

# CHAPTER-1

## INTRODUCTION

### 1. Background of the Study

Overall national development of any country depends upon the economic development of that country and economic development largely depends upon the financial infrastructure of the country. Financial infrastructure is the set of institutions that enable effective operation of financial intermediaries. This includes such elements as payment systems, credit information bureaus and collateral registries. Therefore, the primary goal of any nation including Nepal is rapid economic development to promote the welfare of the people and the nation as well. Nepal being one of the least developed countries has been trying to embark upon the path of economic development by economic growth rate and developing all of economy. A commercial bank is a profit- based financial institution that grants loans, accepts deposits, and offers other financial service, such as overdraft facilities and electronic transfer of funds. A commercial bank can be viewed as a special business which has its products are not physical goods but credit and currencies. Customers of a commercial bank are usually from commercial classes. The main functions of the bank are taking deposits, lending, creating of credit, clearing of cheques, financing international trade and settling funds (Somasherkar,2009).

Economic development of a country. Similarly, integrated and speedy development of the country is only possible when competitive and reliable banking service are reached and operated to every corner of the country. It has been well established that the economic activities of any country can hardly be carried without the assistance and support of financial institutions. A financial institution is an establishment that conducts financial transactions such as investments, loans and deposits. financial institutions on a regular basis. Everything from depositing money to taking out loans and exchanging currencies must be done through financial institutions. financial institutions have catalytic role in the process of economic development. The investment policy of financial institutions, especially banks has long term impact not only on their growth and sustainability but also on the economic development of the country. Successful formulation and effective implementation of investment policy is

the prime requisite for the successful performance of banks and other financial institutions. Good investment policy has a positive impact on economic development of the country and vice-versa.

Commercial bank is a financial institution which transfers monetary sources to users. In the process of such intermediation, commercial bank deploys funds raised from different sources into different assets with prime objective of profit generation and administrative assistance. According to Commercial Bank Act 2031, "Commercial banks are those banks which are established under this act to perform commercial function." The commercial banks pool together the savings of the community and arrange for their productive uses. They supply financial needs of modern business.

The commercial bank has its own role and contribution in the economic development. The general role of commercial banks is to provide financial services to general public, business and companies, ensuring economic and social stability and sustainable growth of the economy. In this respect, "credit creation" is the most significant function of commercial banks. Liu (2004) explain that Commercial banks are "institutions which use the funds entrusted to them by their customer to extend loans to consumers and business customers and distribute profits to the banks shareholders".

Banking sector in Nepal has been boosted up recently with mushrooming new Banks and financial institution appearing day by day in the economic market. Banking in Nepal is highly strengthen by private sector Banks and financial institution.

Banking was first started in Nepal after establishment of Nepal Bank limited (NBL) in 1937. Commercial Banking was a new thing for the community but the establishment of NBL had initiated the banking in Nepal. At present banks in Nepal are mushrooming. Here is name list of all the 'Class A' commercial banks in Nepal. Commercial banks in Nepal are playing vital roles to collect money in the state. Nepal has many nationalized and private banking ventures. There are 28 commercial banks of Nepal. There are enlisted 28 list of licensed commercial banks of Nepal.

