal

Figure 4.3

Trend of Total Loans



By analyzing the above table and graph it is found that among the sample banks trend of HBL’s total loan portfolio is increasing and in case of NABIL, it is also in increasing trend . During the study period HBL’s total loan portfolio is increased by 1.99 times and NABIL’s loan portfolio is increased by 2.6 times.

4.3.2 Analysis of Trend Percentage of Non-Performing Assets

This analysis helps to know the growth trend of non-performing assets of banks under study period. This analysis is done basically to know the exact trend of bad loans of Sample banks. Following table and trend figure shows the trend of non-performing loans Of HBL and NABIL during the study period.

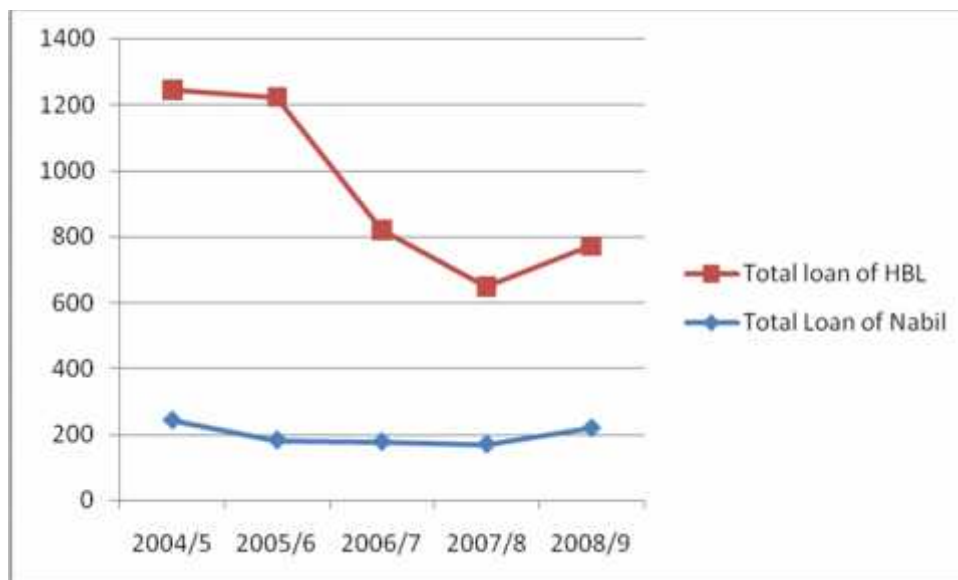
Table 4.12
Trend Percentage of Non-Performing Assets
(Rs: in millions)

Fiscal Year		2004/5	2005/6	2006/7	2007/8	2008/9
HBL	Total NPA	1000.77	1040.29	642.35	477.23	551.31
	Index Number	100	103.95	64.18	47.68	55.09
NABIL	Total NPA	244.50	183.25	178.11	170.40	220.72
	Index Number	100	74.95	72.85	69.69	90.27

Source: Security board of Nepal

Figure 4.4

Trend of Non-Performing Assets



By the analysis of above figure it is found that the trend of NPA fluctuating in 2004/5 to 2005/6 increasing trend then decreasing in 2006/7 to 2007/8 then slightly increase in during the study period. In above table the trend of NPA of NABIL is in decreasing. NPA of NABIL is 0.9 times during the study period.

4.3.3 Analysis of Trend Percentage on Loan Loss Provisioning

In this part of analysis, direction of loan loss provisioning is done to get the idea of position to secure loans and advances. Following table and graph gives the idea of trend of loan loss provisioning on sample banks under study.

