

**LENDING PRACTICE OF COMMERCIAL BANKS IN
NEPAL**

(A case study with reference to NIC Asia Bank Limited)

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RECOMMENDATION

This is to certify that the thesis

Entitled

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(With reference to NIC Asia Bank Limited)

Submitted by:

Divya Karki

Has been prepared as approved by this department in the prescribed format of Faculty of Management. This thesis is forwarded for examination

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And found the Thesis to be the original work of the student written in accordance with the prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirements for Master Degree of Business Studies (M.B.S.)

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DECLARATION

I hereby declare that the work reported in this thesis entitled “**Lending Practice of Commercial Banks in Nepal (with reference to NIC Asia Bank Ltd.)**” submitted to Office of the Dean, Faculty of Management, Tribhuvan University is my original work done in the form of partial fulfillment of the requirement of Degree of Master of Business Studies (MBS) under supervision and guidance of Associate Prof. **Achyut Bhattarai** of Shanker Dev Campus, TU.

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ABBREVIATION

CBs	Commercial Banks
F.Y.	Fiscal Year
GDP	Gross Domestic Product
LC	Letter of Credit
LLP	Loan Loss Provision
NICABL	NIC Asia Bank Limited
NA	Not Applicable
NG	Nepal Government
NPA	None Performing Assets
NRB	Nepal Rastra Bank
Rs.	Rupees
TRs	Trust Receipts

CHAPTER I

INTRODUCTION

1.1 Background of Study

Banking System and the Financial Institutions play very significant role in the country's economy. First and foremost is in the form of catering to the need of credit for all the sections of society. An efficient banking system must cater to the needs of high end investors by making available high amounts of capital for big projects in the industrial, infrastructure and service sectors. At the same time, the medium and small ventures must also have credit available to them for new investment and expansion of the existing units. Rural sector in a country can grow only if cheaper credit is available to the farmers for their short and medium term needs.

The role of the state is changing, markets are increasingly global and developing nations are undergoing rapid urbanization and industrialization. To grow in the next century, developing countries will need sound, well regulated financial systems that can operate within a challenging climate of change. Banking is basic building block of any country's financial sector. Usually commercial banks and other deposit taking institutions are the first and in some countries only formal vehicle for mobilizing household financial savings. In many countries banks dominant position in mobilizing savings also gives them a lead role in allocating credit. (Barger, 1998:5&16)

Commercial banks are one of the vital aspects of this sector, which deals in the process of channelizing the available resources in the needed sectors. It is the intermediary between the deficit and surplus of financial resources. Bank came into existence mainly with the objectives of collecting the idle funds, mobilizing them into productive sector and causing an overall economic development. The bankers have the responsibility of safeguarding the interest of the depositors, the shareholders and the society that they are serving. Hence Commercial Bank act as catalysts in the economic development of a country. (Popli, 2013:2)

Credit management involves the creation and management of risk assets. The process of lending takes into consideration the people and system required for the evaluation and approval of loan requests, negotiation of terms, documentation, disbursement, administration of outstanding loans and workouts, knowledge of the process and awareness of its strength and weakness are important in setting objectives and goals for lending activities and for allocating available funds to various lending functions such as commercial, installment and mortgage portfolios.

Competitive banking service with its effective credit management is essential for integrated and speedy development of the country and its financial position of the people. In a developing country like Nepal, there is always lack of financial resources not only because of its real absence but because of the available resources not properly mobilized and not fully utilized for the productive purpose; in this course the commercial banks play a vital role. In modern times, commercial banks, which are facilitated, regulated and supervised by the Central bank, confined them and concentrated in their activities of fulfilling the financial needs of their customers. In the present scenario, Nepal banking system is evolving itself as a powerful instrument of planning and economic growth of all the developed and underdeveloped sectors. The scope and scale of banking too have undergone substantial change in response to the saving and credit needs of people.

1.2 An Overview of NIC Asia Bank Limited (NICABL)

a. Introduction

NIC Asia Bank has created history in the annals of Nepalese financial landscape by forming ourselves through a first of its kind merger between two commercial banks operating successfully in the country. The Bank has been formed through the merger of NIC Bank and Bank of Asia Nepal on 30th June 2013.

Whilst one of the merger partners – “Bank of Asia Nepal” was a relatively younger bank established in year 2007, the other partner – NIC Bank was established in year 1998 and has been recognized for many achievements including “**Bank of the Year 2007 – Nepal**” by The Banker, Financial Times, UK.

NIC Asia Bank is one of the largest private sector commercial banks in the country in terms of capital base, balance-sheet size, number of branches, ATM network and customer base. The Bank has 53 branches at present, which will be expanded to 66 branches within July 2014 with the relocation of 13 branches, which were merged together during the merger process. The existing branch network, across Nepal, covers almost all major financial centers of the country. NIC ASIA Bank has received the prestigious „Bank of the Year 2013- Nepal“ award from The Banker -Financial Times Publication, London. The judging panel from The Banker magazine chose NIC ASIA Bank as the winner of Bank of the Year in Nepal.

The Bank strongly believes in meritocracy, transparency, professionalism, team spirit and service excellence. These core values are internalized by all functions within the Bank and are reflected in all action it takes during the course of its business.

b. Capital Structure of NIC Asia Bank Limited:

Capital	Rs.(in million)
Authorized Capital	3,600.00
Issued Capital	2,311.55
Paid up Capital	2,311.55

c. Share Holding Pattern of NIC Asia Bank Limited:

S.N	Sources	Percentage
1	Promoters Group	51%
2	General Public	49%

d. Product and Services Offered by NIC Asia Bank

The products and services that are currently available are given below:

- Deposit Product (Current, Savings, Call and Fixed Deposit A/c)
- Business Banking
- Consumer Banking
- ITouch Internet Banking
- ITouch Mobile Banking

- NIC Asia Visa Debit Card
- NIC Asia SCT Debit Card
- Cash Management Product
- Inward Remittance Business
- Safety Deposit Lockers

1.3 Statement of Problem

The present possibility for banks to diversify into broader range of services and products make life really cool for banking entrepreneurs and managers. But this diversification advantage is a once in a life time opportunity that should be consumed with some caution and prudence as this involves a great deal of risk. Banks use their deposits to generate credit for their borrowers, which in fact is a revenue generating activity for most banks. This credit creation process exposes the banks to high default risk which might led to financial distress including bankruptcy. All the same, beside other services, banks must create credit for their clients to make some money, grow and survive stiff competition at the market place.

The principal concern of this thesis is to ascertain to what extent banks can manage their credit risks, what tools or techniques are at their disposal and to what extent their performance can be augmented by proper credit risk management policies and strategies.

Research problems may be stated in following question:

- What is the deposit collection and utilization trend of the bank?
- What is the relationship between deposit, loans and advances, and income of the bank?
- Whether the credit recovery process of the bank is slow owing to poor credit administration?
- Whether Non-performing credits of the banks are increasing year by year?
- Whether the Writing off the non-performing assets is satisfactory?
- Does the bank has Clear-cut objectives and policy of the credit management?
- Whether the Banks are competing unfairly in the limited area, due to limited investment sectors?

1.4 Objectives of the Study

The ultimate objective of this thesis is to help the case study bank possess a reflection on its own credit management framework. Thus attention is geared:

- To see why and how banking credit risk exposure is evolving recently.
- To see the information procedure in controlling the credit policies and practices of the bank.
- To Review NRB guidelines with regard to credit management of the bank.
- To see the non-performing assets of the bank.

1.5 Focus of the Study

This study confirms the analysis of Credit disbursed and recovery of NIC Asia Bank limited. The present study analytically discloses the strengths and weakness of the commercial banks in relation to credit disbursed and their recovery.

Research Questions to find out the exact answer are:

- What information does the bank need about the customers/borrowers while making the credit appraisal?
- What are the processes involved in it for the approval or disapproval of the project appraisal?
- What sort of informational guidelines should the bank considered while making the credit appraisal?

1.6 Importance of the Study

Despite the vital role that banks play in Financial markets (FM) by connecting lenders to borrowers, instability in these financial markets, currency values and the global environment has affected the profitability of banks. Most if not all companies including banks go into business because they want to create value. The banks like other firms thus look for ways to manage their risks while striving to improve productivity and performance for this value to be created. This productivity only comes when the banks give credits to customers from money deposited by shareholders or savings from customers thus putting them at risk in case of default. Despite this risk, the bank cannot stop the business of credit granting because it is the main source of its profitability. For success to be attained, the only option is good credit risk management practices since in the process, returns are correlated to risk.

It has become imperative for commercial banks to strengthen the credit function due to the increased competition and emergence of new types of risks in the financial sector. Therefore, in the present scenario efficient project appraisal is of great importance as it can check and prevent induction of weak account to the bank's loan portfolio.

The study will assist the loan committed managers in their decision making, as it concerns credit policy and management of credit in form of proper assessment of loan applications, proper supervision of credit and evaluation of project proposals. It will help the management to see the need to employ professional staff. Lastly, the study or findings will be of educational importance to the various universities, students, researchers for further research in the said subject and to all those concerned or exposed towards banking industry to gain an ample knowledge about bank and banking sector.

1.7 Limitation of the Study

Limitations are what impede the perfection of this thesis study. First and foremost, the study mainly focuses on the importance and role of the credit management of NIC Asia Bank Limited. In this study, only selected financial tools and techniques are used. The thesis is limited to only NIC Asia Bank hence findings or outcome of the study may not be generalized with any other banks. The data of last 5 years i.e. FY 2065/66-2069/70 are taken for our purpose so the conclusions are drawn on basis of the period.

Actual research is conducted with respect to NIC bank but during the course of research, another commercial bank "Bank of Asia" was merged with NIC bank limited and hence named as NIC Asia Bank Limited. Therefore the financial data used for analysis purpose for past 4 years 2065/66 to 2068/69 is with respect to NIC Bank only while Data of FY 2069/70 is with respect of NIC Asia Bank Limited

1.8 Organization of the Study

The study has been categorized into 5 chapters each dealing with specific aspects of study which are as follows:

Chapter I: Introduction

This chapter includes the background of the study, brief profile of NIC Asia Bank, statement of problem, objectives, significance, limitation and organization of the study.

Chapter II: Review of Literature

This chapter includes review of former studies made on the topics selected in this paper.

Chapter III: Research Methodology

Methods of data collection, financial tools used in data collection and analysis, population and sample data are described in this chapter.

Chapter IV: Data Presentation and Analysis

In this chapter, data and information are presented and analyzed with the help of different financial and other relevant tools.

Chapter V: Summary, Conclusion and Recommendation

Summary and conclusions of the study and further suggestions have been included in this chapter.

CHAPTER II

REVIEW OF LITERATURE

2.1 Conceptual Framework

2.1.1 Concept of Credit

The word 'credit' is derived from the Latin word 'Credere'. 'Credere' means to have trust or to believe. Thus 'credit' is all about trust. There can be no doubt as to serious nature of credit management when the whole business of granting credit has its root in trust. (Bullivant,2010:19)

Credit is usually defined in terms of the borrowing and lending of money. The most basic form is a loan granted to a borrower, who may be a consumer or a company. Credit can also take the form of a financial instrument that entails fixed payment determined upfront and made over a set time period. 'Credit' the English writer Charles Dickens famously said "is a system whereby a person who can't pay gets another person who can't pay to guarantee that he can pay". The near collapse of the U.S financial system in 2008 under the weight of an enormous and growing pile of bad housing loans suggests that Dickens had a point. Extending Credit to anybody or any business or group entails risk. To be successful and stable, any bank needs to have a clear understanding of the risk it is taking with each loan or extension of credit, evaluate those risks, and manage them as a portfolio. The aim is to take on only as much risk as the financial institution can sustain. (Wiley,2012:4)

Credit is the trust which allows one party to provide resources to another party where that second party does not reimburse the first party immediately but instead arranges either to repay or return those resources at a later date. The resources provided may be financial (e.g. granting a loan), or they may consist of goods or services (e.g. consumer credit). Credit encompasses any form of deferred payment. (www.wikipedia.org)

Credit can be defined as a sum of money granted to a certain person, organization or institution with an expectation to get it back after a certain period of time along with agreed rate of interest. The main functions of the banks are accepting deposit and extending credit. The Bank based

under various conditions and restrictions accepts the deposit from the depositors and extends advances in various forms. Bank usually extend advance against movable and immovable collateral security and personal guarantee. However advance can be both secured and unsecured. (NIC Bank ,Guidelines to Credit and Trade Finance Areas:3)

Two essential functions of Commercial Banks may be best summarized as borrowing and lending of money. They borrow money by taking all kinds of deposits and provides money to those who are in need of it by granting overdrafts or fixed loan or by discounting bills. When bank is lending money, it is actually lending money in the form of deposit credit with the right to borrower to draw cheques against it. (Shekhar,1999: 4)

Lending money is the business of banks. Bank lend to individuals and corporations on the condition that it will be returned after an agreed period, usually with interest and fees. But lending is inherently risky. Repayment of a loan and interest on it depends on the future cash flow of the borrowers and the future cash flow can never be certain. To be successful, banks need to ensure that the risks they take are reasonable and controlled within defined limit. (Wiley,2012:4)

Banks extend credit to different categories of borrowers for different purpose. For most of the borrowers bank credit is the primary and cheapest source of debt financing. Both the demand and supply sides of the economy need bank credit. Consumer of goods and services constitute the demand side of the economy, and they require bank credit to enable them acquire assets such as consumer durables, housing or for plain consumption. On the supply side, the need for credit arises for the corporate and government sectors engaged in manufacturing, trading and services. These sectors require bank credit for capital investment in long term projects and for day to day operations.(Suresh,2010:115)

A lender does 'lend' money and does not give it away. There is a judgment therefore that at some future date repayment will take place. However there will always be some risk that the customer will be unable to repay and it is in assessing this risk that the lender needs to demonstrate both skill and judgment. The lender's objective will be to assess the extent of risk

and to try to reduce the amount of uncertainty that will exist over the prospect of repayment. While there are guidelines to follow, there is not magic formula. The lender must gather together all the relevant information and then apply his or her skills to making a judgment. (Rouse,2002:25)

2.1.2 Types of Credit

Bank extends loan facilities by a way of fund-based facilities and non-fund based facilities. Funded credit facilities refer to providing credit or loan facility by way of actually giving money. Whereas non-funded credit facility refers to providing an undertaking such that there is no immediate cash outflow however cash outflow is affected only on happening or non-happening of certain event which is known as contingent treasury of a bank.

Funded Credit Facilities

➤ **Overdrafts:** An overdraft facility means ability to withdraw money more than what is in the account. The customer may be sanctioned on the basis of certain norms, a certain limit within which, a borrower can overdraw its current account within a stipulated period. Balance of overdraft account may fluctuate. It is increased by withdrawals by the customer and is decreased if the customer deposits amount into the account. The borrower wishing to avail overdraft facility should compulsorily maintain a current account with the bank because advance in the form of overdraft is always allowed on current account and is operated through cheques. The overdraft arrangement enables a customer to draw over and above his own balance upto the extent of sanctioned limit. Overdraft facility is usually allowed for a period of 1 year and is regularly renewed upon satisfactory performance.

➤ **Demand loans:** A demand loan is an advance made in lump sum repayable either on fixed installment or in lump sum basis having no subsequent debit except by way of interest, incidental charges etc. Demand loan is generally granted to business for fixed working capital requirement and is usually secured by current assets, Shares, Debentures, Government Bonds and FD receipt, Life Insurance Policies etc. Demand loan in other words is a working capital allowed for a fixed time usually 1 year and renewed on satisfactory performance. Demand loan once repaid in full or

in part cannot be drawn again by borrower, if the borrower requires further accommodations; it will be treated as separate transaction.

➤ **Term loans:** Term loan is an advance made in lumpsum or phase wise repayable either on fixed installment basis or in lumpsum for fairly long period to industries, agriculture or construction companies over the security of fixed asset. Term loans are expected to be granted by financial institutions on the basis of projected cash flow. Term loans are granted for starting or expanding a new project, industry or any other venture requiring fixed investment .It is provided to meet the party's long term fixed asset requirement.

➤ **Bridge Loan:** Bridge loan is temporary short term finance. The very nature of the bridging loan means that the financial accommodation if required only for a short period to bridge the gap in time between the purchase of an assets/fund requirement for bringing the project and the receipt of fund form elsewhere. Where a party has been sanctioned a term loan form the bank, it will take a considerable time for completion of documentation and comply with all the terms and conditions of the loan before the loan is disbursed. To fill the gap at the guarantee from the lending agency or at separate security arrangement, Bank will finance for the requirement of such party which is known as bridge loan. The banks charge interest rate applicable to cash credit/overdraft advances and obtain documents also similar to those applicable to cash credit/overdraft .Security for bank in such case is the commitment letter of the banks since mortgage charges as per loan would not be forth coming.

➤ **Pledge Loan:** Pledge is bailment of goods given as security. In other words, there is actual and constructive delivery of goods to the banker with the intention of being treated as security. Under this agreement, banks reserve the possession of the goods and the customer can only take out the goods form the godown on exclusive permission of the bank. The customer's account is credited by the full amount of the sanctioned pledge loan amount and at the same time a pledge loan account for the customer for this amount, on the whole of which borrower has to pay interest for the period of the loan. After creation of loan there will be only repayment by the borrower. Pledge loan is generally granted to businessmen or individual for working capital requirement to fulfill their short term needs.

➤ **Hire Purchase:** The purchase of relatively expensive goods has always been difficult for the people who find it here to save up the purchase price in advance and it was to overcome this difficulty that hire purchase loan was introduced. Hire purchase loan is a kind of consumer loan where the loanee makes a partial deposit and the rest of the amount is borne by the bank. This amount is spread over the period of 6 months, 2 years and 3 years or sometime even longer, the article being regarded as the property of the bank until the final payment is made, this items under hire purchase financial can range from vehicles to electric house hold appliances to construction equipment depending upon the merit of each case.

➤ **Margin Lending:** Shares are of two main types: ordinary shares and preference shares. The holding of shares is presented by share documents, which is issued under the official seal of the company, showing ownership of shares in that company. Bank may provide loan against lien of these share certificates of various companies approved by the banks appropriate authority, from time to time on those shares of limited companies listed in the stock exchange or stock broker. (NIC Bank Guidelines to Credit And Trade Finance Areas: 5-17)

➤ **Bills Finance:** Banks purchase inland demand bills, whether clean or documentary, cheques/drafts and make the payment after deducting the commission form the face value of the bill/ cheques. Banks also discount local or inland usance bills or promissory notes, whether clean or documentary with usance not exceeding six months at the time of discounting and make the payment after deducting discount charges for the usance period. This facility includes: Demand Bill Purchase, Usance Bill Discounting, Clean bill (Thrid Party Cheques, Government Cheques, Bank drafts and pay order etc). Government Supply Bills, Advance against Bills in the course of collection.