**Table :1.1**  
**List of commercial banks**

S.No.	Name	Operation Date(A.D.)	Head Office	Paid Up Capital in NRS Crore
1.	Nepal Bank Ltd.	15-11-1937	Dharmapath, Kathmandu	649.95
2.	Rastriya Banijya Bank Ltd.	23-01-1966	Singhadurbarplaze, Kathmandu	859.9
3.	Agriculture Development Bank Ltd.	21-01-1968	Ramshahpath, Kathmandu	1037.4
4.	NABIL Bank Limited.	12-07-1984	Beena Marg, Kathmandu	618.35
5.	Nepal Investment Bank Ltd.	09-03-1986	DurbarMarg, Kathmandu	870.66
6.	Standard Chartered Bank Nepal Ltd.	28-02-1987	Nayabaneshwor, Kathmandu	374.99
7.	Himalayan Bank Ltd.	18-01-1993	Kamaladi, Kathmandu	449.91
8.	Nepal SBI Bank Ltd.	07-07-1993	Kesharmahal, Kathmandu	388.37
9.	Nepal Bangladesh Bank Ltd.	06-06-1994	kamaladi, Kathmandu	401.18
10.	Everest Bank Ltd.	18-10-1994	Lazimpat, Kathmandu	274.26
11.	Kamari Bank Ltd.	03-04-2001	Durbarmarg, Kathmandu	269.92
12.	Laxmi Bank Ltd.	03-04-2002	Hattisar, Kathmandu	303.92
13.	Citizens Bank International Ltd.	20-04-2007	Kamaladi, Kathmandu	553.74
14.	Prime Commercial Bank Ltd.	24-09-2007	Newroad, Kathmandu	489.19
15.	Sunrise Bank Ltd.	12-10-2007	Gairidhara, Kathmandu	530.14
16.	Janata Bank Nepal Ltd	05-04-2010	Naya Baneshwor, Kathmandu	206
17.	Mega Bank Nepal Ltd.	23-07-2010	Kantipath, Kathmandu	401.2
18.	Century Commercial Bank Ltd.	10-03-2011	Putalisadak, Kathmandu	368.9
19.	Sanima Bank Ltd.	15-02-2012	Nagpokhari, Kathmandu	530.59
20.	Machhapuchhre Bank Ltd.	09-07-2012	New Road, Pokhara, Kaski	386.45
21.	NIC Asia Bank Ltd.	30-06-2013	Thapathali, Kathmandu	581.96
22.	Global IME Bank Ltd.	09-04-2014	Panipokhari, Kathmandu	616.43
23.	NMB Bank Ltd.	18-10-2015	Babarmahal, Kathmandu	543.01
24.	Prabhu Bank Ltd.	12-02-2016	Babarmahal, Kathmandu	88.14
25.	Siddhartha Bank Ltd.	21-07-2016	Hattisar, Kathmandu	302.21

26.	Bank Of Kathmandu Lumbini Ltd.	14-07-2016	Kamaladi, Kathmandu	458.38
27.	Civil Bank Ltd.	17-10-2016	Kamaladi, Kathmandu	458.38
28.	Nepal Credit and Commerce Bank Ltd.	01-01-2017	Siddharthanagar, Rupendehi	467.91

Source: Nepal Rastra Bank

Bank and Financial Institutions Act (BAFIA) 2064 has defined commercial bank as organization which exchange money, accept deposit, grant loan and perform commercial banking functions and which is not a bank meant for cooperative, agriculture, industries or for such specific purpose. The Basel committee also raises an issue concerning the application of the risk weights used in the capital adequacy framework to determine exposure to risk assets for the purpose of determining large credit exposure (Morris, 2001).

The negative effects of loans default has caused financial institutions to reconsider their internal controls, loan appraisal and loan risk management policies to decrease the increasing rate of credit default. Executive Secretary of Ghana Bankers Association, Mensah (2011) stated that the increasing rate of loan default in the accounts of the financial institutions is causing problems among the institutions and industry watchers. Loans management refers to the effective use of the four major credit policy variables to ensure that there is quick collection of loan given to borrowers when due and at the same time improve on their confidence and loyalty to the bank (Van Horne, 1995).

Myers and Brealey (2003) defined credit as a process whereby possession of goods or services is allowed without spot payment upon a contractual agreement for later payment. The loan should be recoverable and adequate for the reason why it is granted. There should be sufficient information readily available for effective credit assessment. Financial institutions are faced with enormous difficulties in managing their credit loss reserves as of result terrible loans and bad credit management process used by the financial institutions. For this reason a lot of the financial institutions have been left in debt and could soon cease operation if serious measures are not put in place to turn around the situation. Lending is one of the major functions of banking institution. Through this work, banks affect the economic growth and stability in the

economy. Although credit growth can spur investment and economic activity, an excessive growth in credit can impact the price stability as well as stability of the financial system by increasing prudential risks at the micro and macro levels (Igan & Pinheiro, 2011).

### **s1.2 Profile of the Sample Bank**

As there have been 28 numbers of commercial banks established in our country, the research has been taken into consideration of Everest Bank Ltd and Nepal Investment Bank Ltd. Therefore, short introduction of these sample commercial banks are given as:

#### **Everest Bank Limited**

Everest bank limited is the commercial bank of Nepal. Which is joint venture of Punjab National Bank, India. Punjab national bank holds 20% equity shares of Bank. This is first Nepalese Bank which have representative office in India (New Delhi) to support Nepalese citizen remitting money and advising banking related services. Founded in 1994, the bank has been one of the lending banks of the country and catering its services to various segments of the society.

Everest Bank Limited (EBL) provides customer-friendly services through its wide Network connected through ABBS system, which enables customers for operational transactions from any branches. The bank has 80 Branches, 113 ATM Counters, 7 extension counter & 28 Revenue Collection Counters across the country making it a very efficient and accessible bank for its customers, anytime, anywhere. EBL offers a wide range of products and services designed to make banking easier and to match each and every customer's requirements. EBL provide internet user login for this account incase of single signatory.