Table 4.13

Trend Percentage on Loan Loss Provisioning

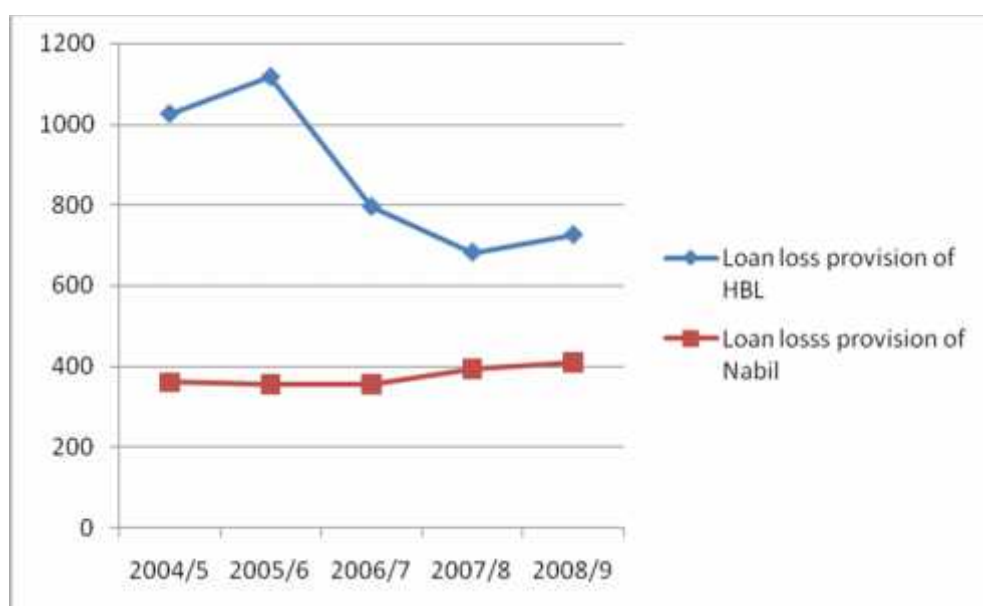
(Rs in millions)

Fiscal Year		2004/5	2005/6	2006/7	2007/8	2008/9
HBL	Loan Loss Provisioning	1027	1119	796	682	726
	Index Number	100	108.95	77.50	66.40	70.69
NABIL	Loan Loss Provisioning	361	356	357	394	410
	Index Number	100	89.61	98.89	109.14	113.57

Source: Security Board of Nepal

Figure 4.5

Trend of Loan Loss Provisioning



In the above figure shows that Loan loss provision of HBL first increase in year 2004/5 to 2005/6 then decrease in 2006/7 to 2007/8 and increase 2008/9. In the case of NABIL first decrease in 2004/5 to 2005/6 then after increase.

4.4 Analysis of Non-Performing Assets and Net Profit

Trend of NPA is compared to evaluate whether the increment ratio of NPA is similar to increment ratio of net profit. With this comparison, it can be found whether the profitability is

affected with the growth of NPA. If the increment ratio of NPA is higher than that of net profit, it can be concluded that significant portion of profit is sacrificed for maintaining required loan loss provisioning and there is reduction on net profit. Likewise, if net profit level is similar even though the NPA level is increased we may conclude that net profit is maintained because banks have been able to boost the profit level and actual profitability is not affected only due to NPA growth.

4.4.1 Analysis of Non-Performing Assets and Net Profit of HBL

Table 4.14

Non-Performing Assets and Net Profit of HBL

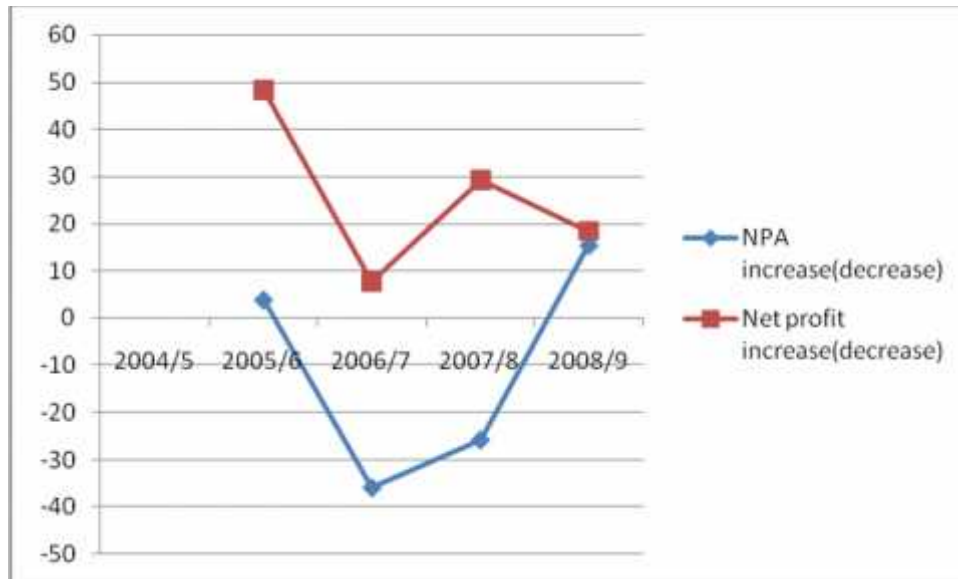
(Rs: in millions)