➤ **Cash Credit:** Cash credit is a drawing account against credit granted by the bank and is operated in exactly the same manner as a current account on which an overdraft has been sanctioned. The principal advantage of a cash credit account is that the borrower permitted to draw on the account within the prescribed limit as and when required, As such they can save interest on the advance by reducing the balances even if temporarily, whenever they are in a position to do so. The cash credit facility can be in following forms: Cash credit against

hypothecation of stocks, Cash credit against hypothecation of book debts, packing credit etc.(Popli,2013:48-49)

Non-Funded Credit Facilities

➤ **Guarantees:** Bank Guarantee is a non-fund based facility which is extended by commercial bank on behalf of their customer in favor of third parties, who will be the beneficiaries of the guarantees. In fact when a bank guarantee is given no credit is extended and bank does not part with any fund, in other words it does not involve extending any fund or money to the borrower, hence it is categorized as Non –funded credit facility. However a banker is only liable at par to the guarantee amount in case of the guarantee is invoked; otherwise the banker is not required to part with any money to the beneficiary. Guarantees are issued to back up performance and payment obligation on the issuer to pay specified documents in the event of default by the principal debtor. Banks and financial institutions are the most common issuers of such instruments.

➤ **Letter of Credit:** Letter of credit is financial instrument issued by a bank at the request of its customer, whereby it undertakes to pay the value of the instrument provided that all terms under the letter of credit have been complied with. Bank provides this service only to the customer who has approved LC facility/limits in place or against adequate cash margin as approved by authorities having appropriate credit approval discretion. Now a days this instrument is widely used as a convenient and confirmed mode of payment in International trade. The LC issuing bank issues the LC on behalf of the applicants (importer) and advises to the beneficiary (the exporters) through their (The Bank's) Correspondent bank (the advising bank) specifying the details of the documents to be presented for payment.

➤ **Trust Receipt (Importers) Loan:** TR Loans are provided to the importers against goods imported under LCs. Despite the importer enjoying a regular facility for TR loans, a separate TR must be obtained each time a TR loan is disbursed. TR loans are disbursed either at the time of D/O issuance or documents payment under sight LCs. TR loan is to be disbursed for usance bills, unless there is an arrangement for providing TRs for a limited period on maturity of usance bills. .(NIC Bank Guidelines to Credit And Trade Finance Areas: 25

2.1.3 Objective of Sound Credit Policy

It is the objective of Credit Policy to:

- Establish a common approach to the identification and quantification of credit risks.
- Establish standard procedures for credit risk management throughout the Bank.
- Provide a perspective on risk concentrations.(NIC Bank Credit Policy Manual: 7)

2.1.4 Lending Consideration

The initial stages of lending consideration are introduction of the customer, the availability of supporting application and other relevant documents from the customer and then processing of credit file. While reviewing the loan application it should include the assessment of the person(s) involved and the appraisal of the company's performance. The analysis should revolve around the below mentioned canons of lending considerations:

➤ **Character:** Before extending credit, the bank must be certain of the borrower's character. How reliable is the borrower's word regarding the details fo the application and the promises made to repay? Is the borrower making overly optimistic claims? (Wiley,2012 : 4) Although some might claim otherwise, it is virtually impossible to assess an individual's character after just one meeting. It is extremely difficult area but a vital one o get right.(Rouse,2002:29)

➤ **Ability:** This aspect relates to the borrower's ability in managing financial affairs and is similar to character as far as personal customers and concerned. An individual borrower's ability to repay can partly be gleaned from the manner with which he or she handles financial affairs. Is there adequate cash flow in present earnings? The bank should examine the borrower's proof of income against his or her bank account records, credit card stalemates and reference from banks and credit agencies. It should watch out for red flags such as personal cheques being dishonored for lack of funds, frequent requests of stop payment on issued cheques , excesses on agreed facilities and loans not being repaid on schedule.

➤ **Margin:** Agreement should be reached at the outset with the borrower in respect of interest margin, commission and other relevant fees. The interest margin will be a reflection of the risk

involved in the lending, while commission and other fees will be determined by the amount and complexity of the work involved.

➤ **Purpose:** Bank should know the customer and the reason for the application. It should lend only for good causes and not for illegal purpose such as smuggling.

➤ **Amount:** Is the customer asking for either too much or too little? There are dangers in both and is important, therefore to establish that the amount requested is correct and that all incidental expenses have been considered. The good borrower will have allowed for contingencies. The amount requested should be in proportion to the customer's own resources and contribution. A reasonable contribution from the borrower shows commitment and a buffer is provided by the customer's stake should problems arise.

➤ **Repayment:** The real risk in lending is to be found in the assessment of the repayment proposals. It is important that the source of repayment is made clear from the outset and the lender must establish the degree of certainty that the promised fund will be received. Where the source of repayment is income/cashflow, the lender will need projections to ensure that there are surplus funds to cover repayment after meeting other commitments.

➤ **Insurance:** ideally the canons of lending should be satisfied irrespective of available security, but security is often considered necessary in case the repayment proposals fail to materialize. It is vital that the provider of security, especially third party security, understands fully the consequences of charging it to the bank. It is equally important that no advance is made until security procedures have been completed, or are at least at a stage where completion can take place without the need to involve the borrower any further.(Rouse,2002:29-31 & Wiley,2012:4))

2.1.5 Principle of Good Lending

The proved principles to be taken into account to extend credit facility by a bank are the following:

➤ **Liquidity:** Liquidity is ability of a bank to satisfy in cash the demand of the depositors. The depositors can at any time demand for withdrawal from their respective account and a bank has

to satisfy the depositors. If the Bank fails to do so, customers may not have faith in it. Liquidity is backbone of any bank. (Popli,2013:10)

➤ **Profitability:** One of the objectives of the bank is to make profit. For this firstly, the bank is required to increase its investment without letting the fund remain idle. Secondly, it should try to invest only on those projects from which it can ensure good and timely interest income. Secured and long-term loan can provide good interest income, but such investment has low liquidity. Thus liquidity and profitability are two opposite factors. Higher liquidity brings less profit while lower liquidity brings high profit. Therefore the Bank should be able to maintain good balance between liquidity and profitability

➤ **Security:** Security is another important principle of lending. No matter how attractive the interest income or rate is there is always the possibility of default if it is not secured. Security means adequate collateral having good value, which can be easily sold off if required at any point of time. Besides, the bank should also look upon the loanee's integrity cash flow and status before sanctioning loan.

➤ **Portfolio Diversification:** The bank should not concentrate only on one sector while extending loan but should try to diversify its investment and lending. It should mobilize its resources on various places, different businesses and different individual and organization so that the bank does not suffer loss if one sector slumps. This shall lessen the bank's risk to a greater extent; Bank should have a prudent spread of its exposure of loans on different sectors to reduce profitability. (NIC Bank ,Guidelines to Credit and Trade Finance Areas: 4)

2.1.6 Project Appraisal

Effectiveness of credit management in the Bank is highlighted by the quality of its loan portfolio. Every bank strives hard to ensure that its credit portfolio is healthy and that non-performing assets are kept at lowest possible level, as both of these factors have direct impact on its profitability. In the present scenario efficient project appraisal has assumed a great importance as it can check and prevent induction of weak accounts to loan portfolio.

The comprehensive and systematic review and study of the project in order to arrive at a decision for project finance is called project appraisal. In other words, the project appraisal is the only method of project finance decision. It provides broad guidance to the bank to form its judgment regarding the future profitability and prospects of the project.

With the help of project appraisal, strength and weakness of the project and the opportunities and threats for its sustainability and profitability is highlighted. It is an exercise done to estimate the future projection based on assumptions. The real security of project finance is represented by the surplus which the project is estimated to yield and the appraisal, the bank ensures that such surplus shall be available not only to meet the loan commitment on time but also to service the risk capital to a reasonable extent. A project is appraised on the basis of following main aspects; Market Aspects, Management Aspect, Technical Aspects and Financial Aspects.. (NIC Bank Guidelines to Credit and Trade Finance Areas: 20)

2.1.7 Credit Risk

Credit risk is the risk of an economic loss from the failure of a counterparty to fulfill its contractual obligations. Its effect is measured by the cost of replacing cash flows if the other party defaults. Credit risk involves the possibility of non-payment either on a future obligation or during transaction. (Jorion,2007:409)

Credit risk is defined as the possibility that a borrower will fail to meet its obligations in accordance with the agreed forms and conditions. Credit risks are not restricted to lenders doing activities only, but included off balance sheet and interbank exposures. The goal of credit risk management is to maximize the bank risk adjusted rate of return by maintaining within acceptable parameters. For most banks, loan is the largest and most obvious resources of credit. However other sources of credit risk exist throughout the activities of bank including in the banking book and in the trading book and also in both on and off balance sheet. Banks are increasingly facing credit risk or counterpart risk in various financing, foreign exchange transaction and guarantee and the settlement of transactions. (Bhandari,2003:108)

2.1.8 Risk Assessment

Without a complete analysis of risks it will not be possible to assess the ability of the counterparty to meet its commitments once facilities are provided. The assessment of the risks will also enable relationship managers to determine the level of reward appropriate to the risk of the exposure. Therefore, facilities will only be provided after a full assessment of the risks associated with the counter parties and facilities proposed has been completed in writing. (NIC Bank Credit Policy Manual: 12)

Risk Assessment will include but need not be limited to analysis of the following:

- Management strengths and weaknesses
- Financial strength, including its ability to repay loans and meet proposed commitments.
- Current and future business prospects.
- The size and structure of the proposed facilities and their fit with customer needs.
- Past performance of facilities
- Environmental risks.
- Revenues / Earnings.
- Projected financials.

2.1.9 Management of Credit Risk

The right credit standard and a good credit culture in which to apply them are essential for the satisfactory management of credit risk. Credit Culture and Credit Standards are discussed below:

i. Credit Culture

Credit Culture can be defined as a bank's attitude to all matters relating to its management of credit risk. If the credit culture is to produce a sound credit risk portfolio it must:

- Fit with the overall business and organization of the bank. The culture must be capable of delivering the service the bank requires to meet the needs of its customers. It can only do this if it is compatible with the overall business strategy of the bank.
- Be championed by top management of the bank. Because the credit culture must be a balance between taking new risks and also limiting the amount of risk, it is bound to run into opposition of various types. Top management is the only source that can ensure that the

culture supports appropriate credit standards. But also commercial enough not to cost the bank good business.

- Cover the type and level of risk the bank is prepared to take and the reward it expects to earn for given levels of risk, both at the individual lending and portfolio level.
- Establish the relative status and authority of the credit risk function in the bank.
- Be robust enough not to be affected by economic conditions. A culture that changes in response to different economic conditions is a weak one.

ii. Credit Standards

Credit standards convert the culture into actions. They must take account, the nature of the bank's business, its structure and the quality and training of staff involved in credit decisions. Credit Standards includes following factors:

- The depth of analysis required and how far this is adapted to the need of the borrower. There is a trade off to be made between a wish to understand all aspects of a proposition and cost.
- How far facilities are to be standardized and how far they are to be tailored to customer's individual needs.
- Structuring facilities to protect the bank which should be done in a way that as far as possible it also benefits the customer.
- Recognizing how far customer's sensibilities are going to be balanced against the bank's need to protect itself against loss.
- The inclusion of a proper degree of monitoring and control. (Rouse, 2002 :19-21)

Banks face a genuine dilemma. If they ignore the market and apply standards rigidly, they will avoid credit losses but lose the good business and market share they need to meet shareholder aspirations. However a strong credit culture can help achieve the right balance. If the bank genuinely understands its customers and has the right sort of relationship with them it can choose when to bend the standards a little and when to adhere to them. (Rouse,2002:22)

2.1.10 Duties and Responsibilities of Credit Officer/Manager

In most of the banks the credit officers may be responsible for cash management, profitability and portfolio growth as well as the following: (Popli,2013:18)

- Accepting and processing applications for credit along with other important papers, information or document required for taking a credit decision.
- Appraisal of complete proposal for financial assistance.
- Evaluation of securities offered.
- Obtaining legal opinion on the properties offered as security.
- Checking credit ratings with credit bureaus and reporting agencies and payment experiences with other suppliers.
- In principle granting or refusing credit or helping senior officers in the process of decision making.
- Compiling and communicating of loan sanctions to the borrowers.
- Documentation and charging of securities.
- Releasing loan only after the post-sanction visits and ensuring end use of funds.
- Keeping the documents alive.
- Setting up repayment Schedules
- Advising customers and clients.
- Handling credit complaints/ Suggestions
- Monitoring and follow-up of advances
- Recovery of Advances

2.2 Review of NRB Directives on Credit Aspects

NRB is the bank of all banks. It regulates, supervises and controls the functions of commercial banks and other financial institutions. Concerned to these activities, NRB has issued various directives to supervise commercial banks. For managing credit NRB has given following directives:

2.2.1 NRB Directive No. 1: Provision Relating to Capital Adequacy

On the basis of risk-weighted assets, the banks shall maintain the prescribed proportion of minimum capital fund as per the following time-table.

Table 2.1
Required Capital Fund on the basis of Risk Weighted Assets

Fiscal Year	Required Capital Fund on the basis of weighted Risk assets (in percentage)	
	Core Capital	Capital Fund
For FY 2065/66	6%	10%
For FY 2066/67	6%	10%
For FY 2067/68	6%	10%
For FY 2068/69	6%	10%
For FY 2069/70	6%	10%

Sources: Unified NRB Directives

While examining capital adequacy of any banks, it can be further classified into core capital and overall capital.

For Core Capital:

$$\text{Capital Adequacy Ratio} = \frac{\text{Core Capital}}{\text{Sum of risk-weighted assets}} \times 100$$

Where, Core Capital= Paid Up Capital+ Share Premium+ Non-Redeemable Preference shares+ General Reserves Fund+ Accumulated Profit and Loss Account . However, where the amount of Goodwill exists, the same shall be deducted for the purpose of calculations of Core Capital.

Sum of risk-weighted assets = Total on-balance sheet risk-weighted assets+ Total off-balance sheet risk-weighted items. The general reserve of EBL has found to be increasing every year. The core capital of EBL is in positive figure and increasing every year compared to Last Fiscal Year due to higher positive amount in retained earning. The reason behind it is that the profit of

the bank in increasing trend. EBL had issued preference shares i.e. Non –Redeemable Preferences shares.

For Overall Capital:

$$\text{Capital Adequacy Ratio} = \frac{(\text{Core Capital} + \text{Supplementary Capital})}{\text{Sum of risk-weighted assets}}$$

Where Supplementary Capital= General Loan Loss provision+ Exchange Equalization Reserve+ Assets Revaluation Reserve+ Hybrid capital Instruments+ Unsecured subordinated Term Debt+ Other Free Reserves not allocated for a specific purpose.

a) General Loan Loss Provision

Under this head, provision made against the pass Loan shall be included and where the banks provide for loan loss provisioning in excess of the proportion as required under the directives of NRB, the whole amount of such additional provision may be included in General Loan Loss Provision under the Supplementary Capital. Similarly, except the priority sector credits, in respect of rescheduling, restructuring or swapping of all other kinds of credits, if such credit falls under Pass loan according to NRB directives, loan loss provisioning has to be provided and such provisioning amount is to be included under General Loan Loss Provisioning.

b) Assets Revaluation Reserve

The amount of Assets Revaluation Reserve can be included for the purpose of calculating Supplementary Capital subject to 2% of the Total Supplementary Capital, inclusive of the amount of this Reserve.

c) Hybrid Capital Instruments

This includes the following instruments that have the characteristics of both debt and equity:

- Unsecured, fully paid up instruments issued by the bank which are subordinated to (priority of payment after) depositors and creditors, and available to absorb losses as well as convertible into ordinary capital.
- Instruments which are non-redeemable at the option of the holder except with the approval of Nepal Rastra Bank.

- Perpetual or long-term preference stock (shares) convertible into common stock if the profit and loss account becomes negative.

d) Unsecured Subordinated Term Debt

Unsecured and subordinated debt instruments (priority of payment after the depositors) issued by bank with a minimum maturity term of over five years and limited life redeemable preference shares. To reflect the diminishing value of these instruments, a discount (amortization) factor of 20 percent during the last five years shall be applied. The issue of these instruments by banks shall not exceed 50 percent of their core capital.

The overall capital fund of any bank is the summation of core capital and supplementary capital held by them.

e) Total Weighted Risk Assets

For the purpose of calculation of capital fund, the risk-weighted assets have been classified into following two components:

i. On- Balance Sheet Risk-Weighted Assets.

For the purpose of calculation Capital Fund, the On-Balance Sheets Assets are divided as follows with assignment of separate risk weightage. Accordingly, for determining the Total Risk-Weightage Assets, the amount as exhibited in the balance sheet assets shall be multiplied by their respective risk-weights and the added together.

Table 2.2
On-Balance Sheet Risk-Weighted Assets

On Balance Sheet Assets	Risk Weightage %
Cash Balance	0
Gold(Tradable)	0
Balance with Nepal Rastra Bank	0
Investment in Govt. Securities	0
Investment in NRB Bonds	0
Fully secured loan against own Fixed Deposit Receipt	0
Fully secured loan against Govt. Securities	0
Balance with Domestic banks and Financial Institutions	20
Fully secured FDR Loan against Fixed Deposit Receipt of Other banks	20
Balance with foreign banks	20
Money at Call	20
Loan against the guarantee of internationally rated*/foreign Banks	20
Other investments with internationally rate*/foreign banks	20
Inter-bank lending	20
Investments in Shares, Debentures and Bonds	100
Other investments	100
Loan, Advances and Bills Purchased/Discounted**	100
Fixed Assets	100
Other net interests amount to be received	100
All Other Assets(except advance income tax payment)	100
Real estate/residential housing loans exceeding the limits	150

Source: Unified NRB Directives

ii. Off-Balance Sheet Risk-Weighted Assets

For the purpose of calculation Capital Fund, the Off-Balance Sheet items are divided as follows with assignments of separate risk weightage. Accordingly, for determining the Total Risk-Weighted off Balance sheet assets, the amount of such transactions shall be multiplied by their respective risk-weights and then added together.

Table 2.3
Off Balance Sheet Risk-Weighted Assets

Particulars of Off-Balance sheet items	Risk Weight age %
Bills Collection	0
Forward Foreign Exchange Contract	10
L/Cs with Maturity of less than 6 months (full value)	20
Guarantees provided against counter guarantee of internationally rated*/foreign banks	20
L/Cs with Maturity of more than 6 months (full value)	50
Bid Bond	50
Performance Bond	50
Advance payment Guarantee	100
Financial Guarantee	100
Other Guarantee	100
Irrevocable Loan Commitment	100
Possible liabilities for income tax	100
All types of possible liabilities including acceptance	100
Unpaid guarantee claims	200

Source: Unified NRB Directives

2.2.2 NRB Directives No. 2: Provisions Relating to Classification of Loans/Advances and Loan Losses

Classification of Loans and Advances

Loans and Advances shall be classified into the following 4 categories:

Pass

Loans and Advances whose principal amount are not past due and past due for a period up to 3 (Three) months shall be included in this category. There are classified and defined as Performing Loans.

Substandard

All loans and advances that are past due for a period of 3 months to 6 months shall be included in this category.

Doubtful

All loans and advances which are past due for a period of 6 months to 1 (one) year shall be included in this category.

Loss

All Loans and advances which are past due for a period of more than 1 (one) year as well as advances which have least possibility of recovery or considered unrecoverable and those having thin possibility of even partial recovery in future shall be included in this category. Loan and Advances falling in the category of Sub-standard, Doubtful and Loss are classified and defined as Non-Performing Loan.

Classification in respect of term loan

In respect of term loans, the classification is made against the entire loan on the basis of the past due period of overdue installment of principal/interest.