#### **Vision**

“To be a Leading Commercial Bank with Pan Nepal presence and become a household name, providing wide range of financial products and services under one roof”

## **Nepal Investment Bank Limited**

Nepal Investment Bank Limited is one of the leading commercial banks of Nepal. Previously known as Nepal Indosuez Bank Ltd., the bank was established in 1986 as a joint venture between Nepalese and French partners in 21<sup>st</sup> January 1986 under the Company Act 1964. The Nepalese investors bought all the shares of French company i.e. 50% in 2001. From then the Nepalese investors have raised this bank to one of the most trusted and popular bank in the country. Till date it has 66 branches, 4 Extension Counters (98 ATM outlets) scattered throughout the country giving modern banking services of international class from 9:30am to 7pm evening. A group of companies comprising of Nepalese businessmen, professional bankers and industrialists acquired the fifty percent of the shareholding of Credit Agricole Indosuez in Nepal Indosuez Bank Ltd on April 2002 with the decision of the latter.

The shareholding of the bank is distributed in a way that a group of companies holds fifty percent of its capital, Rastriya Banijya Bank and Rastriya Beema Sansthan holds fifteen percent each and the remaining twenty percent shares is held by the general public that makes Nepal Investment Bank Limited listed on the NEPSE. The services it provides include ABBS, deposit, saving accounts, internet banking, remittance, ATM cards, debit cards, credit cards, different types of loan, utility payments, mobile phone recharge, phone bill payments, locker services, etc. It is also the only bank in Nepal from where you can withdraw hundred rupees (from its ATM) unlike other bank's ATM that has Rs 500 notes as minimum amount allowed for withdrawal.

## **Vision**

“Our Vision is to be the most preferred provider of Financial Services in Nepal”

### **1.3 Statement of the Problems**

Commercial banks in Nepal have been facing many problems and challenges. Some of them arising due to the economic condition of our country, some of them arising due to confused about the government policy and many of them due to the default nature of borrowers. Loan management is basically taking care of the repayments. The success of loan is not much dependent on the amount of loan but in the kind of discipline and system of the repayment process.

After the liberalization of economy, banking sector has various opportunities. Banks are investing in many sectors like home loan, hire purchase loan, agriculture loan. Lack of lending opportunities, bank face problem of over liquidity. Loan management is the essence of commercial banking; consequently, the formulation and implementation of sound policies are among the most important responsibilities of directors and management. Well-conceived lending policies and careful lending practices are essential if a bank is to perform its credit. Loan management effects on the company's profitability and liquidity so it is one of the crucial decisions for the commercial banks. The need of financial resources in a developing country like Nepal is essential for the economic development of country. The reliability of commercial banks has been treated as one of the essential factors everywhere since the past few decades. In order to draw global attention for dynamic investments in a competitive international business environment, healthy and efficient commercial banks are needed. The proficient commercial banks help to boost the effectiveness of the economy condition. Commercial lending in Nepal is governed under the Commercial Bank Act of 1974, the Finance Company Act of 1985, and the Bank and Financial Institutions Act of 2006, which authorizes the NRB to issue guidelines to all commercial banks and financial institutions on interest rates, interest ceilings, and areas of investment. The regulatory part of the banks and financial institutions, NRB formulate policy for purpose of efficient lending and credit loss provision.

In this perspective this study has tried to address the following research questions.

1. How effectively these selected banks have followed lending policies and practices?
2. What is the trend of liquidity, deposit and loans of selected commercial banks?
3. What is the financial performance (EPS) of selected commercial bank?
4. What is the impact of deposit, total assets and investment (loan management) on loan and advances?

#### **1.4 Purpose of the Study**

The general purpose of this study is to analyse and evaluate the loan management of commercial banks in Nepal. The objectives of this study has been categorized.

1. To assess loan management process, system and practices of selected banks.
2. To examine the trend of liquidity, deposit and loans of selected commercial banks.
3. To evaluate the financial performance(EPS) of selected commercial banks.
4. To examine the impact of deposit, total assets and investment (loan management) on loan and advance.

#### **1.5Significance of the Study**

A commercial bank is a financial institution that is authorized by law to receive money from businesses and individuals and lend money to them. Commercial banks are open to the public and serve individuals, institutions, and businesses. Commercial bank in Nepal are operating their services by many channels from urban to rural by their different services.