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9
NPA	1000.77	1040.29	642.35	477.23	551.31
Increase or decrease		3.95	-38.25	-25.70	15.52
Net Profit	308	457	492	636	753
Increase or decrease		48.38	7.66	29.26	18.39

Source: Annual Report of HBL

Figure 4.6

Non-Performing Assets and Net Profit of HBL



From the above table and figure, we found that Non-Performing assets of the bank is in fluctuating trend and Net profit of the bank is in increasing trend every Year and percentage increasing in Net profit is in fluctuating is not constant.

4.4.2 Analysis of Non-Performing Assets and Net profit of NABIL.

Table 4.15

Non-Performing Assets and Net profit of NABIL

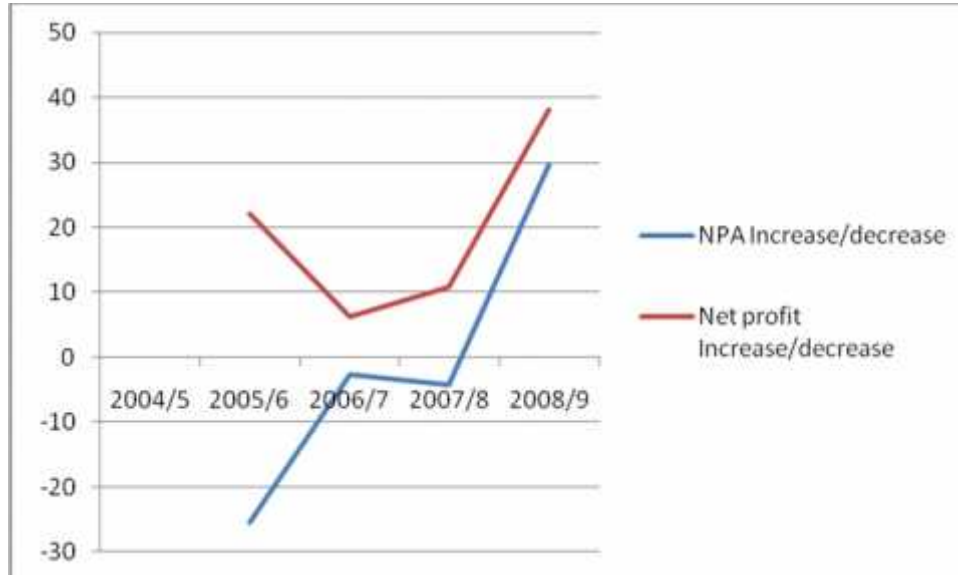
(Rs.inmillions)

Fiscal Year	2004/5	2005/6	2006/7	2007/8	2008/9
NPA	244.50	183.25	178.11	170.40	220.72
Increase(decrease)		-25.05	-2.8	-4.33	29.53
Net profit	520	635	674	746	1031
Increase(decrease)		22.11	6.14	10.68	38.20

Source: Annual Report of NABIL

Figure 4.7

Non-performing Assets and Net profit of NABIL



From the above table and figure, we found that non-performing assets of the bank is in fluctuating trend. Similarly, Net profit of the bank is in increasing trend.

The trend of NPA and Net profit indicates that Net profit depends upon the level of non-performing assets but only non-performing assets is not a cause to increase or decrease of the net profit of the bank.