Classification in respect of reschedule and restructured loan

The term reschedule means process of extending repayment period/time of credit taken by the borrower. The term restructured means process of changing the nature or conditions of loan/facility, adding or deleting of conditions and change in time limit.

Written plan of action from the borrower should be taken while making reschedule/restructure of the loan. Further at least 25% of accrued interest outstanding on date of restructuring or rescheduling should be collected.

Loan Loss Provisioning

The Loan Loss provisioning on the basis of the outstanding loans and advances and bills purchases classified as per NRB Directives shall be provided as follows:

<u>Classification of Loan</u>	<u>Loan Loss provision</u>
Pass	1 Percent
Substandard	25 Percent
Doubtful	50 Percent
Loss/ the loan extended to Black listed person, Firms, Company or corporate body	100 Percent

Note:- Loan loss provision set aside for Performing loans is defined as “General Loan Loss Provision” and Loan loss Provision set aside for Non-performing loan is defined “Specific Loan Loss Provision”.

Provisions on restructured or rescheduled loans are made as follows:

- A minimum of 12.5% provision is to be made on rescheduled or restructured loans.
- In respect of rescheduling or restructuring of deprived sector loan and guaranteed or insured priority loan, the requisite provisioning is 25%.
- Where the installment of principal and interest of restructured or rescheduled loan is serviced regularly for two consecutive years, such loan can be converted into Pass Loan.

Additional Provisions Relating to Loss Loans

In case there seems any of the following discrepancies in any of the following loans, whether or not the deadline for repayment of which is expired, such loans and advances has to be categorized as the loss loan:

- The market price of the collateral cannot secure the loans;
- The debtor is bankrupt or has been declared to be bankrupt;
- The debtor disappears or is not identified;
- In case non-fund based facilities such as purchased or discounted bills and L/C and guarantee which have been converted into fund-based loan, are not recovered within ninety days from the date of their conversion into loan;
- Loan is misused;
- Expiry of six months of the date of auction process after the loan could not be recovered or a case is pending at a court under the recovery process;
- Providing loan to a debtor who has been enlisted in the black-list of Credit Information Bureau Ltd;
- The Project/business is not in a condition to be operated or project or business is not in operation
- The credit card loan is not written off within 90 days from the date of expiry of the deadline;
- While converting the L/C, guarantee and other possible liabilities into a fund based loan under the regular process, if the said loan is not recovered within 90 days; and
- In case of expiry of the deadline of a trust-receipt loan.

2.2.3 NRB Directive No. 3: Provisions Relating to Single Borrower and Limitation of the Sectorial Credit and Facilities

Existing Proviso and Time Frame to meet new Regulation

- Upto FY 2066/67 Single Obligor Limit(SOL) : 25% of core capital for Funded exposure & 50% of core capital for cumulative maximum (Funded and Non Funded) Exposure.
- From FY 67/68 onwards SOL: 25% of core capital for cumulative maximum (Funded and Non Funded) Exposure. Export and Agriculture Sectors, Tourism and other Manufacturing Industries 30% of core capital. For Hydro, Transmission line & Cable car 50% of core capital

Exemption in Limit of Credit and Facilities

- Credits and facilities extended against own fixed deposit receipts, Government of Nepal securities, Nepal Rastra Bank Bonds as well as against unconditional guarantees issued by the World Bank, Asian Development Bank, and International Finance Corporation including international multilateral financial institutions in which Nepal is a member and internationally rated banks.
- Further, on request of the concerned bank and financial institutions, this Bank may allow Zero Risk Weightage on loan extended by the bank and financial institution against the unconditional guarantees issued by such international multilateral financial institutions for the purpose of calculating the capital adequacy ratio together with continuation of the arrangements as provided in Directives issued by this Bank.
- Loan/advances and facilities provide by the "A" Class licensed institutions to the following institutions:-
 1. Nepal Oil Corporation
 2. Nepal Food Corporation

Definition of Group Related Borrowers

- Where a company holds 25 percent or more shares in another company, then both of such companies.
- Where a person, firm, Directors of a company, shareholders of a private company, partners of partnership firm, proprietor and spouse, son, daughter, adopted son, adopted daughter, parents, step mother and brothers and sister who have to be supported by such Director, shareholders, partner, proprietor are residing jointly in the same house or separately.
- Those companies in which the persons referred to in Sub-clause (b) above holds 25 percent or more shares individually or jointly.
- Even if the Director, shareholder or other relatives referred to in Sub-Clause (b) hold less than 25 percent shares of another company jointly or individually, even then if the management of that other company is controlled by them in the following ways, then such companies:-
 - (1) By being a Chairperson of the Board of Directors;
 - (2) By being the Chief Executive of the Company;

(3) By appointing more than 25 percent of the Directors;

- Firms, companies stated to be associated as a group, or members of such group, or
- Where one borrower or company referred to in Sub-clause (b) has provided a guarantee to another borrower or company, then such companies;
- If credit is provided to more than one person against the same collateral, all of such persons;
- If a personal guarantee has been given to each other, all of such person.

Details of Inter-related Customers to be furnished

The licensed institution shall prepare the records of the single borrower and related customers on half-yearly basis and submit to the Bank and Financial Institutions Regulation Department and the concerned Supervision Department of this Bank.

Treatment as Separate Group

Any corporate body or company having full or more than 50 percent ownership of Government of Nepal shall be treated as a separate group.

2.2.4 NRB Directive No. 7: Provisions Relating to Timeframe for Implementation of Regulatory Directives

This Directive deals with timeframe for implementation of regulator directives. This includes timeframe of reply for On Site Inspection Report, Loan Loss Provisioning, Loan Portfolio Improvement Program, Capital Adequacy, Management of Assets and Liabilities, Internal Audit and Control, Implementation of Plans, Policies and Procedures and Quarterly Progress Report, For Effective Credit Management, Bank should reply for On Site Inspection Report within 30 days, Loan Loss Provisioning immediately on receipt of the instruction from NRB and loan Portfolio Improvement program within 30 days.

2.2.5 NRB Directive No. 12: Relating to Credit Information and Blacklisting

Credit Information Center has been established under Companies Act.

Returns to be filed with the Bureau relating to Borrowers (Customers)

Licensed institution shall furnish to the Bureau the following loan details within fifteen days of the completion of every month:

- Credit facilities of 2.5 million rupees and above it have approved.
- Credit facilities of one million or more rupees and below 2.5 million rupees that is overdue.

Obtaining details of the Customers

The following details of the borrower customer shall be obtained prior to providing/approving loan/facilities of Rs. 1 million or above by a licensed institution to any individual, firm, company or corporate body.

- In the case of individual borrower and guarantor, a copy of citizenship certificate, permanent and temporary addresses, particulars of three generations and details of undivided family members.
- In the case of proprietorship partnership firms, particulars of the Proprietors as referred to in clause (a) above and name, surname and address of the individual authorized to carry on business on behalf of the firm and copy of the partnership deed or decision relating there to.
- In the case of private company, particulars as referred to in clause (a) above of Directors and shareholders holding 15 percent or more shares of the company and name, surname and address of the individual authorized to carry on business on behalf of the company and resolution to that effect.
- In the case of public company, particulars as referred to in clause (a) above of Directors and shareholders holding 15 percent or more shares and name, surname and address of the individual authorized to carry on business on behalf of the company and resolution to that effect.
- Name, surname and address of collateral valuator.

Mandatory requirement of acquiring credit information

- Prior to extension or renewal, restructuring or rescheduling of loans of Rs. One Million or more, a licensed institution shall have to obtain credit information about the borrower/customer from the Bureau. In case of request for credit information, the Bureau shall furnish such information not exceeding working days.

- Where the information from the Bureau as above is received in course of extension of credit/facilities to any customer/ borrower, information from other agencies shall not be necessarily.
- For the credit information received from the Bureau under this clause, the licensed institution shall pay fee to the Bureau as prescribed by the Bureau.
- The Bureau shall have to update the details received from the concerned licensed institution for the purpose of enlisting in or delisting from blacklist within three working days.

Procedures for Blacklisting

- The concerned licensed institution may recommend the Credit Information Bureau Ltd. to blacklist the debtors who have availed the credit, advances and facilities of whatsoever amount from that licensed institution but have not repaid that amount. The Credit Information Bureau Ltd. shall, within fifteen days, ascertain the name list recommended from the concerned licensed institution for blacklisting and put them in the blacklist.
- The concerned bank may recommend the Credit Information Bureau Ltd. to blacklist the customers who have utilized the credit card facility to be provided by licensed banks but have not repaid any amount/credit for using the card. Once the recommendation to blacklist is received from the concerned bank, the name list shall be blacklisted within fifteen days and the procedures for delisting from the blacklist shall be according to the prevailing policy and procedural provisions.
- Licensed institution shall have to make recommendation for blacklisting the loan of any amount whatsoever only after getting a loan of more than 2.5 million rupees blacklisted first under the clauses relating to blacklisting.
- If the licensed bank and financial institution recommends, the Credit Information Bureau Ltd. shall have to blacklist the customer of any amount of loan.

Prohibition to Extend Credit by Licensed Institutions to Blacklisted Borrowers

A licensed institution shall not extend new loans/facilities, give additional loan/facilities, renew loan/facilities or release of balance of installment in case of installment credit to or accept guarantees of the individual, firm, company or corporate body included in black list according to their Directives.

2.3 Review of Relevant Articles and Journals

In this section, effort has been made to examine and review of some related articles and journals published in different economic journals, which among the various reviews of various journals pertaining to the study ,the major and mostly contributing to the study has been outlined below:

Koirala (2006), in his well read article, "*Credit Culture of Commercial Banks in Nepal*", has concluded that the unorganized moneylenders in Nepal never loose. They used to assess the record of accomplishment of potential borrowers and innocent characters termed as the best borrower. The bank, on the other hand, is an institution established to support and improves development process of a nation. The politicians and the staff have been responsible for the existence of huge volume of NPA in state-owned commercial banks. In order to improve the situation, there is a need to evolve a more acceptable working system backed by cooperation and realization by the banks employees as well as the politicians and stakeholders, who can influence in banks operation.

Zerith (2008), in her article well read article, "*Loan Portfolio Management*", affirmed that to manage the loan portfolios, bankers must understand not only the risk posed by each credit but also how the risks of individual loans and portfolios are interrelated. These interrelationships can multiply risk many times beyond what it would be if the risks were not related. Until recently, few banks used modern portfolio management concepts to control credit risk. Now, many banks view the loan portfolio in its segments and as a whole and consider the relationships among portfolio segments as well as among loans. These practices provide management with a more complete picture of the bank's credit risk profile and with more tools to analyze and control the risk.

Pandey (2011), in her read article, "Risk Management in Banks and Financial Institutions (BFIs)- A challenge" has concluded that , recent failures of financial systems have forced all the financial players to realize the truth that risk management is actually a a crucial element. Central Bank Financial institutions and government should now be proactive rather than reactive and experimental. Boom and financial slow down are part of business cycle which tend to repeat in years. However, the most important thing is to be ready and prepared for the possible problem.

Risk management is the only one solution to do this. Timely review and inspection of Nepal Rastra Bank, self management of the risks by the bank management itself are felt desperately.

2.4 Review of Dissertations

Thapa R. (2005) The thesis *entitled "Lending policy of Commercial Banks in Nepal"* was intended to study the lending practices in NIBL and SBI.

Major Objectives of the study were:

- To examine the liquidity and assets management of NIBL and SBI.
- To evaluate the investment policy of NIBL and SBI.
- To study the growth ratio of Loans and Advances.
- To analyses the investment, total deposit and net profit of NIBL and SBI.

Major Findings of the Study were:

- Both bank's current assets have exceeded the current liabilities therefore the ratios is considered satisfactory. But the cash reserve ratio has fluctuated in high degree.
- NIBL has maintained both current ratio and cash reserve ratio better than that of SBI.
- The assets management ratio shows that deposit utilization of NIBL is less effective than SBI.
- NIBL has invested lower amount of government securities and share & debenture than that of NIBL.
- The growth ratio of total deposit, loan and advances, investment and net profit of NIBL are less than that of SBI.

Gautam (2007) Thesis entitled, *"Lending Practice: A study on NABIL Bank Limited, Standard Chartered Bank Nepal Ltd and Himalayan Bank Limited."* has find out that the measurement of lending strength in relative term has revealed that the total liability to total assets of SCBNL has the highest ratio. However, the performance of other two banks has not deviated far from the mean ratio of SCBNL and the combined average. SCBNL tendency to investment in government securities have resulted with the lowest ratio of loan and advances to total assets ratio. The steady and high volume of loans and advances throughout the years has been observed.

Major Objectives of the study were:

- To analyze the different sectors of Deposit of Sample Banks.
- To find out the relations between deposit and investment of the commercial banks.

Major Findings of the Study are:

- The market is highly sensitive toward the interest rate and SCBNL has generally been offering low interest rate as compared to other banks.
- The analysis of lending strength of HBL in loan and advance is the best.

Shrestha B. (2008) Thesis entitled “*Effective Implementation of Credit Policy in Nepalese Commercial Banks*” had following objectives and findings:

Major Objectives of the Study were:

- To study the relationship between deposits and lending.
- To study the classification, provision of loans and advances and its effect in profitability.
- To examine the sector wise and security wise lending
- To identify and analyze the problems and prospects of lending practice of Nepalese Commercial Banks.

Major Findings of the Study were:

- The flow of lending depends upon the availability of low cost deposit in the market.
- Consumer financing and loan to manufacturing units are more secured than other sectors.
- First preference of banks for security to loan is fixed assets collateral followed by Government Bonds.
- Lengthy procedure in loan processing and tedious legal procedures is the key factor affecting growth of lending.
- Lack in follow ups and irregular site visits lead to generation of NPA.

Dahal P. (2009) “*Credit Management of Nepal Credit and Commerce Bank Limited*” was a study carried to know of effective credit policy in commercial bank and the efforts used to manage them.

Major Objectives of the Study were:

- To analyze the lending process of commercial banks.
- To analyze the deposit utilization toward lending.
- To assess the impact of credit policy on liquidity
- To assess the non-performing assets and loan loss provision.
- To give suggestion for appropriate credit management.

Major Findings of the Study were:

- The Bank is developing limit for the aggregate volume of outstanding loans as well as for total commitments,
- Financial performances standards are usually based on the purpose and types of loan which has resulted to achieve better performances.
- Credit policy of the bank establishes guidelines on the percentage of total loans that can be allocated to particular category. Hence focus has been made on such distribution of loan.

Acharya L.(2010) The thesis entitled “*Lending Policy of Commercial Banks in Nepal, A comparative study of EBL,NABIL & LBL*” is a study aimed at analyzing the lending policy of those banks under study.

Major Objectives of the Study were:

- To analyze status of non-performing loans of EBL, NABIL and LBL.
- To analyze the portfolio behavior of lending of banks under study.
- To measure the commercial bank’s lending strength.
- To measure the lending performance quality and efficiency.
- To identify major weakness of lending policy of these commercial banks.

Major Findings of the Study were:

- EBL and LBL are able to mobilize their deposit in right way as a result being able to earn more profit from their loans and advances as compared to NABIL.
- Banks having lowest credit risk indicates bad performance of the bank in terms of efficient utilization of their total asset as loans and advances.

- NABIL and EBL are able to manage their loan loss provision as less than 1% while LBL was having difficulty managing the same.
- All banks under study have positive relationship between total deposit and loan & advances.

Regmi P. (2010) *"A Comparative Study of the Financial Performance of Himalayan Bank Ltd and Nepal Bangladesh Bank Ltd"* has following objective and findings:

Major Objectives of the Study were:

- To acknowledge financial status of those banks.
- To compare their position so that their rank could be identified.

Major Findings of the Study are:

- Both banks were able to utilize its capital efficiently in productive sectors.
- Non-Performing asset of NBBL found higher than HBL.
- Profitability ratios of NBBL were not satisfactory in comparison to HBL.

Aryal K. (2011) *"An Evaluation of Credit Investment and Recovery of Financial Public Enterprises in Nepal"*, has following objectives and findings.

Major Objectives of the Study were:

- To analyze the credit disbursement pattern of ADB/N.
- To analyze the recovery pattern of ADB/N.

Major Findings of the Study were:

- Actual credit disbursement, collection and outstanding are increasing in decreasing rate.
- Yearly increase in credit disbursement is higher than that of collection.
- Positive relation between credit disbursement and collection i.e. 0.996.
- Targeted credit collection and disbursement fixed by planning and project department is not significantly different than the actual.
- Most of the customers are unaware of the policy of the bank.

Pradhan M. (2012) Thesis entitled “*A Study on Lending Practices of Joint Venture Commercial Banks*”, has attempted to analyze and evaluate the lending practices of Himalayan Bank Limited, SBI Bank Limited and Everest Bank Limited.

Major Objectives of the Study were:

- To measure the lending performance in quality, efficiency and its contribution in profitability.
- To analyze the lending practices of HBL, SBI and EBL.
- To measure the bank’s lending strength. The lending strength shall be measured in absolute terms also to analyze the volume of contribution made by each commercial bank under study.
- To study the loans and advances, profitability, deposits positions fo the joint venture banks.

Major Findings of the Study were:

The total asset to total liability ratio remained almost constant in the study period of all the three banks.

- Loans and advances to total assets ratio has been fluctuating in the study period of EBL, SBI and HBL banks.
- Non-performing loans out of the total loan and advances is highest in case of HBL. EBL and SBI have lower non-performing loan than HBL.
- The ratios conclude that SBI and HBL are successful in granting high volume of credit as much as the capital fund allows it than EBL.

Bhusal R. (2013) Thesis entitled “*Comparative Study on Credit Management of Nepal Investment Bank Limited and Himalayan Bank Limited*”, has attempted to analyze the credit management adopted by the sample bank with a view to provide workable suggestion which may be helpful to the formulation of credit policy.

Major Objectives of the Study were:

- To see the effectiveness of credit practices of the Commercial Banks. .
- To study the position and utilization of deposit, lending efficiency and its contribution to total profitability of banks under study.

- To see the recovery status of the credit disbursed.
- To provide suggestions and recommendations for the proper credit system

Major Findings of the Study were:

- Both banks aim to maximize the wealth of shareholders, to provide modern services to its customers, to help the monetary policy taken by the central bank NRB' and ultimately to help to reduce the poverty of the country.
- Performing assets to total assets ratio of both banks is Fluctuating regularly in the research period. It shows that there is no consistency in the level of performing assets on total assets over the research period. Correlation of coefficient is highly positive for NIBL and HBL bank. It suggests that the increasing in total assets leads in increase in performing assets. The performing assets ratio suggests that banks should be more conscious to decrease the amount of non-performing assets. Credit and advances should be invested in more secured and the recovery process should be more effective.
- Provision for credit and losses also indicate that the non-performing credits are increasing. In another words, the recovery of the credit is not satisfactory.
- Banks have invested huge money in granting credit and advances but the recovery process of the banks is slow. Efficiency in the management of credit is not satisfactory.

Kunwar T.R. (2013) Thesis entitled "*Credit Management: A Comparative Himalayan Bank Limited and NABIL Bank Limited*", aims to find out credit management position of HBL and NABIL.

Major Objectives of the Study were:

- To compare the volume of loans and advances of selected banks with aggregate loan and advances of banking industry.
- To see the deposit collection and utilization trend of sample banks.
- To see the relationship of deposit collection and utilization trend of sample banks.
- To see the relationship of deposit, loan and advances and net profit of sample bank.