Research made especially on Loan management of commercial bank couldn't be found. This study too is made under the guidelines of the previous researches made on commercial banks, which too very few in numbers. As this research is made mainly to analyze the loan and their management in reference to NRB directives and measures, it will provide valuable insight to different stakeholders about the major problems of banks and bank's action for its management. More than that, this can provide adequate information about overall trend of commercial bank to the shareholders, investors, professionals and also to the students and teachers of commerce.

The presentation of this study will also help to clear out misconceptions people have about commercial banks regarding their trustworthiness. Besides, this comparative study of loan management of commercial bank is probably the first attempt of its kind so it is going to be of an important value for the people interested in this field.

This study will be also useful to various parties such as researcher, students, teachers, financial institutions, investors, business organizations, and general individual to get

some useful information about commercial bank loan management system. More than all, myself being a commerce student and also interested in commercial bank this study will prove to be very important in my individual level, for my career in the up growing and challenging field of commercial bank.

### **1.6 Limitations of the Study**

The outcome of the study is an individual effort. The study focuses the sensitive part of the financial institutions which resultants the management a little bit hesitation to come up with open view regarding the loan management and provision method. Therefore, the study has been conducted on the basis of annual reports of selected commercial bank, published and unpublished material, NRB publications, and interview with the bankers and my personal judgment. This research has following limitations.

1. The evaluation is made through the analysis of financial statement published and presented by the banks. Therefore, generalization of the whole banking industry cannot be made.
2. The data used are all secondary. The annual reports published by the respective companies are the major data used for the analysis in the study. Besides those, reports published by NRB, articles, journals, and news published are used as the source of data. Thus, any miss presentations, mistakes and omissions affect the outcome of the study.
3. Since the study was made for fiscal year 2009/10 to 2016/17 only and the performances of others years ignored, this might not give the accurate picture. And the trend analysis might not be correct too.
4. This study includes only two commercial banks. That may not representative to other study.

### **1.7 Organization of the Study**

The study has been organized into five chapters. They are as follows:

**Chapter I: Introduction**

The first chapter presents a brief introduction of the study. Which has covered background of the study, focus of the study, statement of problem, objectives of the study, significance of the study.

**Chapter II: Review of Literature**

This chapter has included conceptual framework i.e. theoretical analysis and review of related different studies. In this chapter, it has been attempted to show how this present study is different from previous studies.

**Chapter III: Research Methodology**

This chapter has dealt with the research design, population and sample, sources of data, data collection techniques and data analysis tools (financial tools and statistical tools) and methods of analysis and presentations.

**Chapter IV: Result**

This chapter presents analysis and interpretation of data of related topic based on annual reports of sample banks. It has included secondary data and primary data presentation, data analysis, interpretation, testing of hypothesis and major findings.

**Chapter V: Conclusion**

The last chapter states the summary, conclusion of the whole study and recommendations. It also offers several avenues for future research and the reference, appendices have also incorporated at the end of the study.

## CHAPTER-II

### REVIEW OF LITERATURE

Review of literature is a critical summary of research on a topic of interest, generally prepared to put a research problem in context or to identify gaps and weaknesses in prior studies so as to justify a new investigation. A literature review is both a summary and explanation of the complete and current state of knowledge on a limited topic as found in academic books and journal articles. A literature review surveys books, scholarly articles, and any other sources relevant to a particular issue, area of research, or theory, and by so doing, provides a description, summary, and critical evaluation of these works in relation to the research problem being investigated. Literature reviews are designed to provide an overview of sources to have explored while researching a particular topic and to demonstrate to the readers how research fits within a larger field of study. The literature review may also identify gaps or controversies in the literature and topics needing further research.

Review the literature from the available sources like library, internet, book, journal, research papers and dissertations. It has been categorized into two groups:

- Conceptual framework
- Review of empirical study

#### **2.1 Conceptual Framework**

##### **2.1.1 Concept of Bank**

A bank is an organization, which deals with money and credit. The bank may be a company, firm, business, organization or person, which is involved in lending and borrowing activities. In modern term, we cannot say that bank activities are limited to just borrowing and lending. This is a very primitive concept. In modern concept, the bank is an institution that deals in monetary transactions. Monetary transactions mean dealing in money and credit. When not necessarily motivated by the public good, such restrictions probably made banks safer by giving them franchise value and enhance transaction possibilities between banks and their clients (Keeley,1990).