4.5 Analysis of Correlation Coefficient

Correlation coefficient measures the relation between two or more variables. It also measures the extent to which one variable affects the other one. The correlation coefficient lies between +1 and -1. The +1 coefficient indicates that the variables are perfectly positively correlated and -1 coefficient indicates that variables are perfectly negatively correlated and if the correlation coefficient is 0, it means that the variables are not related to each other.

The negative correlation indicates that the increase in value of one variable leads to decrease in the value of the other variables. The positive correlation indicates that the increase in the value of one variable leads to increase in the value of the other variable also. The number indicates the degree of correlation between the variables. Correlation coefficient of different

dependent and independent variables are tried to analyze to find out the relation of these variables in different years. The statistical tool correlation analysis is preferred in this study to identify relationship between NPA and Net profit, NPA and total loan and NPA and loan loss provisioning to find out whether the relationship is significant or not.

4.5.1 Correlation Coefficient between NPA and Total Loan

As the NPA is the part of loans which is not performing well, it is necessary to analyze the correlation between total loans and NPA"s. Positive correlation indicates that nonperforming assets are simultaneously increases with the increases of loan portfolio. Negative correlation indicates decrease in nonperforming assets even loan portfolio increases and vice versa.

Table 4.16

Correlation Coefficient between NPA and Total Loan of HBL

(Rs: in millions)

Fiscal Year	Total NPA	Total Loan
2004/5	1000.77	12424.52
2005/6	1040.29	14642.56
2006/7	642.35	16997.99
2007/8	477.23	19497.52
2008/9	551.31	24793.16
Correlation(r)	-0.84	

Source: Annex 1

From the above table we can conclude that there is negative relationship between credit expansion and NPA level of HBL. It means that when loan portfolio is increased, NPA level is decreased and vice versa. NPA level seems to decrease with the rise in the volume of total loan.

Table 4.17**Correlation Coefficient between NPA and Total Loan of NABIL**

Fiscal Year	(Rs in million)	
	Total NPA	Total Loan
2004/5	244.5	10586.17
2005/6	183.25	13278.78
2006/7	178.11	15903
2007/8	170.4	21365.05
2008/9	220.72	27589.93
Correlation(r)	- 0.12	

Source: Annex 2.

From the above table, the correlation coefficient is - 0.12 which is negative. It indicates that there is negative relationship between NPA and Total Loan of NABIL. It means that Loan portfolio of the bank increased but NPA level of the bank is decreased and vice versa. NPA level seems to decrease with the rise in the volume of Total Loan.

4.5.2 Correlation Coefficient between NPA and Net profit**Table 4.18****Correlation Coefficient between NPA and Net profit of HBL**

Fiscal Year	(Rs.in millions)	
	Total NPA	Net profit
2004/5	1000.77	308
2005/6	1040.29	457
2006/7	642.35	492
2007/8	477.23	636
2008/9	551.31	753
Correlation (r)	- 0.82	

Source: Annex 3.

Above table depicts that the correlation between NPA and net profit is remained -0.82. It indicates that the NPA and net profit of the bank is negatively related. It means that when NPA level is decreased, net profit of the bank is increased and vice versa. The bank can raise its net profit by decreasing NPA.

Table 4.19

Correlation Coefficient between NPA and Net profit of NABIL

(Rs in millions)

Fiscal Year	Total NPA	Net profit
2004/5	244.50	520
2005/6	183.25	635
2006/7	178.11	674
2007/8	170.40	746
2008/9	220.72	1031
Correlation (r)	- 0.03	

Source: Annex 4

Above table shows that the correlation between NPA and net profit is -0.03. It that the shows NPA and Net profit of the bank is negatively related. It means that when NPA level is increased, net profit of the bank is decreased and vice versa. The bank can raise its net profit by decreasing NPA.

4.5.3 Correlation Coefficient between NPA and Loan Loss Provisioning.

Loan loss provisioning is the vehicle for adjusting the degradation of quality of loan which could arise from the reduction in quality of loan. In general more NPA means amount of operating profit to set aside for loan loss provisioning resulting decrease in portion of Net income. In other aspects, more loan loss provisioning reflects that adequate cushion is maintained to protect the banks from the loss of degradation of their loans. It is found that there is + or - correlation between NPA and Loan loss provisioning under study.