Major Findings of the Study were:

- Performing assets to total assets ratio of both banks is Fluctuating regularly in the research period. It shows that there is no consistency in the level of performing assets on total assets over the research period.
- Provision for credit and losses also indicate that the non-performing credits are increasing. In another words, the recovery of the credit is not satisfactory.
- Banks have invested huge money in granting credit and advances but the recovery process of the banks is slow. Efficiency in the management of credit is not satisfactory.

2.5 Research Gap

There has to be continuity in research. This continuity in research is ensured by linking the present study with the past research studies. Here, it is clear that the new research cannot be found on the exact topic. Therefore to fulfill this gap, this research is selected. The purpose of this research is to develop some expertise in one's area , to see what new contribution can be made to receive some ideas, knowledge and suggestions in relation to lending practices of commercial bank. All the research studies mentioned herein are concerned with the study of credit strength and contribution in regard with capital capacity. Most of them have indicated the credit risk management. In this research some financial tools are used for calculation of lending policy of financial institutions. Besides this, factors mentioned below have been studied analytically and intensively by this research.

- Measuring the credit strength and efficiency,
- Analyzing the contribution of credit in total profitability and study of the loan and advances, profitability.
- Testing the compliance of NRB directives on credit aspects.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Introduction

Having stated the conceptual aspects and reviewing of literature in the previous chapter, now the task has come to make decisive choice of research methods to support the study in realistic term with sound empirical analysis. Research methodology refers to the various sequential steps to be adopted by a researcher in studying a problem with certain objectives in view. It is a way to solve the research problem systematically & scientifically. The scope of Research methodology is much wider than research methods i.e. research method constitutes a part of research methodology. It considers the logic behind the use of the methods in the context of research study & explains why a particular method or techniques is used.(Kothari,2003:10-11) Thus research methodology is concerned not only about the different types of methods used but also about various other facts like what data have been collected, what are the purpose & problem of research etc. Research oriented task ask for serious consideration on research design; sample size; sources of data; data collecting instruments and procedure; data tabulation; data analyzing techniques to be adopted and study limitation in term of tools unavailable. Hence this chapter will deals with the research methodology used in the analysis of the lending practice of NIC Asia Bank Limited.

3.2 Research Design

Research design is necessary to fulfill the objectives of well-set research. Research design may be defined as conceptual structure within which the research is conducted. It constitute blueprint for collection, measurement and analysis of data. (Kothari,2003:39)

The basic objective of the study is to examine the existing policies and practices of credit management of NIC Asia Bank Limited, its role, its effectiveness in decision making and to provide suggestion for better information system. According to the type of the research design, this thesis falls under **descriptive and analytical design**. It lies under analytical design as it tries to analyze the financial data to reach at conclusion. At the same time, it also represents

descriptive research design as it describes much more about the efficiency of the understudied bank. The research will mainly base on the data and information provided by the bank. On the basis of qualitative and quantitative information the analytical framework will be drawn. After the evaluation of this information the interpretation will be presented as an outcome and based on the finding of the study conclusion and recommendation has been given.

3.3 Population and Sample

Population or universe refers to the industries of the same-nature of its service & product. It is an aggregate of objects or the set of results of an operation. On the other hand sample means the representative parts of population selected from it with the objectives of investigating its properties. Thus, a sample is just a portion of the population selected with a view to draw conclusions about the population under study.

Sampling technique is very much essential for conducting any research. It allows the researcher more time to make an intensive study of the research problem. When the study of whole population is not possible, the sampling technique is adopted. The ideal sampling represents the whole universe accurately and independently. For the study purpose too, sampling is done while extracting data required. The study of financial data of some banks from very beginning period makes the study lengthy and vague. Thus, the financial data of recent 5 years are taken as sampling for the study.

In the context of Nepal there are 31 commercial banks in operation. Among them, NIC Asia Bank Limited has been selected for the present study. Similarly, financial statements of NICABL for 5 years i.e. FY 2065/66 to 2069/70 have been taken as samples for this purpose.

3.4 Sources of Data

The sources of the information required for any study will be either primary or secondary data. The data possessing original character and collected from actual field by the researcher or through agent for the first time is known as primary data. The data are utilized when secondary data are not accessible easily. The data compiled by previous researchers for their purpose is known as secondary data. The use of secondary data reduces the considerable amount of time and tension of collecting information from the actual workplace. For the study, both primary and

secondary data are basically used for analyzing the subject matter of the thesis. But the primary data are collected by informal discussions which are unstructured. Secondary data is collected or applied for the study will be obtained from journals, books, web sites, newspapers and other sources. Official records and publications on related field are also used for the study. The sources of data selected are authentic and reliable and cross checking of data has been done. The secondary data used are internal reports, annual reports and published materials of EBL, Nepal Rastra Bank directives and other sources. . Most of the required data, collected from the official website of NICABL www.nicasiabank.com.

3.5 Data Analysis Tools & Techniques

The information, received from different sources, has been firstly tabulated into separate formats systematically in order to achieve the desired objectives. After that, the data has been tabulated and analyzed. For the purpose of analysis, generally the following tools have been used:

3.5.1 Compliance of NRB Directives

Nepal Rastra Bank is Central Bank of Nepal. Its major objectives are concentrated on financial sector stability in the country. To keep stable financial system some laws, regulations, directives and provisions are imposed to Financial Institutions.

Commercial banks collect deposits from public and it is very same fund they use to make profit. Thus, to prevent this public fund being mis-utilized and to protect the savings of public, NRB has given directives to the commercial banks regarding investment of public fund along with the directives to perform all other jobs of commercial bank. Since loan and advances and leased assets is the first and the main sector of investment, to minimize the risk here, NRB has specifically given guidelines relevant to loan and advances and leased assets in NRB directives as follows:

- a. NRB Directive 1: Provision relating to Capital Adequacy Ratio
- b. NRB Directive 2.: Classification and Provisioning of Loan
- c. NRB Directive 2. Provision Deprived Sector Lending

CBs and FIs are bound to comply with the directives issued by NRB that covers diverse area of banks.

3.5.2 Financial Analysis

Financial analysis is the process of analyzing various items of financial statements of a firm to ensure its comparative strengths and weakness. There are various tools and techniques available for the analysis of any financial data obtained.

Ratio analysis, the easiest way of having assessment of two or more than two firms quantitatively, has been adopted as financial tool for the purpose of study. Although there are various ratios relating to the evaluation of firm's performance, few ratios are merely taken into consideration for our purpose. The ratios used for assessing credit are categorized as:

- a) Credit Practice Ratio
- b) Stability Ratio

a) Credit Practice Ratio: The credit ratios attempt to find out the credit position of any financial institution in relative to various variables. These ratios give the ideas about the extension limit in term of credit. The strategic position i.e., aggressive or conservative of any financial institution is assessed with the help of these ratios.

i) Total Credit to Total Deposit Ratio

Total Credit to Total Deposit= Total Credit/ Total Deposit

The credit of any financial institutions basically depends upon the amount of deposit accumulated by them. The ratio assists to know the lending status and fund utilization position of the particular financial institutions. The higher ratio means huge portion of deposit is employed on lending various sectors and vice versa.

ii) Total Credit to Fixed Deposit Ratio

Total Credit to Fixed Deposit= Total Credit/ Fixed Deposit

The ratio attempts to acknowledge the portion of total credit facility provided among the total fixed deposit. The higher ratio depicts that the portion of credit provided is higher in comparison to fixed deposit and vice versa.

iii) Total Credit to Saving Deposit Ratio

Total Credit to Saving Deposit= Total Credit/ Saving Deposit

The ratio attempts to acknowledge the portion of total credit facility provided among the total saving deposit. The higher ratio depicts that the portion of credit provided is higher in comparison to saving deposit and vice versa.

iv) Total Credit to Total Asset Ratio

Total Credit to Total Asset Ratio = Total Credit/ Total Asset

Loans and Advances are the major part of Total Assets of the bank. This ratio indicates the volume of loans and advances out of the total Assets. A higher degree of the ratio indicates that the bank has been able to mobilize fund through lending function. However lending always carries a certain risk of default. Therefore a high ratio represents low liquidity and low ratio represents low productivity with high degree for safety in terms of liquidity.

v) Interest Income to Total Credit Ratio

Interest Income to Total Credit= Interest Income / Total Credit

Interest income is one of the major sources of income of a commercial Bank. The high volume of interest income is an indicator of good performance of lending activities.

vi) Interest Income to Total Income Ratio

Interest Income to Total Credit= Interest Income / Total Income

This ratio measures the volume of interest income in total income. The high ratio indicates the high contribution made by lending and investment whereas low ratio indicates low contribution made by lending and investment and high contribution by other fee based activities in total income.

b) Stability Ratio:

The solvency position of any financial institutions is measured by their Core capital. The huge accumulated capital ensures about the longer and safe of these financial institutions. Their capital bases are matter of concern of outsiders, insiders and regulatory bodies. Relatively, higher capital instills confidence in the mind of depositors & creditors. In certain long term project financing, preference is placed on capital funds to deposit It is evaluate by the use below mentioned ratios:

i) Capital to Total Deposit:

Capital to Total Deposit=Capital/ Total Deposit

The ratio attempts to tell about the relative position of the capital and total deposit of any financial institutions. The higher ratio ensures about the better capital and solvency position and vice versa. The ratio having value greater than one means the amount of capital is greater than deposit. The ratio also assists to know the fact that by how much degree these financial institutions are playing with deposit holders' money in relative to their own capital.

ii) Capital to Total Credit:

Capital to Total Credit= Capital/ Total Credit

The ratio tells about the relative position of capital and credit. The amount of credit outflow of any financial institutions is generally found much more than the capital accumulated except newly established financial institutions. Thus, these ratios are generally found less than 1. The ratio having greater value is preferable and assumed to be safer than other.

3.5.3 Growth Rate

Growth of Deposit= (Current Year-Previous Year Deposit)/Previous Year Deposit

It gives idea about the increment in the amount of deposit in respect to last year. The aforesaid formula can also assess the increment rate of loan as well as other variables.

Also, Cumulative Average Growth Rate is calculated as:

$$\text{CAGR} = [(\text{Ending Value} \div \text{Beginning Value})^{1/n}] - 1$$

3.5.4 Interest Spread

This rate used to be one of the regulating measure adopted by NRB for the performance of commercial banks. The spread rate having lower value demonstrates the higher efficiency in term of handling deposit and lending. The higher operating expenses and deposit handling cost collectively boost the interest-spread rate of the particular FI. The financial institutions having lower interest spread rate is preferable as it enables the general people to acquire comparatively higher interest rate on deposit and lower interest rate on loan withdrawn. The lower interest spread rate also enables to enhance the competitive position of the particular financial institutions. (NRB Circular)

Method of Calculation of the Spread as prescribed by NRB:

- a) The interest spread has to be calculated on the basis of the interest paid on all deposits in Nepalese Rupee as well as Foreign Currency and Interest earned on Nepalese Rupee and Foreign Currency lending, investments, money at call as well as balance held in foreign nostro accounts.
- b) For the purpose of obtaining average weighted deposit rate, the interest expenses for the particular period shall be divided by the monthly average deposit of the same period with the quotient multiplied by 100. The deposit amount should include all types of deposits, meaning Current, Saving, Fixed, Call deposit and other deposits, including deposits in foreign currency.

Similarly, for the purpose of obtaining average weighted loan rate, the interest income from lending, investment, money at call and foreign nostro account for a particular period shall be divided by the monthly average balances (of loan, investment, money at call and foreign nostro accounts) of the same period with the quotient multiplied by 100. For the purpose of consideration of average loans and advances, only interest bearing loan, investment, money at call and balances held in foreign nostro accounts shall be considered. The inter-bank lending shall not be included for the purpose.

Despite the above methodology, the deposit and lending amount could not obtain in monthly data so the annual data is used for the purpose of analysis.

- c) The difference between the weighted average lending rate and the weighted average deposit rate is the Weighted Interest Spread. It can be expressed as:

Interest Spread Rate= WALR- WADR (NRB Circular)

Where, WALR= Weighted Average Lending Rate

WADR= Weighted Average Deposit Rate

3.5.5 Statistical Tools

Statistic may be defined as the science of collection, presentation, analysis and interpretation of numerical data. It is a method of decision making in the face of uncertainty on the basis of numerical data and calculated risk. (Gupta,2002:7)

For supporting the study, statistical tools such as Correlation Coefficient, Coefficient of determination and Probable Error has been used.

i) Correlation Coefficient

Correlation is defined as the statistical technique which measures the degree and direction of relation between two or more variables. The variables are said to be correlated when the change in the value of one result change in other variables. Correlation is of three types: Simple, Partial and Multiple Correlation. Correlation may be positive, negative and zero. The result of correlation is always between -1 to +1 and it is indicated by 'r'. When $r = +1$, it means there is perfect positive relationship between the variables, when $r = -1$ it means there is perfect negative relationship between the variables and when $r = 0$ it means there is no relationship between the variables.

It is computed using formula given below:

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

Where,

N = no. of Observations

X and Y = Variables for which correlation is determined

ii) Coefficient of Determinations

Coefficient of Determination is a much more useful measure of the linear covariation of two variables. It gives the percentage variation in the dependent variable that is accounted for by the independent variable. Coefficient of Determination is given as r^2 .

iii) Probable Error(P.E) of Correlation Coefficient

The probable error of the correlation coefficient is applicable for the measurement of reliability of the computed value of the correlation coefficient 'r'. It is denoted as P.E. and is given by:

$$P. E = 0.6745 \frac{1 - r^2}{\sqrt{N}}$$

Where,

r = Correlation Coefficient

N= No. of Observation

P.E is used in interpretation whether calculated value of 'r' is significant or not.

a. If $r < P.E$, then Correlation(r) is not significant. In other words there is no correlation between the variables.

b. If $r > 6*P.E$, then Correlation (r) is significant. There is certainly correlation between the variables

CHAPTER IV

DATA PRESENTATION & ANALYSIS

4.1 Introduction

This chapter deals with the presentation, analysis and interpretation of relevant data of NICABL in order to fulfill the objectives of this study. To obtain the best result, the data have been analyzed according to the research methodology as mentioned in third chapter.

“The data after collection has to be processed and analyzed in accordance with the outline laid down for the purpose at the time of developing the research plan.”(Kothari,2003:151) The purpose of this chapter is to introduce to the mechanics of data analysis and interpretation. Data analysis is the relationships or differences supporting or conflicting with original or new hypothesis should be subjected to statistical tests of significance to determine with what validity data can be served to indicate any conclusion.

With the help of this analysis, efforts have been made to highlight credit management of NICABL as well as other cases of problems of NICABL can be visualized. The main objective of the study is to examine the existing policies and practices of Credit Management of NIC Asia Bank Limited.

In order to enhance and strengthen the credit management of the Bank, NIC Asia Bank Limited has implemented credit policies and various credit manuals, product papers, Country Circulars and guidelines in conformity to NRB rules and regulation before the credit proposal or appraisal is actually made and after the credit exposure has been sanctioned to the borrower.

4.2 Financial Analysis

4.2.1 Test of Compliance of NRB Directives

NRB has issued various directives to streamline the commercial banks and other financial institutions. CBs and FIs are bound to comply with the directives issued by NRB that covers diverse area of banks. Capital adequacy, Liquidity position, Loan Classification, Single

Obligor's Limit (SOL) and Provision and Priority Sector Lending are major aspects of these directives.

A. Capital Adequacy Norms for Commercial Banks (NRB Directive No. 1)

Capital adequacy ratio is the ratio which determines the bank's capacity to meet the time liabilities and other risks such as credit risk, operational risk etc.

On the basis of risk-weighted assets, the banks shall maintain the prescribed proportion of minimum capital fund as per the following table:

Fiscal Year	Required Capital Fund on the basis of weighted Risk assets (in percentage)	
	Core Capital	Capital Fund
For FY 2065/66	6%	10%
For FY 2066/67	6%	10%
For FY 2067/68	6%	10%
For FY 2068/69	6%	10%
For FY 2069/70	6%	10%

Source: Unified NRB Directive

While examining capital adequacy of any banks, it can be further classified into core capital and overall capital.

For Core Capital:

$$\text{Capital Adequacy Ratio} = \frac{\text{Core Capital}}{\text{Sum of risk-weighted assets}} \times 100$$

For Overall Capital Fund:

$$\text{Capital Adequacy Ratio} = \frac{\text{Capital Fund}}{\text{Sum of risk-weighted assets}}$$

Where, Capital Fund = Core Capital+ Supplementary Capital

On basis of actual capital maintained by NICABL on respective years to the capital as prescribed by NRB, one can easily know that whether NICABL is complying the directive in this regard or not. For the purpose, the data of 5 years are presented as below:

Table 4.1
Capital Adequacy Test of NICABL

Rs. in Million

For Core Capital (% of Total Risk Assets)	Fiscal Year				
	2065/66 (6%)	2066/67 (6%)	2067/68 (6%)	2068/69 (6%)	2069/70 (6%)
Required Core Capital	944.49	933.56	1,035.04	1,237.83	2,137.45
Actual Core Capital	1,649.01	1,750.45	1,956.12	2,044.94	4,348.99
Result	Complied	Complied	Complied	Complied	Complied
For Overall Capital (% of Total Risk Assets)	(10%)	(10%)	(10%)	(10%)	(10%)
Required Total Capital	1,574.16	1,555.93	1,725.07	2,063.05	3,562.42
Actual Capital Fund	1,954.93	2,010.56	2,223.77	2,271.86	4,693.28
Result	Complied	Complied	Complied	Complied	Complied

Source: NICABL Annual Reports

The core capital of CBs must be at least up to 6.00% of total risk asset held by them. Table 4 shows that the actual core capital maintained by NICABL were more than that prescribed by NRB in all five years. It portrays that NICABL has complied NRB requirement of core capital adequacy.

Another requirement relating to capital adequacy is the overall capital. CBs must maintain its overall capital at least 10% of total risk assets. The actual capital funds of NICABL were more

than prescribed by NRB in all five years. It portrays that NICABL has complied NRB requirement of capital adequacy.

Apart from above analysis of the capital adequacy test, capital to total risk asset ratio of 5 previous years are also discussed as below:

Table 4.2
Capital Adequacy Ratios of NICABL

Rs in Million

Particulars	Fiscal Year				
	2065/066	2066/067	2067/068	2068/069	2069/070
Core Capital	1,649.01	1,750.45	1,956.12	2,044.94	4,348.99
Capital Fund	1,954.93	2,010.56	2,223.77	2,271.86	4,693.28
Total risk Assets	15,741.61	15,559.35	17,250.71	20,630.57	35,624.17
Core Capital/Total Risk Assets (a)	10.48%	11.25%	11.34%	9.91%	12.21%
NRB Requirement (b)	6%	6%	6%	6%	6%
Excess in Core Capital (a-b)	4.48%	5.25%	5.34%	3.91%	6.21%
Capital Fund/ Total Risk Assets (a)	12.42%	12.92%	12.89%	11.01%	13.17%
NRB Requirement (b)	10%	10%	10%	10%	10%
Excess in Total Capital Fund (a-b)	2.42%	2.90%	2.89%	1.01%	3.17%

Source: NICABL Annual Reports

In Table 4.2, CAR (Capital Adequacy Ratio) in Core Capital of NICABL is found to be 10.48%, 11.25%, 11.34%, 9.91% and 12.21% of total risk asset in Ashad 2066-Ashad 2070 respectively whereas the Capital Adequacy Ratio in terms of capital fund has been found 12.42%, 12.92%,

12.89%, 11.02% and 13.17% of total risk asset in Ashad 2066- Ashad 2070. It clearly gives sense that NICABL has complied NRB directive of capital adequacy ratio in all 5 years.