### 2.1.2 Concept of Commercial Banks

Commercial banks are an institution which accepts deposits, makes business loans, and offers related services. Commercial banks also allow for a variety of deposit accounts, such as checking, savings and time deposit. These institutions are run to make a profit and owned by a group of individuals. In Nepal, Nepal Rastra Bank is the central bank of Nepal. NRB the governing body of banking and financial institution has categorized the bank and financial institution in four distinct categories. i.e. 'A' Class' 'B' Class, 'C' Class and 'D' Class institutions. Commercial banks are categorized under A class banks in Nepal. A commercial bank can also refer to a bank, or a division of a large bank, which more specifically deals with deposit and loan services provided to corporations or large/middle-sized business – as opposed to individual members of the public/small business.

The bank have to evaluate the risk, which it face daily while lending (Mohammad, 2014). Banks involves continuously in corporate governance to monitor, screen and recovery of loan for better performance of loan (Mohammad, 2014). Performance of commercial banks influences economic growth positively.

“Commercial banks are those banks which are established under this act to perform commercial functions except those which are established for specific purposes like development, cooperatives etc.”- Commercial Bank Act, 2031

### 2.1.3Types of Commercial Bank

Commercial banks are classified into two categories i.e. **scheduled commercial banks** and **non-scheduled commercial banks**. Further, scheduled commercial banks are further classified into three types:

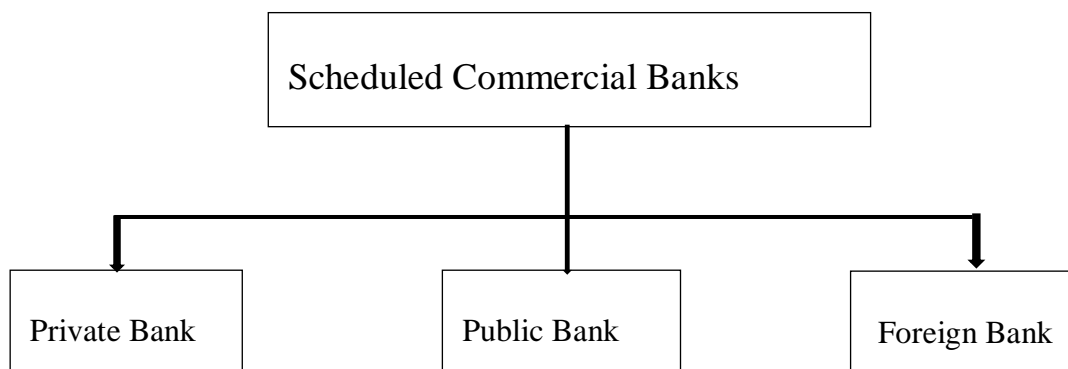


Fig 2.1: Types of schedule commercial Bank

Sources: Business Jargons

**Private Bank:** When the private individuals own more than 51% of the share capital, then that banking company is a private one. However, these banks are publicly listed companies in a recognized exchange.

**Public Bank:** When the Government holds more than 51% of the share capital of a publicly listed banking company, then that bank is called as Public sector bank.

**Foreign Bank:** Banks set up in foreign countries, and operate their branches in the home country are called as foreign banks.

#### 2.1.4 Function of Commercial Banks

Commercial bank being the financial institution performs diverse types of functions. It satisfies the financial needs of the sectors such as agriculture, industry, trade, communication, etc. The functions performed by banks are changing according to change in time and recently they are becoming customer centric and widening their functions. Generally, the functions of commercial banks are divided into two categories viz. primary functions and secondary functions. According to Nepal Rastra bank, for getting “A” grade commercial bank, the bank should have capital of 8 billion rupees.

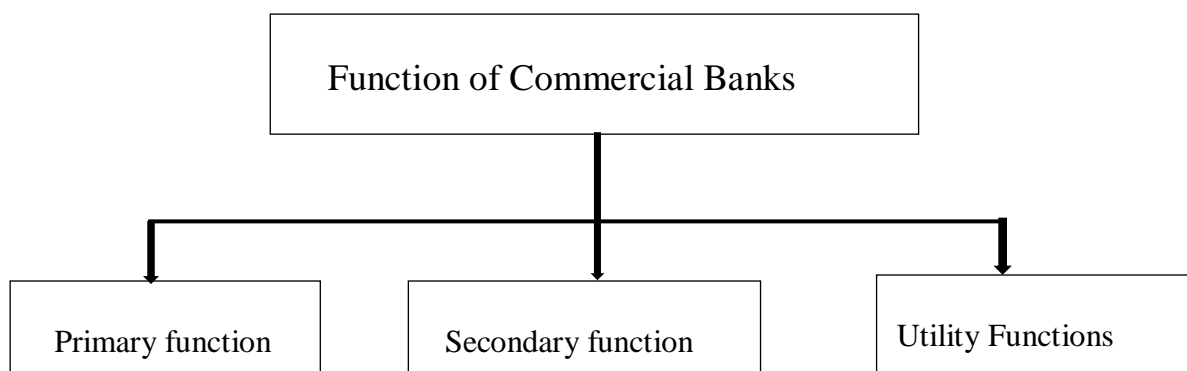


Fig2.2: Function of commercial Banks

Sources: Smriti Chand (Article)