Table 4.20**Correlation Coefficient between NPA and Loan loss provisioning of HBL**

(Rs.in million)		
Fiscal Year	Total NPA	Loan Loss Provisioning
2004/5	1000.77	1027
2005/6	1040.29	1119
2006/7	642.35	796
2007/8	477.23	682
2008/9	551.31	726
Correlation (r)	0.99	

Source: Annex 5

Above table shows that the correlation between NPA and Loan loss provisioning is +0.99. It indicates that the NPA and Loan loss provisioning of the bank is positively related. It means that when NPA level is increased, Loan loss provisioning also increased and vice versa. The bank can raise its Loan loss provisioning by increasing NPA.

Table 4.21**Correlation Coefficient between NPA and Loan loss provisioning of NABIL**

(Rs. in millions)		
Fiscal Year	Total NPA	Loan loss provisioning
2004/5	244.5	361
2005/6	183.25	356
2006/7	178.11	357
2007/8	170.40	394
2008/9	220.72	410
Correlation (r)	0.08	

Source: Annex-6

Above table shows that the correlation between NPA and Loan loss provisioning is + 0.08. It indicates that the NPA and Loan loss provisioning of the bank is positively related. It means that when NPA level is increased, Loan loss provisioning also increased and vice versa.

4.6 Major Finding

In this part major finding of the study are presented on the data and analyzed and presented. Major finding of this study are presented on the following.

4.6.1. Finding of Himalayan Bank Limited.

During the study period, Gross NPA with respect to total assets of HBL is ranges from 3.65 to 1.31 with average mean, standard deviation, and coefficient of variance of 2.36, 1.02 and 42.22 respectively. Similarly Gross NPA with respect to total loan of HBL is ranges from 7.10 to 2.22 with average mean, standard deviation and C.V of 3.6, 1.83, and 50.83 respectively. In conclusion it's found that HBL's average NPA as a % of total loan is 3.60% which is under the criteria of NRB;s directives issuing for commercial banks for managing NPA.

From the analysis of part of Net NPA out of gross NPA of HBL is ranging from 85.51 to 91.35 during the study period. Average mean, S.D and C.V are 89.20, 2.24, and 2.51 respectively. This stastical figure suggests us to conclude that in average 89.20 of NPA of HBL is not secured by means of provisioning Net NPA with respect to total NPA are slightly fluctuating during the study period.

During the study period, amount of loan provisioning over the total NPA of HBL is ranging from 69.89 to 97.47. Average mean, S.D and C.V of loan loss provisioning to NPA is 85.03, 9.65 and 11.35 respectively. This statistical figure us to conclude that 85.03 of total NPA of HBL is secured by loan loss provisioning.

By analyzing the trend percentage of total loan, it is found that among the sample banks of HBL's total loan portfolio is increasing. During the study period HBL's total loan portfolio is increasing by 1.99 times.

While analyzing the trend of NPA of HBL is fluctuating in decreasing trend and its NPA is decreased by 0.47 times during the study period.

From the analysis, it is found that HBL's loan loss provisioning is in decreasing trend during the study period it increases 0.70 times.

From analysis it is found that non-performing assets of the bank is in fluctuating trend and net profit of the bank is increasing trend every year in study period.

From above analysis it is concluded that there is negative relationship between credit expansion, Net profit but positive relation with loan loss provisioning an NPA level of HBL. It means that when loan portfolio is increased, NPA level is decreased and vice versa.

4.6.2 Finding of NABIL Bank Limited

During the study period, Gross NPA with respect to total assets of NABIL is ranges from 1.42 to 0.50 with average mean, standard deviation and C.V of 0.768, 0.351 and 45.7 respectively. Similarly Gross NPA with respect to total loan of NABIL is ranges from 2.31 to 0.79 with average mean, standard deviation and C.V of 1.28, 0.56 and 43.75 respectively. In conclusion it's found that NABIL.