B. Directives relating to loan classification and provisioning (Directive no.2)

The Loan Loss provisioning on the basis of the outstanding loans and advances and bills purchases classified as per NRB Directives shall be as follows:

<u>Classification of Loan</u>	<u>Loan Loss provision</u>
➤ Pass	1 Percent
➤ Substandard	25 Percent
➤ Doubtful	50 Percent
➤ Loss	100 Percent

Note: A minimum of 12.5% provision is to be made on rescheduled or restructured loans.

Table 4.3
The Classification and Provisioning of NPA of NICABL

Rs in Million

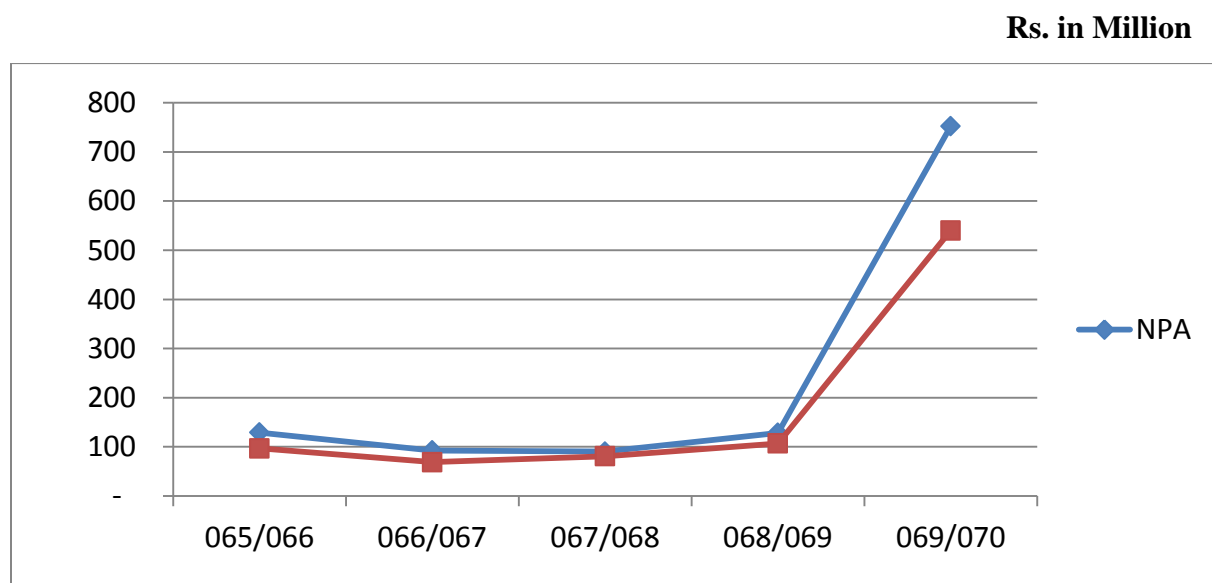
Particulars	Ashad 2066			Ashad 2067			Ashad 2068		
	Amount	% of loan to total credit	Provision	Amount	% of loan to total credit	Provision	Amount	% of loan to total credit	Provision
Pass Loan(a)	13,771.07	98.96	137.71	12,836.81	99.28	128.36	15,075.15	99.40	150.75
Sub-Standard Loan(b)	2.42	0.02	0.605	18.64	0.14	4.66	5.67	0.04	1.41
Doubtful Loan(c)	61.13	0.44	30.56	19.17	0.15	9.58	10.55	0.07	5.27
Loss Loan(d)	65.62	0.47	65.62	54.67	0.42	54.67	74.12	0.49	74.12
Total NPA :-	129.17	0.93	96.79	92.49	0.72	68.92	90.35	0.60	80.82
Rescheduled Loan (e)	15.59	0.11	1.94	-	0.00	-	0	0	
Total of (b+c+d+e)	144.77	1.04	98.74	92.49	0.72	68.92	90.35	0.60	80.82
GRAND TOTAL	13,915.85	100.00	236.45	12,929.30	100.00	197.28	15,165.51	100.00	231.57

Particulars	Ashad 2069			Ashad 2070		
	Amount	% to total credit	Provision	Amount	% to total credit	Provision
Pass Loan(a)	17,394.64	99.27	173.94	31,663.82	97.68	316.63
Sub-Standard Loan(b)	13.88	0.08	3.47	210.14	0.65	52.53
Doubtful Loan(c)	22.39	0.13	11.19	109.43	0.34	54.71
Loss Loan(d)	92.26	0.53	92.26	432.75	1.34	432.75
Total NPA :-	128.54	0.73	106.93	752.34	2.32	540.01
Rescheduled Loan(e)	-	-	-	-	-	-
Total of (b+c+d+e)	128.54	0.73	106.93	752.34	2.32	540.01
GRAND TOTAL	17,523.19	100.00	280.88	32,416.17	100.00	856.65

Source: NICABL Annual Reports

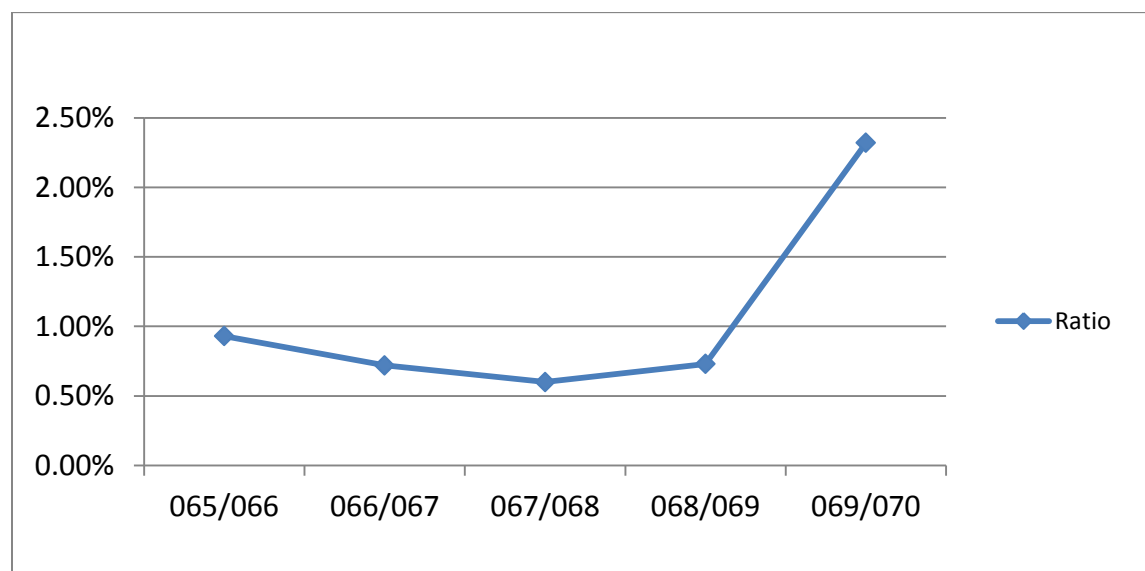
As per the NRB guidelines Loan loss provision of 25% on Substandard Loan, 50% on Doubtful Loan and 100% on Loss Loan, Table 6 depicts that NICABL has followed the NRB guidelines.

Figure 4.1
Non-Performing Asset & Provision



Against the Non-performing Assets of Rs 129.17 Million, the total provisioning has been made for an amount of Rs 96.79 Million (i.e. 74.93 %) for the period ending Ashad 2066. Against non-performing Assets of Rs 92.49 Million, the provisioning has been made for an amount of Rs 68.92 Million (i.e. 74.51%) for the period ending Ashad 2067. Against non-performing Assets of Rs 90.35 Million, the provision of Rs 80.82 Million (i.e. 89.45 %) has been made for the period ending Ashad 2068. Against non-performing Assets of Rs 128.54 Million, provision of Rs 106.93 Million (i.e. 83.19 %) has been made for the period ended Ashad 2069 and for the period ending Ashad 2070 for NPA of Rs. 752.34 provision has been made of Rs.540.01 which is 71.77%.

Figure 4.2
Ratio of Gross NPA to Total Credit



The percentage of Nonperforming Assets (excluding rescheduled accounts) to Total loan for the year ended Ashad 2066 is 0.93%, 0.72% for the year ended Ashad 2067, 0.60% for the year ended Ashad 2068, 0.73% for the year ended Ashad 2069 and 2.32% for the year ended Ashad 2070. This shows that the percentage of non-performing assets to the total credit is consistently below 1% for the majority of the Years under review. This demonstrates a very strong asset quality of the bank. However post-merger, it appears that due to the credit quality as demonstrated by Non-Performing Asset Level of the Bank of Asia (Nepal) Ltd., the overall Non Performing Loan to Total Loan ratio has jumped to 2.32%. Hence there lies a challenge to the Bank to manage and streamline its NPA portfolio post-merger.

C. Requirement to Extend Advances to Deprived Sector

Commercial Banks are required to extend advances in the deprived sector at various % depicted in the table below.

Fiscal Year	Minimum Percent of Total Credit to be invested in Deprived Sector
2065/66	3.0%
2066/67	3.0%
2067/68	3.0%
2068/69	3.5%
2069/70	4%

Source: Unified NRB Directives

The deprived sector lending is based on the Loans & Advance Outstanding six months before the actual date of compliance. For example the deprived sector lending at Ashad end 2068/69 shall be 3.5% of Loans and advances outstanding as of Poush 2068/69.

Table 4.4

Test of Deprived Sector Lending of NICABL for 2065/66 to 2069/70

Rs in Million

Particulars	2065/066	2066/067	2067/068	2068/069	2069/070
Deprived Sector Lending	422.80	442.79	448.06	541.13	1,190.23
(Applicable) Loans and Advances	12,584.98	14,727.03	14,293.01	15,322.87	18,158.53
Percentage	3.36%	3.01%	3.13%	3.53%	6.55%

Source: NICABL Financial Publications & Corporate Office

Table 4.4 shows that the Deprived Sector Lending of NICABL is in increasing trend except for FY 2066/067. It has decreased by 10.41% in FY 2066/67, then increased by 4% in FY 2067/68 by 12.77% in FY 2068/69 and by 85.5% in FY 2069/70. Huge fluctuation seen in 2069/70 is on

account of merger of Loan portfolio of Bank of Asia and NIC Bank. The table above depicts that NICABL's deprived sector lending is above mandatory requirement of NRB and hence it has duly fulfilled its deprived sector lending.

4.2.2 Credit Practice Ratios:

This ratio tells about the credit position of any bank. It gives idea of comparative status of credit with respect to overall deposit and its component. The below mentioned credit ratios provide clear-cut ideas of banks about credit.

i. Total Credit to Total Deposit Ratio

Table 4.5
Total Credit to Total Deposit Ratio

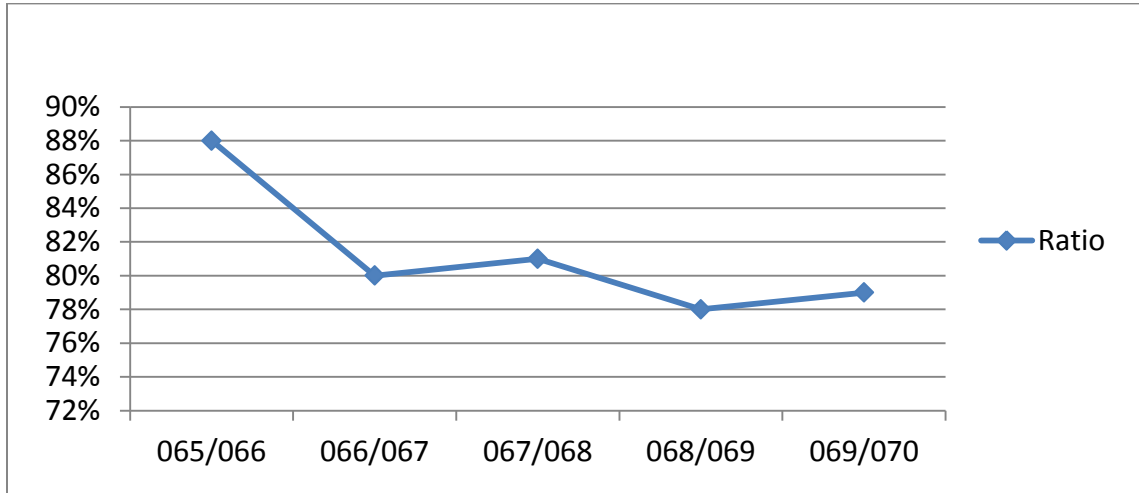
Rs in Million

Year	Total Credit	Total Deposit	Ratio (%)
2065/066	13,679.39	15,579.93	87.80
2066/067	12,732.01	15,968.91	79.73
2067/068	14,933.93	18,394.43	81.19
2068/069	17,242.30	22,111.85	77.98
2069/070	31,559.51	39,908.77	79.08
Total	90,147.14	111,963.89	80.51

Source: NICABL Annual Reports

As illustrated in Table 4.5 the **Credit to Total Deposits ratios** was observed to be very high at an average of 80% in NICABL over the review period. NICABL has extended more than 80% of its deposit as loan & advances. The highest ratio in NICABL was 87.80% in FY 2065/066 and lowest 77.98% in FY 2068/069. In general, 70%-80 % credit deposit ratio is assumed to be appropriate considering to market demand and internal strength of a particular bank. The higher Credit to Total deposit ratio increases liquidity risk of the Bank whereas lower CD ratio decrease profitability. Hence a fine balance should be the Bank's endeavor so as to enhance profitability but minimize liquidity risk.

Figure 4.3
Total Credit to Total Deposit Ratio



NICABL's high Credit to Deposit ratio on the one hand signifies efficient deployment of its deposit fund and increase profitability however this also indicates low liquidity ratios which might bring about high liquidity risk. CD ration within a range of 75-78% is considered appropriate.

ii. Total Credit to Fixed Deposit Ratio

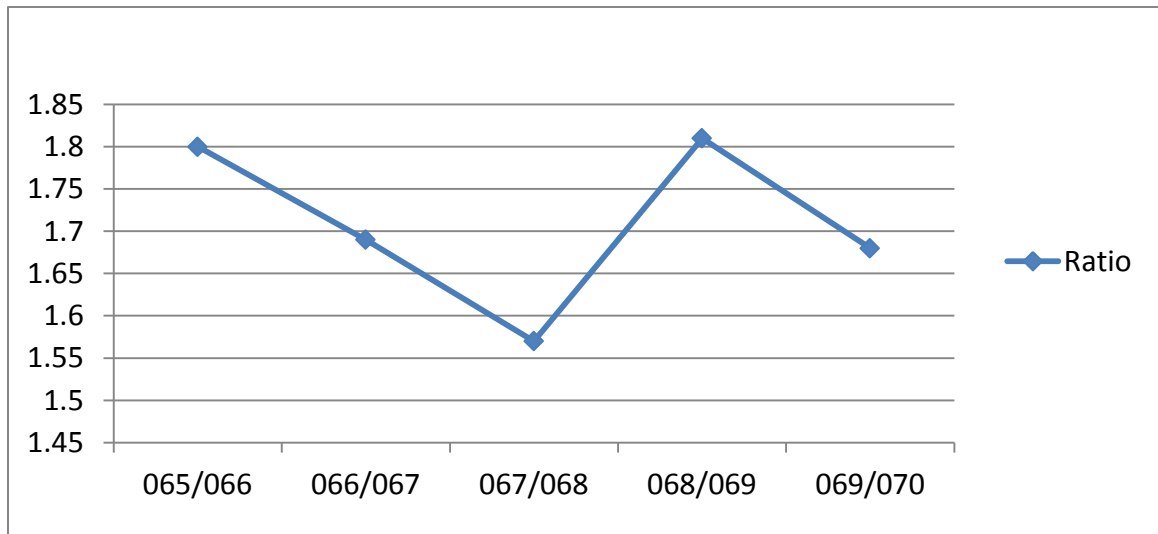
Table 4.6
Total Credit to Fixed Deposit

			Rs in Million
Year	Total Credit	Fixed Deposit	Ratio(times)
2065/066	13,679.39	7,580.05	1.80
2066/067	12,732.01	7,554.05	1.69
2067/068	14,933.93	9,517.55	1.57
2068/069	17,242.30	9,535.56	1.81
2069/070	31,559.51	18,824.56	1.68
Total	90,147.14	53,011.77	1.70

Source: NICABL Annual Reports

This ratio is observed in decreasing trend in each year in case of NICABL except in FY 2068/69. It shows that the growth in credit is higher relative to fixed deposit collected in NICABL.

Figure 4.4
Total Credit to Fixed Deposit Ratio



The **credit as a ratio of fixed deposit** demonstrates the credit as a whole in comparison to stable deposit's portion. This ratio is observed in decreasing trend in each year in case of NICABL except in FY 2068/69.