Finance is the life blood of trade, commerce, and industry. Nowadays, banking sector acts as the backbone for modern business. Central bank of country issues notes and currencies for exchanging purpose. The bank could offer implicit promises of credit to potential borrowers, and the latter could be confident that the promises would largely be honoured (Bhattacharya &Thakor ,1995).

#### **2.1.5 Significance of Commercial Banks:**

The major function of commercial banks is to provide credit. Loan and advances constitute the highest portion of the total assets of banks. It is the main source for generating profit. In the view of Nwankwo (2000), “credit constitutes the largest single income-earning asset in the portfolio of most banks.

Commercial banks play such an important role in the economic development of a country that modern industrial economy cannot exist without them. They constitute nerve centre of production, trade and industry of a country. In the words of Wick-sell, “Bank is the heart and central point of modern exchange economy.”The significance of banks in an economy may not be eliminated as they are institutions, which provide liquidity for both lender and borrower (Kashyap,1999).

#### **The following point highlight the significance of commercial banks:**

They promote saving and accelerate the rate of capital formation.

They are source of finance and credit for trade and industry.

They promote balance regional development by opening branches in backward areas.

Bank credit enables entrepreneurs to innovate and invest which accelerates the process of economic development.

They help in promoting large-scale production and growth of priority sectors such as agriculture, small-scale industry, retail trade and export.

They create credit in the sense that they are able to give more loans and advances than the cash position of the depositor's permits.

### **2.1.6 Concept of loan**

A loan is money, property or other material goods that is given to another party in exchange for future repayment of the loan value amount along with interest or other finance charges. A loan may be for a specific, one-time amount or can be available as an open-ended line of credit up to a specified limit or ceiling amount. A loan is a kind of advance made with or without security at agreed rate of interest. It is the most profitable asset of the bank. So bank management always tries to increase loan portfolio in order to get more profit.

According to Adedoyin and Sobodun (1991), "lending is undoubtedly the heart of banking business. Therefore, its administration requires considerable skill and dexterity on the part of the bank management".

Ezirim (2005) further stressed that "bank lending decisions generally are fraught with a great deal of risks, which calls for a great deal of caution and tact in this aspect of banking operations. The success of every lending activity to a great extent therefore, hinges on the part of the credit analysts to carry out good credit analysis, presentation, structuring and reporting."

Bank loan management is crucial and it is instrumental in ensuring the success of failure of any credit institution. Ivaskeviciute, Macerinskiene and Laura (2008) has suggested that, the loan portfolio should be distributed into sub-portfolios according to activity segments of the bank: large scale projects, corporate and private clients to get more comprehensive results and loan portfolio evaluation.

Loan management is the process by which risk that is inherent in lending process are managed and controlled. It is concerned with formulating and implementing lending policies. Income and profit depends on lending and investment procedure. A sound procedure provides high return and profit. So higher the loan, higher will be profit but loan should be increased such that it is manageable. Moreover, lending and investment are important not only for bank but also to the overall economic development of the country. Loan management affects bank's profitability and liquidity. Today, credit management constitutes a critical component of a comprehensive approach to risk management in banking sector (Arora & Kumar, 2014).

Operational strength of a bank in relation to its revenue and expenditure as revealed by its financial statement in any bank deposit money, financial performance affected by loan management (Lymon & Carles, 1978).

According to Asiedu-Mante (2011) loans management includes instituting proper rightful policies and measures that will make sure that proper authorities give out loans, the loans get to the right customers, the loan is given for productive reasons which are economically viable and appropriate.

### **2.1.7 Types of Credit offered by Commercial Banks:**

A commercial bank offers short-term loans individuals and organizations in the form of bank credit, which is a secured loan carrying a certain rate of interest. Thapa and Rawal (2010) have mentioned in their book that Credit is a kind of product which can be developed on the basis of terms and conditions demanded by the credit agreement between bank and the borrower. There are various types of bank credit provided by a commercial bank, as shown in figure.