From the analysis of part of Net NPA out of Gross NPA of NABIL is ranges from 64.03 to 98.46 during the study period average mean, standard deviation and C.V are 84.13, 13.18 and 15.67 respectively. This statistical figure suggests us to conclude that in average 84.13 of NPA of NABIL is not secured by means of provisioning. Net NPA in decreasing trend in 2004/5 to 2007/8 and increasing in 2008/9 during the study period.

During the study period, amount of loan loss provisioning over the total NPA of NABIL is ranging from 43.2 to 67.81 and average mean, standard deviation and C.V of loan loss provisioning to NPA is 53.25, 8.12 and 15.25 respectively. This statistical figure us to conclude that 53.25 % of total NPA of NABIL is secured by loan loss provisioning.

By analyzing the trend percentage of total loan, it is found that among the sample banks of NABIL total loan portfolio is increasing. During the study period NABIL total loan portfolio is increasing by 2.60 times.

From the analysis of correlation coefficient there is Negative (-0.12) correlation between total loan and NPA, correlation coefficient between Net profit and NPA also negative (-0.03) and correlation coefficient between loan loss provisioning and NPA of NABIL is positive (+0.08). It indicates that when loan loss portfolio and loan loss provisioning is increased, NPA level of the bank is also increased and vice versa. But there is negative relationship between total loan and NPA, Net profit and NPA. It indicates that means inverse relation. It means when total loan increased NPA decreased and vice versa so that when Net profit increased NPA decreased and vice versa.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

This chapter is the final chapter of the study which consists of the summary, conclusion and recommendation. As mentioned in the objectives of the study this chapter summarizes the problems area with regards to management of NPA and various impacts of NPA.

This study has undertaken to analyze as well as explore the various factors contributing for NPA and their corresponding impacts of sample bank i.e. NABIL Bank Limited and Himalayan Bank Limited. This is done by the studying various figures and factors related to NPAs in term of their impacts on profitability position, their contribution in the growth of NPA and problem area in their effective management. The financial statement of the last five years. Fiscal Year 2004/5 to 2008/9 have been examined for the subject analysis. To analysis the impact of NPAs if the banks

Various financial dated with respect to NPA are sorted, tabulated, interpreted and correlated by using appropriate tools and techniques.

The study has been divided into five chapters; they are Introduction, Review of literature, Research Methodology, Data presentation and Analysis and finally Summary, Conclusion and Recommendation.

In first chapter, Background of the study, profile of selected Bank.(NABIL and HBL), Focus of the study, Statement of the problem, Objectives of the study, Significance of the study and Limitation of the study and plan of the study are highlighted.

In the second chapter, we discuss about Conceptual review of banking, various terminologies related to NPA and review of previous research and study etc. have been defined to facilitate in the analysis part of the study, various NRB directives, NRB Banking and Financial Statistics etc.

In the third chapter, the research methodology which is used to analyze the NPA of sample banks under consideration is briefly explained, this chapter consists of research design, population and sample, types and sources of data, Data collection techniques, Data Analysis tools, Financial tools and types of hypothesis.

In the fourth chapter, the data required for the study are collected from primary as well as secondary data for the purpose of the study are presented, analyzed and interpreted by using various tools and techniques of financial management accounts and statistics to present the result.

In the fifth and final chapter consists of the summary, conclusion, and recommendation of the previous four chapters.

5.2 Conclusion

This part of the study is based on the result which could be derived from the findings of the study. Major conclusion of finding are cited below to not only leads on the way meet the objectives of the study but also gives the idea to manage NPAs of Nepalese banks.

In conclusion it is found that HBLs average NPA ratio at a % of total loan is 3.60 and gross NPA with respect to total loan of HBL is in decreasing trend, average NPA of NABIL is 1.28 which is under the criteria of NRBs directives issuing from commercial banks for managing NPA.

This statistical figure suggests us to conclude that in average 89.20% of NPA of HBL is not secured by means of provisioning. Net NPA with respect to total NPA are slightly fluctuating during the study period and the figure of NABIL suggests to conclude that in average 84.13% of NPA of NABIL is not secured by means of provisioning.

This statistical figure impels us to conclude that 85.03 of total NPA of HBL and 53.25 of total NPA of NABIL secured by loan loss provisioning. During the study period HBLs total loan portfolio is increased by 1.99 times and NABIL s loan portfolio is increased by 2.60 times.