It shows that the growth in credit is higher relative to fixed deposit collected in NICABL. It also demonstrates that the credit is decreasingly backed by high cost source of fund that is fixed deposits and hence increasing the Yield on Lending and Spread. In case of NICABL, this ratio was recorded lowest in FY 2067/068 i.e. 1.57 times and highest in FY 2068/069 i.e. 1.81 times. Very low credit as a ratio of fixed deposits reduces stability of the Institution/Bank however very high credit as a ratio of fixed deposits increases cost of funding hence decrease in Yield on lending as well as profitability. This ratio is also unique to the specific market and hence should be compared with the Peer Bank as well as industry average for coming into right conclusion. Generally a ratio of 25% of the deposits being funded in the form of Fixed Deposit is considered appropriate.

iii. Total Credit to Saving Deposit Ratio

Table 4.7
Total Credit to Saving Deposit

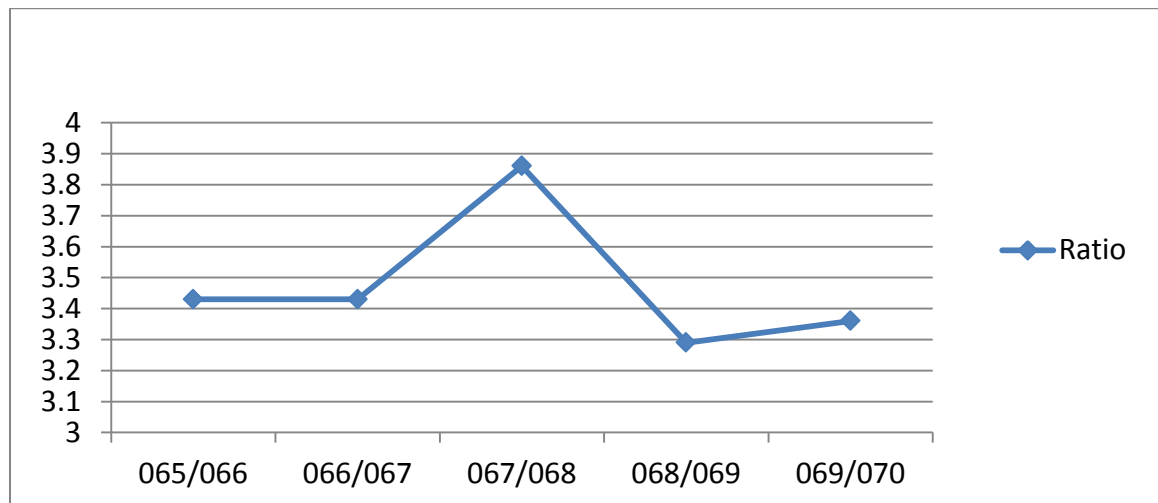
Rs in Million

Year	Total Credit	Saving Deposit	Ratio (times)
2065/066	13,679.39	3,993.71	3.43
2066/067	12,732.01	3,715.84	3.43
2067/068	14,933.93	3,869.84	3.86
2068/069	17,242.30	5,243.83	3.29
2069/070	31,559.51	9383.95	3.36

Source: NICABL Annual Reports

The credit as a ratio of saving deposit is observed to be in increasing trend in review years. This also implies that the % of saving deposit funding for credit growths is increasing in NICABL. The highest ratio recorded in FY 2067/068 i.e 3.86 and lowest at FY 2068/069 i.e 3.29

Figure 4.5
Total Credit to Saving Deposit Ratio



The savings deposits forms a very stable base of funding and also has relatively lower costs. Its increasing back up for extending credit is very positive sign and also signifies decrease in cost of fund hence increase in Yield and spread. NICABL in this respect is moving towards the right direction.

iv. Total Credit to Total Asset Ratio

Table 4.8
Total Credit to Total Assets

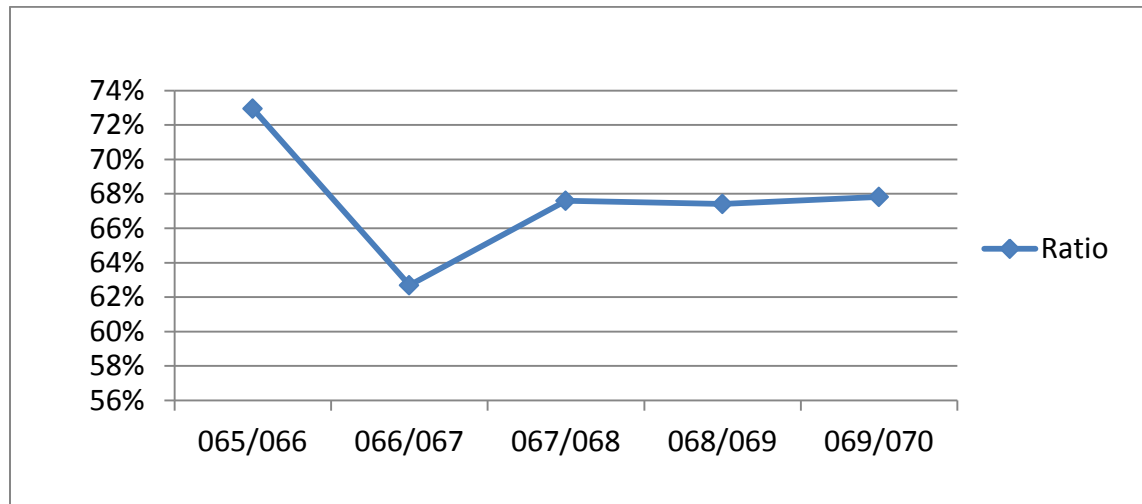
Rs In Million

Year	Total Credit	Total Assets	Ratio (%)
2065/066	13,679.39	18,751	72.95
2066/067	12,732.01	20,309	62.69
2067/068	14,933.93	22,090	67.60
2068/069	17,242.30	25,580	67.41
2069/070	31,559.51	46,535	67.82

Source: NICABL Annual Reports

Loans and advance is part of Total Assets. Thus there is direct relationship between Credit and total assets. The “credit as percentage of total assets” of NIC Asia Bank is in decreasing trend as depicted by the above table.

Figure 4.6
Total Credit to Total Assets Ratio



Credit or Loans and Advances are the major source of income for any commercial Bank. Higher portion of such items in Total assets signifies solid base for the earnings and causes increase in Interest Income vis a vis total revenue and hence profitability. However the decrease proportion

of Credit in total Asset of NICABL is quite concerning which is at a minimal of 62.69% in FY 2066/067. However same has increased in later fiscal years.

v. Interest Income to Total Credit Ratio

Table 4.9
Interest Income to Total Credit

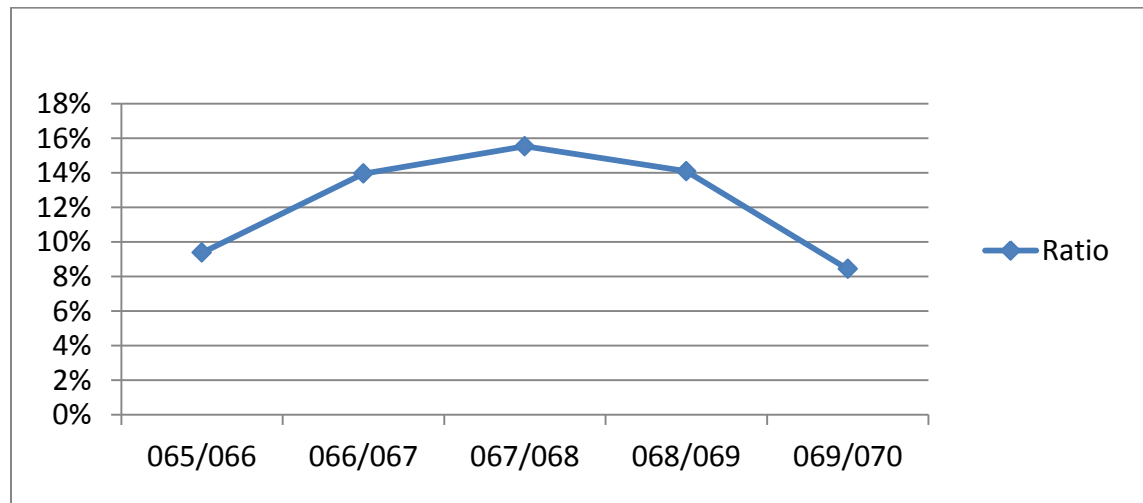
Rs in Million

Year	Interest Income	Total Credit	Ratio (%)
2065/066	1,283.52	13,679.39	9.38
2066/067	1,777.16	12,732.01	13.96
2067/068	2,321.40	14,933.93	15.54
2068/069	2,431.53	17,242.30	14.10
2069/070	2,663.45	31,559.51	8.44

Source: NICABL Annual Reports

Interest Income is directly proportional to loans and advances. If Loans and advances increase, then interest income also increases and vice versa. In case of NICABL, % of interest income to total loans and advances is observed to be in increasing trend upto 2067/068 while the same has decreased in later FYs.

Figure 4.7
Interest Income to Total Credit Ratio



This gives an estimate that Yield on Lending (YOL) of NICABL has continuously increased in the review period upto FY2067/068 which is a positive sign and reflects significant improvement in profitability. However Yield on lending has dropped in FY 2068/069 and 2069/70.

vi. Interest Income to Total Income Ratio

This ratio measures the volume of interest income in total income. The high ratio indicates higher contribution made by lending and investment whereas low ratio indicates low contribution made by lending and investment and high contribution by other fee based activities in total income.

Table 4.10
Interest Income to Total Income

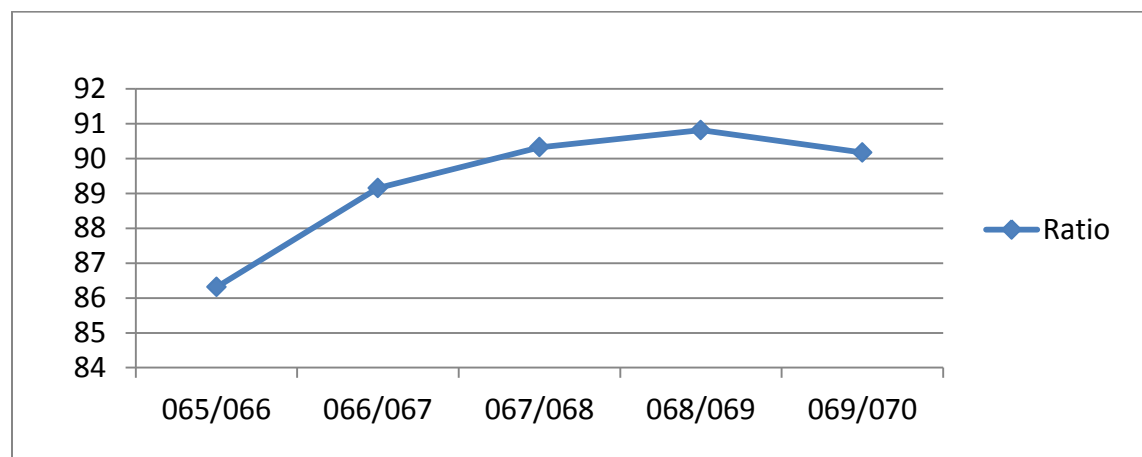
Rs in Million

Year	Interest Income	Total Income	Ratio (%)
2065/066	1,283.52	1,487.11	86.31
2066/067	1,777.16	1,993.48	89.15
2067/068	2,321.40	2,570.31	90.32
2068/069	2,431.53	2,677.50	90.81
2069/070	2,663.45	2,953.66	90.17

Source: NICABL Annual Reports

The proportion of interest income to total income is in increasing trend in case of NICABL.

Figure 4.8
Interest Income to Total Income Ratio



Interest income is the major income of a commercial bank. The proportion of interest income to total income is in increasing trend in case of NICABL. This reflects increasing yield on lending and healthy loans and advances portfolio. However simultaneously it reflects shrinking portion of non-interest income. For a growing Bank which has attained a reasonable size, it is also appropriate that it diversify its earning avenues and explore more on Fees and Commission and other income fronts. This appears to be the need of the hour for NICABL.

4.2.3 Stability Test Ratio

Stability test of any bank is carried to ascertain the sustaining capacity in long run. The test is carried by studying Capital position (Core Capital) in relative to various variables

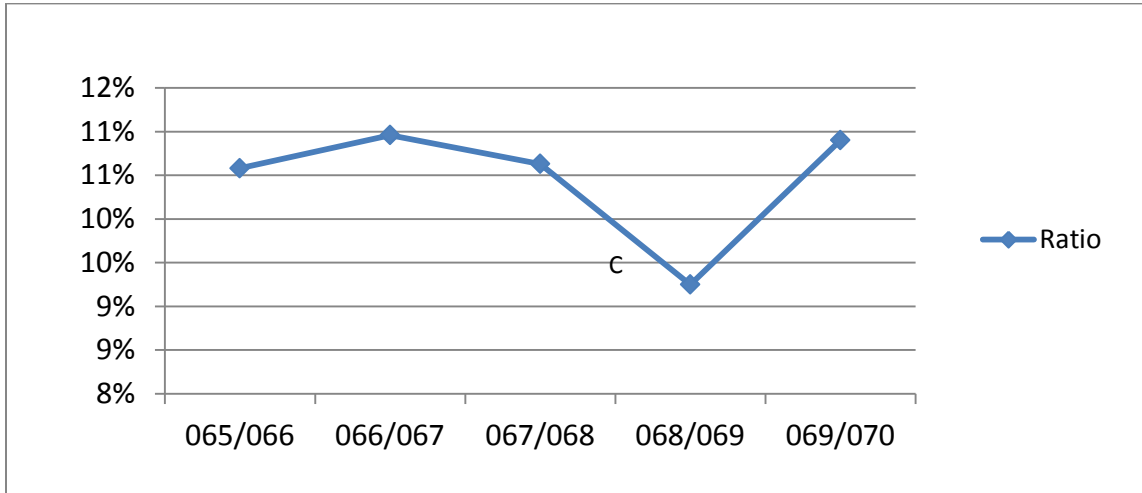
Table 4.11
Stability Test Ratios of NICABL

Rs in Million

Year	Core Capital	Total Deposit	Total Credit	Capital to Total Deposit (%)	Capital to Total Credit (%)
2065/66	1,649.00	15,579.93	13,679.39	10.58	12.05
2066/67	1,750.45	15,968.91	12,732.01	10.96	13.75
2067/68	1,956.12	18,394.43	14,933.93	10.63	13.10
2068/69	2,044.94	22,111.85	17,242.30	9.25	11.86
2069/70	4,348.99	39,908.77	31,559.51	10.90	13.78

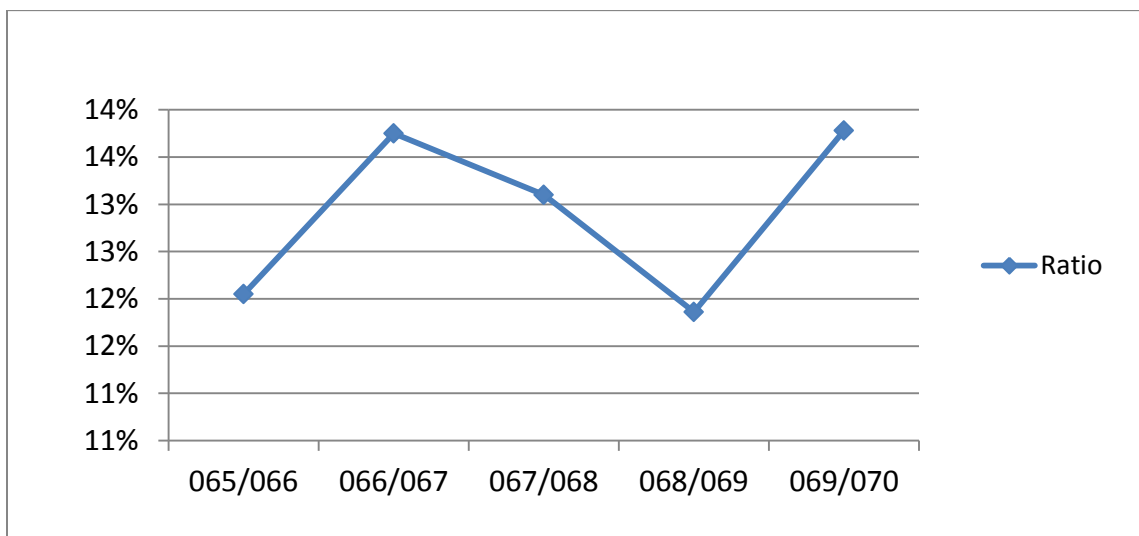
Source: NICABL Annual Reports

Figure 4.9
Core Capital to Total Deposit Ratio



Capital to Total Deposit Ratio of NICABL is more or less stable with a fluctuation of around 1%. This ratio reflects capital coverage for the depositors and the higher ratio increases comfort of the deposit holders. Capital's position in relative to deposit has maintained at around 10.50% average in five years.

Figure 4.10
Core Capital to Total Credit Ratio



“**Capital to Total Credit**” is found stable in NICABL in all five years. NICABL has maintained around 12.90% in average Capital to total Credit in the review period. It means both the capital and total credit are in increasing trend at NICABL. The improvement made by NICABL in building up its stability position is remarkable. It is due to higher growth rate of capital in comparative to growth rate of credit floated.

4.2.4 Analysis of Cost of Deposit Fund, Yield on Lending and Interest Spread

Interest rate spread is one of the most important indicators of financial intermediation efficiency of any CB's. Every financial institution pays certain prevailing interest rate on deposits and receive higher rate of interest from lending. The differential interest margin is basic incentive to FI's to cover their operational costs and contribute to the worth of equity holders. NRB has directed to CBs to lower their weighted interest rate spread within 5 %. The higher interest rate spread indicate that depositors are getting lower interest rate while borrowers are being punished with high interest charge curtailing the flow of loans to the export and industrial sectors or other productive projects. This situation retards the pace and process of economic development.

The table below shows the cost of deposit, lending rate and interest spread rate of NIC Asia Bank Limited for five years from FY 065-66 to FY 069-70.

Table 4.12
Cost of Deposit, Yield on Lending and Interest Spread of NICABL

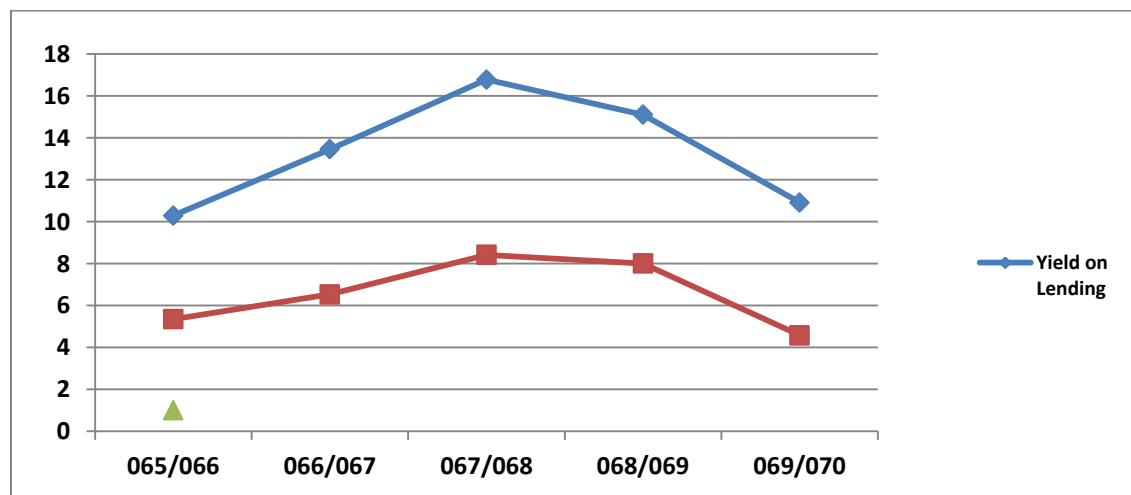
Particulars	Rs. in Million				
	2065/066	2066/067	2067/068	2068/069	2069/070
Average Deposit	14,332.31	15,774.42	17,181.67	20,253.14	31,010.31
Interest Expenses	767.19	1,031.47	1,446.63	1,621.80	1,420.12
Cost of Deposit (a)	5.35%	6.54%	8.42%	8.01%	4.58%
Average Lending	12,472.03	13,205.70	13,832.97	16,088.12	24,400.90
Interest Income	1,283.52	1,777.16	2,321.40	2,431.53	2,663.45
Yield on Lending (b)	10.29%	13.46%	16.78%	15.11%	10.92%
Interest Spread (b-a)	4.94%	6.92%	8.36%	7.11%	6.34%

Source: NICABL Annual Reports

The figure portrays that the cost of deposits are in continuously increasing trend and simultaneously the Yield on Lending has also followed the increasing Trend. The Interest spread has also significantly increased until 67/68 and has taken downward trend thereafter.