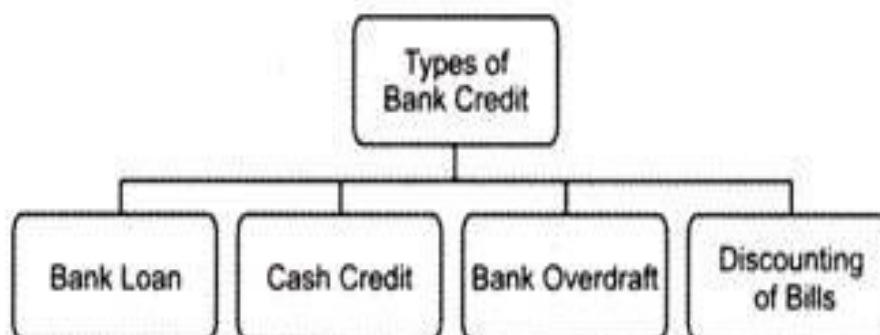


Fig 3: types of bank credit

Sources: Jan Cernohorsky, 2017

### **2.1.8 General Principles of Good Lending**

A commercial bank is an institution that provides service such as accepting deposits, providing business loans, and offering basic investment products. The main function of a commercial bank is to accept deposit from the public for the purpose of lending money to the borrowers. In between these intermediations banks earns profit from different in interest and charge paid by the borrowers. Thus the income and profit of each bank and financial institution depends upon the lending principle and policy. When a request for a loan is received, it is important to ensure that the borrower has the legal capacity to borrow. The other matters upon which the information should be obtained are: the purpose of advance, the amount involved, the duration of the advance, the source of repayment, the profitability of transaction, and where applicable, the security offered. There can be multiple aspects and arrangements by which bank can set specific policies before granting the loan to borrower (Moti, 2012).

Banks follow some fundamental principles of lending in order to ensure safety, security and profitability on money it lend. Lending is one of the most important functions performed by the commercial banks and is major source of income of bank. If financial institutions do not follow well administered collection procedures, this would result in loan defaults (Boldizzoni, 2008).

Credit risk is one of the most significant risks that banks face, considering that granting credit is one of the main sources of income in commercial banks. Therefore, the management of the risk related to that credit affects the profitability of the banks (Li & Zou, 2014).

"Commercial banks are the most important savings mobilization and financial resources allocation institution. Eventually, those roles make them an important phenomenon in economic growth and development. In order for them to perform these roles, it must be realized that banks have the potential, scope and prospects of financial intermediation" (Olokoyo 2011). Therefore, banks should pay great attention on some basic principles of lending. Borrower may differ in terms of their purpose of advance, activities, financial health, repayment capacity, risk so some important principles / considerations are followed by bank before taking lending decision.

## 1. Liquidity

Liquidity is an important principle of bank lending. Bank lend for short periods only because they lend public money which can be withdrawn at any time by depositors. They advance loans on the security of such assets which are easily marketable and convertible into cash at a short notice. A bank chooses such securities in its investment portfolio which possess sufficient liquidity. It is essential because if the bank needs cash to meet the urgent requirements of its customers, it should be in a position to sell some of the securities at a very short notice without disturbing their market prices much. Bank is considered to be liquid if the total of its liquid assets or liquid funds which it can quickly mobilize and ability of fulfilling obligations of depositors in timely (Lavrushin, 2000).

## 2. Safety:

Safety means that the borrower should be able to repay the loan and interest in time at regular intervals without default. Banks are trustee of public money. Bank's deposits are always payable on demand. As such the first and foremost principle of lending is to ensure safety of funds lent. Now the question is how to ensure safety of lending? To ensure the safety of lending the following factors may be considered:(Greenbaum & Thakor, 2007)

Five Cs	Five Ps	Five Ms	Five Rs
Character/conduct Capacity Capital Condition Collateral	Person Purpose Product Place profit	Man Management Money Materials Market	Reliability Responsibility Resources Respectability returns

## 2. Diverity

In choosing its investment portfolio, a commercial bank should follow the principle of diversity. It should not invest its surplus funds in a particular type of security but in different types of securities. It should choose the shares and debentures of different types of industries situated in different regions of the country. Diversification aims at minimising risk of the investment portfolio of a bank. A bank should follow the

maxim: “Do not keep all eggs in one basket.” It should spread its risks by giving loans to various trades and industries in different parts of the country. Regulators must be careful in endorsing diversification across multiple sectors or regions as a goal for banks and related intermediaries (Winton, 1999).