While analyzing the trend percent of non-performing assets, it is found that the trend of NPA of HBL is fluctuating. Its NPA is decreased by 0.55 times and in the case of NABIL it is in fluctuating trend and is 0.90 times during the period.

From the analysis, it is found that HBLs loan loss provisioning is in fluctuating trend and increases 0.70 times more than base year 2004/5 and in the case of NABIL it is also found in fluctuating trend and its loan loss provisioning is 1.135 times.

From the analysis, it is found that non-performing assets of HBL is in fluctuating trend and Net profit of the bank is in increasing trend every year and non-performing assets of the NABIL decreasing trend in 2005/6,2006/7, 2007/8 and then after increasing trend.

From the above analysis it's concluded that there is negative relationship between credit expansion and NPA, negative relationship between Net profit and NPA and positive relation between loan loss provisioning and NPA of HBL and there is negative relation between NPA and total loan, negative relationship between NPA and net profit and positive relation between NPA and loan loss provisioning of NABIL.

5.3 Recommendation

High level of non-performing assets not only decreases the profitability of the Bank but also affects the entire financial as well as operational health of the organization. Based on the major findings of this study; some recommendations have made so as to overcome issues of non-performing assets of the banking sector.

-) NRB should tight the supervision and inspection activity towards the commercial banks so that the accounting manipulation can be avoided and Net profit of the banks is not decrease and NPA level of banks not increase.
-) In the sample banks, NABIL banks has non-performing assets low in comparison with the HBL so to maintain the loan portfolio is important for HBL.
-) Banks should take enough collateral so that banks at least can cover its amount in case of being unable to repay by the borrower

-) Banks should provide necessary training regarding NPA management to the managers and staffs who are involving in managing NPA.
-) Lack of proper financial analysis of the borrower by the banks is one of the major causes behind increasing NPA of Nepalese commercial banks. Therefore proper financial analysis should be performed before giving loan to the borrower.
-) Control mechanism of the bank should be managed properly. Black listed customers should not be given the new loan, as it would lead to the same situation to the bank.
-) Every commercial bank should maintain loan loss provision as per NRBs directives regarding nonperforming assets.
-) The accounting policies must be transparent and must follow best auditing practices.
-) Bad intension, weak monitoring and mismanagement at top level are the major internal reasons turning good loan into bad loan therefore commercial banks should take corrective action immediately.

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Niranjan Shrestha(2007): " **Non-Performing Assets of Commerical Banks of Nepal**" unpublished master Degree Thesis, shanker Dev campus Putalisadak, Kathmandu.

Rajesh Bhandary(2004): "**Analysis of Non-Performing Assets of Commerical Banks of Nepal**" unpublished master Degree Thesis , shanker Dev campus, Putalisadak, Kathmandu.

Related journals and Articals

Naryan Sapkota(2004) Published on 19th may 2004 in Rajdhani National Daily entitled" portion of NPA in Commerical Banks-High in public, Low in Private. Source previous Thesis.

Pradhan 2058 in his article " NPA some suggestions to Tackle them" Source Previous Thesis.

Professor Bishwambher Pyakuryal(2001) " our Economy is in a volatile stage" that the banks have not able to collect their overdue due to the increasing cumulative NPA's in Nepalese Commerical banks.

Online Resources and Websites:

[www.himalayan](http://www.himalayanbank.com.np) bank Ltd

[www.nabil](http://www.nabilbank.com.np) bank Ltd

www.nrb.org.gov.np

www.finance-yahoo.com

www.sebon.com

[www.Nepalstock](http://www.Nepalstockexchange.com) exchange.com

ANNEX-1
Correlation Coefficient between NPA and Total Loan of HBL

(Rs in millions)

X	Y	x=X-X	x ²	y=Y-Y	y ²	xy
1000.77	12424.52	258.38	66760.22	-5246.63	27527126.36	-1355624.26
1040.29	14642.56	297.9	88744.41	-3028.59	9172357.39	-902216.96
642.35	16997.99	-100.03	10006	-673.16	453144.39	-67336.19
477.23	19497.52	-265.16	70309.83	1826.37	3335627.38	-484280.27
551.31	24793.16	-191.08	36511.57	7122.01	50723026.44	-1360873.67
		x=0.00	x ² =272332.03	y=0.00	y ² =91211281.6	xy= - 4170331.35

$$r = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}} = -0.84$$

There is high inverse relationship between NPA and Total Loan of HBL.