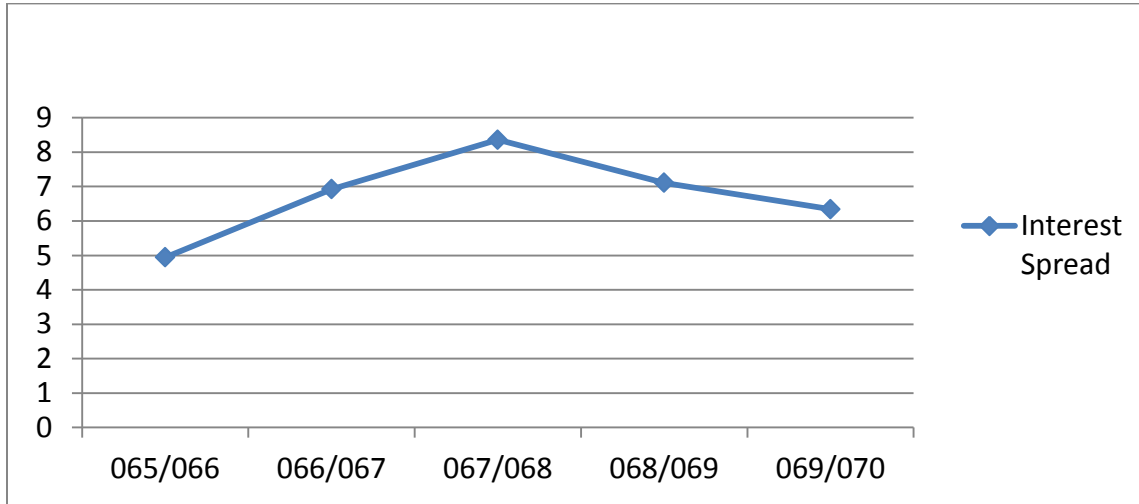
From general public's point of view, it is better when FIs provide higher interest rate in deposit and charge lower interest rate on loan & advances. In fact, it is idle situation that is desired by society & government. NRB on behalf of government attempts to attain perfect harmony. Until now, the matter of interest-spread rate was been completely deregulated by NRB since our economy is maneuvering towards free market economy and market's demand and supply takes its own course in adjusting interest spread, however now NRB has come up with circular in this FY 2070/71 requiring Banks and FI to maintain their spread at a maximum of 5% .

Figure 4.11
Yields on Lending and Cost of Deposit



It is believed that in a competitive economy, those FIs desiring excessively high interest spread shall be in severe difficult situation as in free market-oriented economy, customers will not prefer those FIs that have high interest spread and this will raise question in the concerned FIs sustainability. In fact, maintaining lower interest spread rate means possessing higher competitive position and higher financial intermediation efficiency.

Figure 4.12
Interest Spread



In a situation where the level of non-performing asset of the bank is quite large, all the bad debts get translated into higher interest rate for the borrowers & lower interest rate for the depositors. It is a clear symptom of financial & commercial inefficiency. To sum up, Darwin's principle of "Survival of Fittest" also fits in the banking sector. Financial market is very competitive and only fittest FIs can sustain or exist.

4.2.5 Analysis of Deposits, Loans & Advances and Investments

The deposit of banks and FIs are raw material that is essential for providing loans and advances to the customers and hence vital for the operation of the Bank. The deposit must be sufficient to meet the demands of the loans as well as ensure mandatory investment requirement, of course this is also to some extent supplemented by Capital Fund and long term Funds like Bonds etc. Inadequate level of deposit hinders the growth of the particular financial institutions so various deposit schemes are introduced by various banks to get rid from deposit crunch.

Table 4.13

Deposit, Loan and Investment position of NICABL

Rs in Million

Year	2065/66	2066/67	2067/68	2068/69	2069/70	CAGR
Deposits	15,579	15,968	18,394	22,111	39,908	21%
Loans & Advances	13,679	12,732	14,933	17,242	31,559	18%
Investments	3,026	4,946	4,868	3,992	6,811	18%

Source: NICABL Annual Reports

The Deposits of NICABL are in increasing trend over the review period as shown in table 16. Its deposit rose from Rs. 15,579 million in 2065/066 to Rs. 39,908 million till 2069/070. This is an increase of Rs.24,329 million in the period of five years. A cumulative average growth rate (CAGR) of about 21% on deposits has been witnessed during the review period. This huge growth in deposit is also on account of merger of Bank of Asia with NIC Bank.

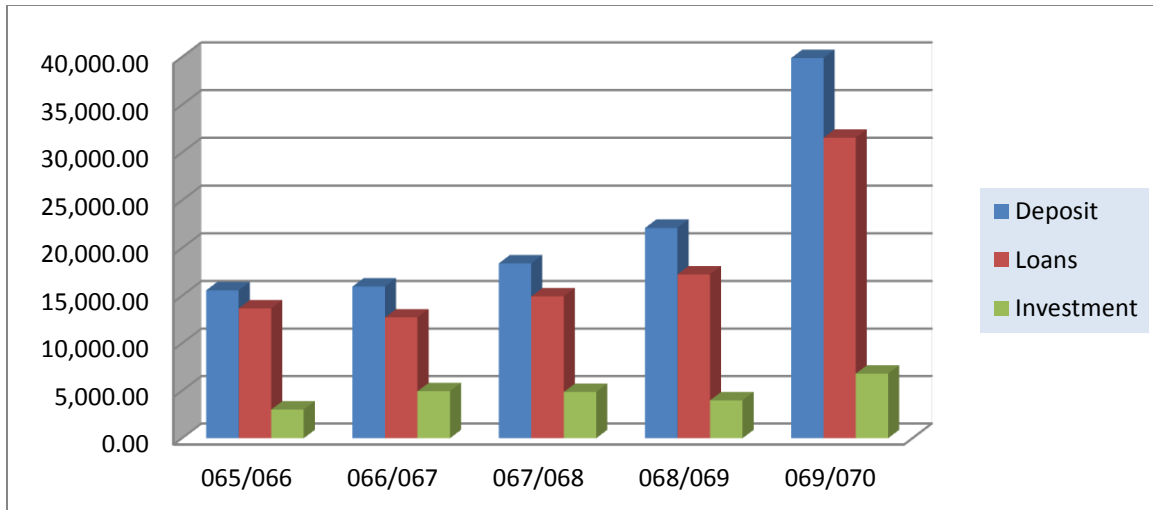
The lending of the bank has also increased continuously from Rs. 13,679 million to Rs. 31,559 million till 2069/070. This is an increase of Rs. 17880 million in five years. A cumulative average growth rate (CAGR) of about 18% on Loans has been witnessed during the review period.

Similarly the investments have also increased from Rs 3,026 million in 2065/066 to Rs. 6,811 million till 2069/070. A cumulative average growth rate (CAGR) of 18%

Figure 4.13

Deposits, Loans & Advances and Investment Position of NICABL

Rs in million



The above bar diagram has been drawn on basis of table 16 and reveals the comparative position of deposit and lending of NICABL in respective years.

4.2.6 Analysis of Growth Rate of Deposits, Loans & Investments

It is essential to know the growth rate of various important variables to evaluate the performance of any organization. The Deposit, Lending and Investments are key variables of banking sector and they have serious impact on the overall profitability of any FIs. Profitability can't be imagined without adequate amount of lending on the basis of capital base and accumulated deposit. The data of deposit collected by NICABL is given below:

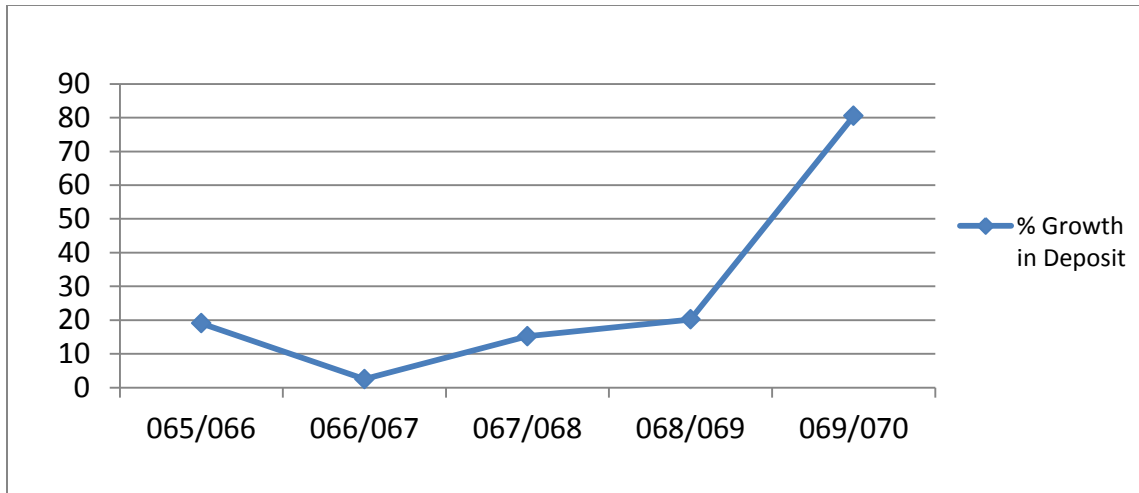
Table 4.14
Growth rate of Deposits of NICABL

Rs in millions

Year	2065/066	2066/067	2067/068	2068/069	2069/070
Deposit (Rs.)	15,579.93	15,968.91	18,394.43	22,111.85	39,908.77
Growth Rate	19.07%	2.50%	15.19%	20.21%	80.49%

Source: NICABL Annual Reports

Figure 4.14
Growth Rate of Deposit



Deposit growth rate in the FY 2065/066 is the maximum i.e. 30.00% and the growth rate is lowest in 2066/067 i.e. 2.50%. It appears that NICABL has been performing best in terms of Deposits by meeting the requirement of depositors as well as portraying stability and confidence in them. The Bank's growth in deposit volume is above the average performance of the banking sector.

Table 4.15
Showing Growth rate of Loan and Advances of NICABL

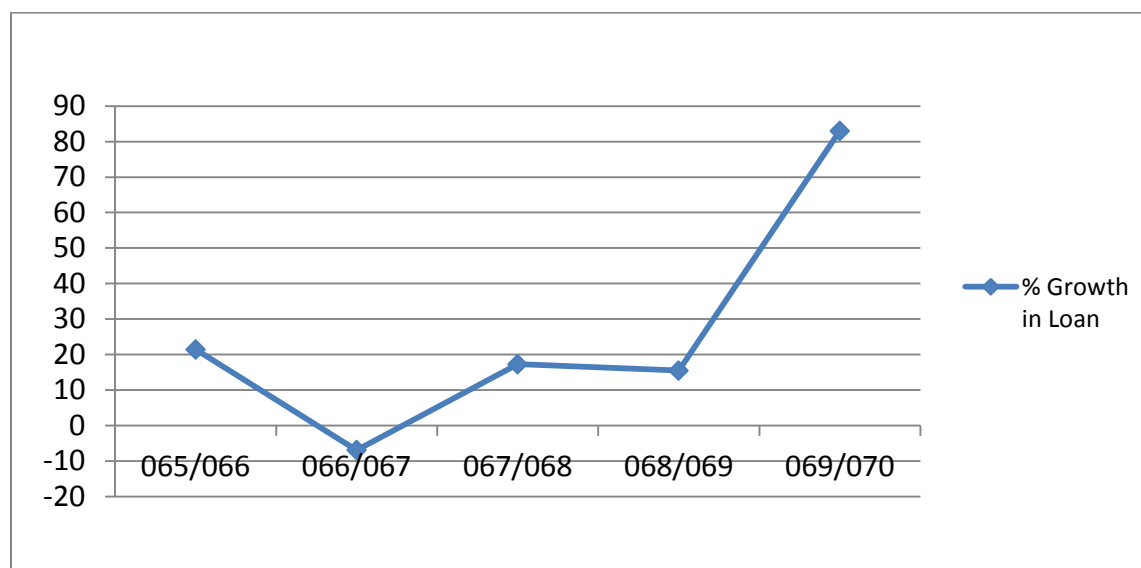
Rs in millions

Year	2065/066	2066/067	2067/068	2068/069	2069/070
Loan & Advances	13,679.39	12,732.01	14,933.93	17,242.30	31,559.51
Growth Rate	21.44%	(6.93)%	17.29%	15.46%	83.03%

Source: NICABL Annual Reports

The amount of loan & advances of NICABL has increased each year except for FY 2066/67 however its rate of increment is fluctuating over period of time. The rate is the lowest in 2066/067 i.e. -6.93% whereas highest in 2069/070 i.e. 83.03%. The abnormal growth of 83.03% in FY 2069/70 is on account of merger of Bank of Asia with NIC Bank.

Figure 4.15
Growth Rate of Loans & Advances



Growth rate of Loans and advances during the review period is quite impressive and is above 15%. However Year 2066/67 the Loan portfolio saw a decrease of around 7%. However the same picked up in later fiscal years. Keeping a steady growth rate of assets without compromise in quality is a great challenge for any commercial Bank.

Table 4.16
Showing Growth rate of Investment of NICABL

Rs in millions

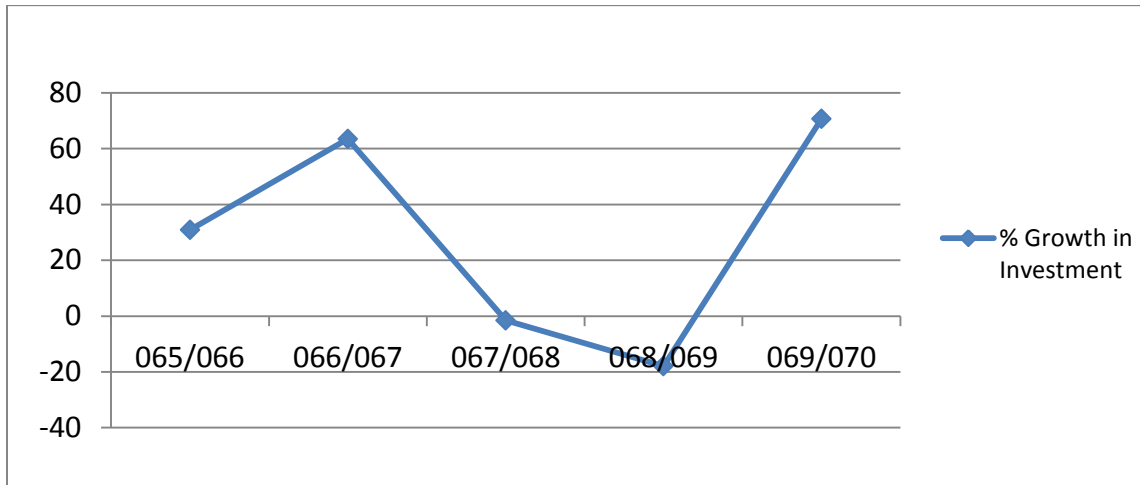
Year	2065/066	2066/067	2067/068	2068/069	2069/070
Investments	3,026.02	4,946.77	4,868.91	3,992.73	6,811.87
Growth Rate	30.91	63.47	(1.57)	(18.00)	70.60%

Source: NICABL Annual Reports

Investment is in fact resultant figure. Its volume depends upon the deposits portfolio. NRB directive currently requires at least 5.0% of deposits portfolio to be parked as Compulsory Cash Reserve (CRR) at NRB and also requires 12% of such deposits as Statutory Liquidity Ratio (SLR). However commercial Bank should maintain a Liquidity ratio of at least 20%. CRR and

SLR however form part of this liquidity ratio. Investments are done out of the fund available under Liquid funds.

Figure 4.16
Growth Rate of Investment



Basel II capital adequacy Framework under NRB directive 1 requires additional Risk Weighted exposure towards liquidity risk in case over all liquidity is deficit than 20%. Such funds in excess of CRR and that forms part of Liquid Funds are usually invested in Treasury Bond, Savings Bonds, Placements etc. and forms the Bank's Investment portfolio.

4.2.7 Position of Major Financial Indicators in NIC Asia Bank Limited for FY 2065/66 to 2069/070

Table 4.17
Major Financial Indicators of NICABL

Rs. in million

Particulars	2065/66	2066/67	2067/68	2068/69	2069/70	CAGR
Loan & Advances	13,679	12,732	14,933	17,242	31,559	18%
Deposit	15,579	15,968	18,394	22,111	39,908	21%
Interest on Loan	1,283	1,777	2,321	2,431	2,663	16%
Total Income	1,487	1,993	2,570	2,677	2,953	15%
Total Expenditure	961	1,288	1,774	2,012	1,887	14%
Operating Profit	486	687	760	615	978	15%
Net Profit	317	449	495	391	642	15%
NPA	129	92	90	128	752	42%
Ratio of NPL to Credit	0.93%	0.72%	0.6%	0.73%	2.32%	20%

Source: NICABL Annual Reports

Table 4.17 highlights that the amount of loan & advances of NICABL has increased each year except for FY 2066/67 however its rate of increment is fluctuating over period of time. The rate is the lowest in 2066/067 i.e. -6.93% whereas highest in 2069/070 i.e. 83.03%. The abnormal growth of 83.03% in FY 2069/70 is on account of merger of Bank of Asia with NIC Bank. A cumulative average growth rate (CAGR) of about 18% on Loans has been witnessed during the review period.

The increase in the figure of loan and advances has resulted increase in the interest income of the Bank. The loan and advances of the bank portrays direct relation with the interest income of the bank. Increase in loan and advances by an average of 18% have led the bank's increase in interest income by an average of 16%. This reflects that bank has been able to command higher pricing hence Bank's Yield on lending has substantially increased over the review period resulting in the increased profitability.

In general, there is high chance of increase in the non-performing loan as the loan and advances of the bank increases. On the contrary the non-performing loans of NIC Asia Bank appear to be in decreasing trend which is very impressive.

Total deposit of the NICABL is also in increasing trend following Loans and advances. In fiscal year FY 2066/67 the deposit has increased by 2.5%, in FY 2067/68 by 15.19%, in FY 2068/69 by 20.21% and in FY 2069/70 by 80.49% amounting to Rs 39,908.77 Million. The average growth of deposits over the review period is about 21% which is in line with overall growth of Loans and advances by 18%.

The total operating profit and net profit is also observed in increasing trend except for FY 2068/69. In fiscal year in FY 2066/067 the operating profit has increased by 41.47%, compared to the corresponding period of Last fiscal year, in FY 2067/068 by 10.64% and in FY 2068/069 by -19.33% and in FY 2069/70 . The average growth in Operating profit of NIC Asia Bank is 16%.

Likewise the net profit of NICABL is also in increasing trend. In fiscal year 2066/067 the net profit has increased by 41.71%, compared to the corresponding period of Last fiscal year, in FY 2067/068 by 10.14% and in FY 2068/069 by -21.01 and in FY 2069/70 by 64.19%. This is an average overall growth of 15% in Net Profit.

4.3 Statistical Analysis

4.3.1 Coefficient of Correlation

Coefficient of correlation analysis is used to find out relationship between Total Deposit and Credit, Interest Income from loan and Total Income, Non-Performing Loan and Total Credit, Loan Loss Provision and Total Credit & NPA and LLP

i) Coefficient of Correlation between Total Deposit and Total Credit

The Coefficient of Correlation between Total Deposit and Total Credit measures the degree of relationship between two variables. In our analysis Total Deposit is an independent variable and Total Credit is dependent variable. The main objective of computing correlation between the two

variables is to find out whether deposits are significantly used as loans and advances of NICABL.

Table 4.18
Correlation between Total Deposit and Total Credit

Evaluation Criteria	Result
Coefficient of Correlation (r)	0.9974
Coefficient of Determination (r^2)	0.9948
Probable Error(P.E)	0.0016
6*P.E	0.0094

Source: Annexure I

Table 4.18 shows coefficient of correlation between total deposits and credit of NICABL. It shows high degree of relationship between the two variables. The coefficient of correlations, coefficient of determination, PE and 6P.E of NICABL are 0.9974, 0.9948, 0.0016, 0.0094 respectively. Coefficient of Correlation between deposit and credit is highly significant as correlation (r) of NICABL is greater than 6P.E as shown in above table. Correlation of determination is 0.9948 which mean that 99.48% of change in one variable is due to the effect of another variable

ii) Coefficient of Correlation between Interest Income and Total Credit

The Coefficient of Correlation between Interest Income and Total Credit measures the degree of relationship between two variables. The value of 'r' explains whether a percentage change in credit contribute to change the same percentage of interest income or not.

Table 4.19
Correlation between Interest Income and Total Credit

Evaluation Criteria	Result
Coefficient of Correlation (r)	0.6897
Coefficient of Determination (r^2)	0.4757
Probable Error(P.E)	0.1581
6*P.E	0.9481

Source: Annexure II

The coefficient of Correlation, coefficient of determination, P.E and 6P.E are 0.6897, 0.4757, 0.1581, and 0.9481 respectively. Coefficient of Correlation is 0.6897 means that there is just a moderate correlation between interest income and total credit. 6*P.E is greater than 'r' which means that correlation is not highly significant. 'r²' shows that change in total credit will have impact on interest income by 47.57% only.

iii) Coefficient of Correlation between Non-Performing Asset (NPA) and Total Credit

The main objective of computing correlation between the two variables is to find out whether NPA increases/decreases in proportion of increase/decrease of loans & advances.

Table 4.20
Correlation between NPA and Total Credit

Evaluation Criteria	Result
Coefficient of Correlation (r)	0.9803
Coefficient of Determination (r ²)	0.961
Probable Error (P.E)	0.0118
6*P.E	0.071

Source: Annexure III

Coefficient of Correlation is 98.03% which shows that there is high degree of correlation between NPA and Total Credit. If credit increases, NPA also increases and vice-versa. Correlation (r) is greater than 6P.E therefore it is significant. The correlation of determination between the two variables is 0.961 which means 96.1% of total change in the NPA is affected by change in total credit.

iv) Coefficient of Correlation between Loan Loss Provision (LLP) and Total Credit

The Coefficient of Correlation between LLP and Total Credit measures the degree of relationship between two variables.

Table 4.21

Correlation between LLP and Total Credit

Evaluation Criteria	Result
Coefficient of Correlation (r)	0.9577
Coefficient of Determination (r^2)	0.9173
Probable Error (P.E)	0.0249
6*P.E	0.1497

Source: Annexure IV

The above table shows that NICABL has significant value of 'r' since its value is greater than the value of 6*P.E. Hence there is positive relationship between loan loss provision and total loans and advances. If credit increases, LLP also increases and vice-versa. The correlation of determination between the two variables is 0.9173 which means 91.73% of total change in the LLP is affected by change in total credit.

v) Coefficient of Correlation between Loan Loss Provision (LLP) and Non-Performing Asset (NPA)

Table 4.22

Correlation between LLP and NPA

Evaluation Criteria	Result
Coefficient of Correlation (r)	0.9996
Coefficient of Determination (r^2)	0.9991
Probable Error(P.E)	0.0003
6*P.E	0.0016

Source: Annexure V

The coefficient of correlations, coefficient of determination, PE and 6P.E of NICABL are 0.9996, 0.9991, 0.0003, 0.0016 respectively. Coefficient of Correlation between LLP and NPA is highly significant as correlation (r) of NICABL is greater than 6P.E as shown in above table. Correlation of determination is 0.9948 which mean that 99.48% of change in one variable is due to the effect of another variable.

4.4 Major Findings of the Study

- Percentage of Non-performing Assets to Total Loan is consistently below 1% for FY 2065/66 to 2068/69. This demonstrates a very strong asset quality of the bank. However in FY 2069/70 post-merger, it appears that due to the credit quality as demonstrated by Non-Performing Asset Level of the Bank of Asia (Nepal) Ltd., the overall Non Performing Loan to Total Loan ratio has jumped to 2.32%. Hence there lies a challenge to the Bank to manage and streamline its NPA portfolio post-merger.
- Capital to Total Deposit Ratio of NICABL is more or less stable with a fluctuation of around 1% from FY 2065/66 to 2069/70. It means that the capital position in relative to deposit has slightly improved and is at an average of around 12.90% for the review period thus enhancing stability position of the Bank. This ratio reflects capital coverage for the depositors and the higher ratio increases comfort of the deposit holders.
- The Deposits of NICABL are in increasing trend over the review period as shown in Table 4.14. Deposit has rose from Rs. 15579.93 million in 2065/066 to Rs. 39908.77 million till 2069/070. This is an increase of Rs.24328.84 million in the period of five years. A cumulative average growth rate (CAGR) of about 21% on deposits has been witnessed during the review period. It appears that NICABL has been performing well in terms of Deposit by meeting the requirement of the depositors.
- The Deposit, Loan & Advances and Investment of NICABL are in increasing trend over the review period. However in Fiscal Year 2069/70 ,abnormal growth/increase in Deposit, Loans and Investment has been observed which is on account merger for Bank of Asia with NIC Bank Limited
- The interest rate spread is observed to be in increasing trend except in FY 068/069 and 69/70. The higher interest rate spread indicate that depositors are getting lower interest rate while borrowers are being punished with high interest charge curtailing the flow of loans to the export and industrial sectors or other productive projects. This situation retards the pace and process of economic development.
- Although NICABL has complied statutory requirement of Lending on deprived sector, it has sanctioned merely average of 3.91% of its lending to deprived sector.
- Core Capital of NICABL has been observed 10.48%, 11.25%, 11.34% & 9.91% and 12.21% of total risk asset as of Ashad 2066 to Ashad 2070 respectively.

- Capital Adequacy Ratio in terms of capital fund is at 12.42%, 12.92%, 12.89% 11.01% and 13.17% respectively of total risk asset in the review period of Ashad 2066- to Ashad 2070. It clearly gives sense that NICABL has complied NRB directive of capital adequacy ratio in all the years.
- Development of effective risk assessment and monitoring systems will help in improving the quality of credit decisions thereby reducing loan losses on an ongoing basis and thus gradually improving the quality of loan portfolio which is adopted by the NICABL in effective way.
- NIC Asia Bank offers as a full-fledged Commercial Bank, they provides services to clients such as : Credit and Advances, Consortium Finance, Working Capital Credit, Term Credit, Demand Credit, Trade Finance (Import/ Export), Hire Purchase, Credit and Letter of Credit, Bills Purchases, Bank Guarantee and others. Bank's major objectives are as to maximize the wealth of shareholders, to provide modern services to its customers, to help the monetary policy taken by the central bank 'NRB' and ultimately to help to reduce poverty in the country.

CHAPTER V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

Banking sector plays an important role in the economic development of the country. Commercial banks are one of the vital aspects of this sector, which deal in the process of channelizing the available resources in the needed sectors. It acts as the intermediary between the deficits and surplus of financial resources.

NICABL has started its operation from July 21, 1998 with the objective of extending professionalized banking services to various sections of the society in the kingdom of Nepal and thereby contribute to the economic development of the country.

NICABL has been promoted by some of the prominent business houses of the country. At present NICABL has been successfully operating 35 branches all over Nepal. Post-merger with Bank of Asia Nepal Ltd. number of Branches in operations has reached 53 and 14 Branches are in pipeline for relocation.

NIC Asia Bank Limited with its concept of mass banking has a broader view to reach the borrowers within its reach thus increasing financial accessibility of the people. The bank is committed to provide products and services as per the needs of the customers. The bank has different schemes of products and services as compared to other commercial banks. NICABL is the pioneer and front-runner in retail lending introducing Direct Housing Finance, Vehicle Loan Scheme, Education Loan Scheme, Loan against Future Lease Rentals and Loan against Lease Rentals of the properties.

The central focus of commercial banking concerns the acquisition and servicing of loans. A bank mobilizes deposits and lends to businesses. Banks lend or invest up to 70 – 80% of their deposits. Indeed, commercial banks are the primary, if not only, source of loans for most small and medium-sized business firms and provide vital service to business organizations and to the

community as a source of loans. There is a risk involved in lending the money. With the opening up of the economy rapid changes are taking place in the technology and financial sector exposing banks to greater risks. The well managed bank must institute loan policies designed to ensure that adequate control exists in the approval and disbursement of loans and that outstanding loan are monitored so as to ensure compliance with terms of the loan and ultimate repayment of principal and interest.

The basic objectives of the study are to examine the existing policies and practices of credit management during the loan processing and appraisal of the loan. The research is based on a case study and is descriptive in nature. Being a case study, the research is mainly focused on the primary data and the information provided by the Bank. The data was obtained through various interviews, experience and formal and informal discussion with the personal of NICABL. Secondary data was also used for the study. The secondary sources include data obtained through journals, annual reports, bulletins, web sites and various other sources.

5.2 Conclusion

Bank is a resource mobilizing institution, which accepts deposit from the various sources and invest such accumulated resources in the fields of agriculture, trade, commerce, industry, tourism etc. The commercial bank has its own role and contribution and it is a source for economic development. It maintains economic confidence of various segments and extends credit to people. Now the role of bank is not only limited to the lending. It has also extended its business to remittance - non fund based business where the bank can generate income without lending to borrowers. However, the income generated from the fund based business cannot be ignored as it covers more than 70% of the total income of the bank.

Credit activity is the integral part of banking business. Detailed information on various aspects of credit activities and the system implemented by the bank has to be included during the process of loan sanction in order to minimize risk inherent with it. It is crucial for a banking institution to lay down clearly defined systems and procedures for conducting its day to day operations. It is still more crucial that the laid down systems and procedures are meticulously compiled with by all concerned.

Based on the entire study and findings some conclusions have been made. This study particularly deals with conclusion about credit management banking system and information flows.

- NIC Asia Bank Limited appears more focused on fund based income rather than non fund based and others. The major portion of the bank's income is generated through the interest earned from the loan and advances. This is apparent from the review of interest income as a % of total income, which is ever increasing.
- Despite in increase in number of commercial banks, the growth of loan and advances of NICABL is up to mark. The bank is also maintaining low non-performing loans amongst the commercial banks. This shows good credit management practices at NIC Asia Bank Limited. The bank has zero tolerance and complies strictly every rules and regulation. All possible steps are taken to strengthen the pre sanction appraisal of the loan – "Prevention is better than Cure".
- The increasing interest income on Loans and advances over the volume of Loans & Advances indicate that the bank has been able to command high interest rate year on year thus increasing profitability and stability of the Bank.
- The loan proposal processed and the lending criterion of the bank is very comprehensive and robust which is commensurate to the size and complexity of credit volume of the Bank. The Bank has separate credit risk management function which is independent of the Business. This has caused accumulation of quality assets in the Bank's portfolio.

5.3 Recommendations

Information is the life blood of any organization. The value of it cannot be ignored. It's only by the help of information that keeps any organization up to date with the present scenario and prepares for the future comings.

Based on the entire research work, some suggestions have been recommended to be adopted by the bank.

- The ratio of non performing loans on total loans of the bank among others highlights the sound credit management of the bank. Although low, there are still outstanding non performing loans of the bank. The bank should take the optimum advantage from Debt

Recovery Tribunal (DRT) in order to minimize non-performing loans specially those at higher provisioning.

- The bank has made average lending of 3.91% on deprived sector. This is well within the statutory requirement however it should endeavor to obtain higher exposures to promote its social liability to the lower segment of the economy. Also Bank has extended its deprived sector lending via intermediaries and no direct exposure has been observed. It is suggested that having regards to long term requirement, self-exposures needs to be taken to understand and gain expertise in this segment.
- The bank may consider introducing credit card facility to its customers. It helps to increase the lending portfolio as well as meet diverse requirement of the customers.
- As the bank is fully computerized, it should take full advantage of it. The support module available in the Core Banking system has not been fully utilized by the bank. The module should be made in operation in order to gain competitive edge.
- Yield on advances are observed to be in increasing trend and no commensurate to increase in cost of deposits. Although this is good for the short run, customers may find the pricing expensive or only customers of high risk grade may come to the Bank which is not desirable at all. The Bank should review its current pricing and also focus on Non-Interest income source for the longer run.
- In order to be competitive in the market and provide better facility to the customer the bank should speedily process the loan application received and notify the concerned customer in case of loan rejection duly assigning the reasons for such rejection.

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ANNEXURES

Annexure I

Computation of Correlation between Total Deposit and Total Credit

Year	Total Deposit (X)	Total Credit (Y)	X^2	Y^2	XY
2065/066	15,579.93	13,679.39	242,734,218.80	187,125,710.77	213,123,938.64
2066/067	15,968.91	12,732.01	255,006,086.59	162,104,078.64	203,316,321.81
2067/068	18,394.43	14,933.93	338,355,055.02	223,022,265.24	274,701,130.01
2068/069	22,111.85	17,242.30	488,933,910.42	297,296,909.29	381,259,151.26
2069/070	39,908.77	31,559.51	1,592,709,922.91	996,002,671.44	1,259,501,225.90
Total	111,963.89	90,147.14	2,917,739,193.75	1,865,551,635.39	2,331,901,767.62

We have,

$$N=5 \quad \sum X = 111963.89 \quad \sum Y = 90,147.14 \quad \sum X^2 = 2,917,739,193.75$$

$$\sum Y^2 = 1,865,551,635.39 \quad \sum XY = 2,331,901,767.62$$

Correlation Coefficient can be computed using following formula:

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

$$\text{Coefficient of Correlation (r)} = 0.9974$$

$$\text{Coefficient of Determination (r}^2\text{)} = 0.9948$$

Calculation of Probable Error (P.E)

$$P.E = 0.6745 \frac{1-r^2}{\sqrt{N}}$$

$$\text{Therefore P.E} = 0.0016$$

$$\text{Now } 6 * P.E = 6 * 0.0016 = 0.0094$$

Annexure II

Computation of Correlation between Interest Income and Total Credit

Year	Interest Income (X)	Total Credit (Y)	X^2	Y^2	XY
2065/066	1,283.52	13,679.39	1,647,423.59	187,125,710.77	17,557,770.65
2066/067	1,777.16	12,732.01	3,158,297.67	162,104,078.64	22,626,818.89
2067/068	2,321.40	14,933.93	5,388,897.96	223,022,265.24	34,667,625.10
2068/069	2,431.53	17,242.30	5,912,338.14	297,296,909.29	41,925,169.72
2069/070	2,663.45	31,559.51	7,093,965.90	996,002,671.44	84,057,176.91
TOTAL	10,477.06	90,147.14	23,200,923.26	1,865,551,635.39	200,834,561.27

We have,

$$N=5 \quad \sum X = 10,477.06 \quad \sum Y = 90,147.14 \quad \sum X^2 = 23,200,923.26$$

$$\sum Y^2 = 1,865,551,635.39 \quad \sum XY = 200,834,561.27$$

Correlation Coefficient can be computed using following formula:

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

$$\text{Coefficient of Correlation (r)} = 0.6897$$

$$\text{Coefficient of Determination (r}^2\text{)} = 0.4757$$

Calculation of Probable Error (P.E)

$$P. E = 0.6745 \frac{1-r^2}{\sqrt{N}}$$

$$\text{Therefore P.E} = 0.1581$$

$$\text{Now } 6 * P.E = 6 * 0.1581 = 0.9489$$

Annexure III

Computation of Correlation between NPL and Total Credit

Year	NPA(X)	Total Credit (Y)	X ²	Y ²	XY
2065/066	129.17	13,679.39	16,684.89	187,125,710.77	1,766,966.81
2066/067	92.49	12,732.01	8,554.40	162,104,078.64	1,177,583.60
2067/068	90.35	14,933.93	8,163.12	223,022,265.24	1,349,280.58
2068/069	128.54	17,242.30	16,522.53	297,296,909.29	2,216,325.24
2069/070	752.34	31,559.51	566,015.48	996,002,671.44	23,743,481.75
Total	1,192.89	90,147.14	615,940.42	1,865,551,635.39	30,253,637.98

We have,

$$N=5 \quad \sum X = 1,192.89 \quad \sum Y = 90,147.14 \quad \sum X^2 = 615,940.42$$

$$\sum Y^2 = 1,865,551,635.39 \quad \sum XY = 30,253,637.98$$

Correlation Coefficient can be computed using following formula:

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

$$\text{Coefficient of Correlation (r)} = 0.9803$$

$$\text{Coefficient of Determination (r}^2\text{)} = 0.961$$

Calculation of Probable Error (P.E)

$$P.E = 0.6745 \frac{1-r^2}{\sqrt{N}}$$

$$\text{Therefore P.E} = 0.0118$$

$$\text{Now } 6 * P.E = 6 * 0.0118 = 0.071$$

Annexure IV

Computation of Correlation between LLP and Total Credit

Year	LLP (X)	Total Credit (Y)	X ²	Y ²	XY
2065/066	96.79	13,679.39	9,368.30	187,125,710.77	1,324,028.16
2066/067	68.92	12,732.01	4,749.97	162,104,078.64	877,490.13
2067/068	80.82	14,933.93	6,531.87	223,022,265.24	1,206,960.22
2068/069	106.93	17,242.30	11,434.02	297,296,909.29	1,843,719.14
2069/070	540.01	31,559.51	291,610.80	996,002,671.44	17,042,451.00
Total	893.47	90,147.14	323,694.97	1,865,551,635.39	22,294,648.64

We have,

$$N=5 \quad \sum X = 893.47 \quad \sum Y = 90,147.14 \quad \sum X^2 = 323,694.97$$

$$\sum Y^2 = 1,865,551,635.39 \quad \sum XY = 22,294,648.64$$

Correlation Coefficient can be computed using following formula:

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

$$\text{Coefficient of Correlation (r)} = 0.9577$$

$$\text{Coefficient of Determination (r}^2\text{)} = 0.9173$$

Calculation of Probable Error (P.E)

$$P.E = 0.6745 \frac{1-r^2}{\sqrt{N}}$$

$$\text{Therefore P.E} = 0.0249$$

$$\text{Now } 6 * P.E = 6 * 0.0249 = 0.1497$$

Annexure V

Computation of Correlation between LLP and NLP

Year	LLP (X)	NPA(Y)	X ²	Y ²	XY
065/066	96.79	129.17	9,368.30	16,684.89	12,502.36
066/067	68.92	92.49	4,749.97	8,554.40	6,374.41
067/068	80.82	90.35	6,531.87	8,163.12	7,302.09
068/069	106.93	128.54	11,434.02	16,522.53	13,744.78
069/070	540.01	752.34	291,610.80	566,015.48	406,271.12
Total	893.47	1,192.89	323,694.97	615,940.42	446,194.77

We have,

$$N=5 \quad \sum X = 893.47 \quad \sum Y = 1,192.89 \quad \sum X^2 = 323,694.97$$

$$\sum Y^2 = 615,940.42 \quad \sum XY = 446,194.77$$

Correlation Coefficient can be computed using following formula:

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

Coefficient of Correlation (r) = 0.9996

Coefficient of Determination (r²) = 0.9991

Calculation of Probable Error (P.E)

$$P. E = 0.6745 \frac{1-r^2}{\sqrt{N}}$$

Therefore P.E = 0.0003

Now 6*P.E = 6*0.0003 = 0.0016