ANNEX-2

Correlation Coefficient between NPA and Total Loan of NABIL

(Rs in millions)

X	Y	x=X-X	x ²	y=Y-Y	y ²	xy
244.50	10586.17	45.1	2034.01	-7158.42	51242976.9	-322844.74
183.25	13278.78	-16.15	260.82	-4465.81	19943458.96	72122.83
178.11	15903	-21.29	453.26	-1841.59	3391453.73	39207.45
170.40	21365.05	-29	841	3620.46	13107730.61	-104993.34
220.72	27589.93	21.32	454.54	9845.34	96930719.72	209902.65
		x=0	x ² =4043.63	=0	y ² =184616339.9	xy= -106605.15

$$r = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}} = -0.12$$

There is negative relationship between NPA and Total Loan of NABIL.

ANNEX-3

Correlation Coefficient between NPA and Net profit of HBL

(Rs in millions)

X	Y	x=X-X	x ²	y=Y-Y	y ²	xy
1000.77	308	258.38	66760.22	-221.2	48929.44	-57153.66
1040.29	457	297.9	88744.41	-72.2	5212.84	-21508.38
642.35	492	-100.03	10006	-37.2	1383.84	3721.12
477.23	636	-265.16	70309.83	106.8	11406.24	-28319.09
551.31	753	-191.08	36511.57	223.8	50086.44	-42763.70
		x=0	x ² =272332.03	y=0	y ² =117018.8	xy= - 146023.71

$$r = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}} = -0.82$$

There is inverse relationship between NPA and Net profit

ANNEX-4

Correlation Coefficient between NPA and Net profit of NABIL.

(Rs in millions)

X	Y	x=X-X	x ²	y=Y-Y	y ²	xy
244.50	520	45.1	2034.01	-201.2	40481.44	-9074.12
183.25	635	-16.15	260.82	-86.2	7430.44	1392.13
178.11	674	-21.29	453.26	-47.2	2227.84	1004.89
170.40	746	-29	841	24.8	615.04	-719.2
220.72	1031	21.31	454.54	309.8	95976.04	6601.84
		x=0	x ² =4043.63	y=0	y ² =146730.8	xy= - 794.46

$$r = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}} = -0.03$$

There is inverse relationship between NPA and Net profit of NABIL.

ANNEX-5

Correlation between NPA and loan loss provisioning of HBL

(Rs in millions)

X	Y	x=X-X	x ²	y=Y-Y	y ²	xy
1000.77	1027	258.38	66760.22	157	24649	40565.66
1040.29	1119	297.9	88744.41	249	62001	74177.1
642.35	796	-100.03	10006	-74	5476	7402.22
477.23	682	-265.16	70309.83	-188	35344	49850.08
551.31	726	-191.08	36511.57	-144	20736	27515.52
		x=0	x ² =272332.03	y=0	y ² =148206	xy=199510.58

$$r = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}} = 0.99$$

There is highly positive relationship between NPA and Loan loss provisioning of HBL.

ANNEX-6

Correlation Coefficient between NPA and Loan loss provisioning of NABIL

(Rs in millions)

X	Y	x=X-X	x ²	y=Y-Y	y ²	xy
244.50	361	45.1	2034.1	-14.6	213.16	-658.46
183.25	356	-16.15	260.81	-19.6	384.16	316.54
178.11	357	-21.29	453.26	-18.6	345.96	395.99
170.40	394	-29	841	18.4	338.56	-533.6
220.72	410	21.31	454.54	34.4	1183.36	733.06
		x=0	x ² =4043.63	y=0	y ² =2465.2	xy=253.53

$$r = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}} = 0.08$$

There is positive relationship between NPA and Loan loss provisioning of NABIL.