### **3. Stability**

Another important principle of a bank's investment policy should be to invest in those stocks and securities which possess a high degree of stability in their prices. The bank cannot afford any loss on the value of its securities. It should, therefore, invest its funds in the shares of reputed companies where the possibility of decline in their prices is remote. Government bonds and debentures of companies carry fixed rates of interest. Their value changes with changes in the market rate of interest. But the bank is forced to liquidate a portion of them to meet its requirements of cash in case of financial crisis. Otherwise, they run to their full term of 10 years or more and changes in the market rate of interest do not affect them much. Thus bank investments in debentures and bonds are more stable than in the shares of companies. So the principle of stability the loan also brings growth to the bank as well as the economy as a whole (Greuning & Bratonovic, 2003).

### **4. Profitability**

This is the cardinal principle for making investment by a bank. It must earn sufficient profits. It should, therefore, invest in such securities which would ensure a fair and stable return on the funds invested. Banks are not charitable institutions. All banks are profit-earning institutions. The ultimate objective of lending is to earn profits. Banks receive interest on loans and advances lent, and they pay interest to their depositors. This difference between the receipts and payments will be the bank's gross profit. Hence it is important that whatever the business the bank engages itself with, the business be profitable enough not just to cover its costs but to ensure generation of surplus funds or margin. So this study is also related to the broader financial stability literature, as bank profitability as an important predictor of financial performance (Demirguc-Kent & Detragiache, 1999).

## **5. Security**

A banker avoid lending to a borrower without any security. Security act as an insurance to lender bank in case of default by the borrower. So another principle of sound lending is the security of lending. The banker carefully scrutinizes all the different aspects of an advance before granting it. It is the duty of the banker to check the nature of the security and assess whether it is adequate for the loan granted. If the bank not consider, it may results in loan losses of high level and even failure of financial institution (Chijoriga, 2011).

## **6. purpose**

The purpose should be productive so that the money not only remain safe but also provides a definite source of repayment. Loans may be required for productive purposes, trading purposes, agriculture, transport, self-employment etc. If a loan is required for a non-productive or speculative purpose, the banker should be very much cautious in entertaining such proposals.

### **2.1.9 Some related terms of lending criteria**

#### **i) Character**

The character of a customer refers to its willingness to pay in a timely manner, usually as evidenced by its payment history. This information is available in a credit report, which is available from one of the credit bureaus. A good example of character is a business that has paid its bills when due for many years, without having had any litigation with its suppliers. Conversely, a history of late payments and litigation is a clear sign of lack of character. As to the factors that influence a client categorize them into personal, cultural, social and economic factors (Ouma, 1996).

#### **ii) Capacity**

The capacity of a customer refers to its ability to pay back a loan or credit advance. A high level of capacity is evidenced by a history of strong positive cash flow and a reasonable ratio of liabilities to cash flow. An additional issue is whether the

customer's projected circumstances will change enough to alter its current cash flow or liquidity position. Various approaches have been created in customer evaluation for capacity which run from generally straightforward (Horcher, 2005).

### **iii) Capital**

The capital of a customer is its net worth which is the residual amount of assets left after all liabilities have been subtracted. For capital analysis, financial statements, like certified balance sheet, profit and loss account is the only tools.

### **iv) Collateral**

Collateral refers to the ability of the customer to make a secondary source of repayment available to the company. This is especially important when the cash flows of the customer are weak or variable. Collateral is the security proposed by the borrower. Collateral may be of either nature moveable or immovable. Moveable collateral comprises right from stock, inventories to playing vehicles. In case of immovable it may be land with or without building or fixture, plant machineries attached to it. The collateral ought to be secure, readily merchantable and that its quality ought to have the capacity to meet obligation when sold off in the event that the borrower defaults in payment (Van Horne, 2007).

### **v) Conditions**

Once the funding company is satisfied with the character, capacity, capital and collateral then a credit agreement (sanction letter) is issued in favor of the borrower stating conditions of the credit to which borrower's acceptance is accepted. The credit officer ought to carve a sensible judgment in regards to the possibilities of default and appraise the likelihood of losses under such condition Pandey (2008).

#### **2.1.10 loan process:**

The objective of loan management is to control loan approval and achieve loan quality. However, every loan approval process should introduce adequate controls mechanism to achieve quality in credit at the time of origin. The process should be in line with bank's credit guideline, its risk profit, and the capabilities of its lenders. The

loan approval decisions are made by credit committee of a bank. Bank lending policy refers to the policy and guideline adopted by a bank in order to make its lending process systematic and methodical. Bank cannot effort to either keep the deposit idle in the vaults or lend the deposits and not recollect. Hence, it is essential that a proper lending policy is in place.

Considering the different kinds of loan process, Petersen and Rajan (1994) have classified in two categories: hard and soft. Hard information is produced by the analysis of financial document and soft information is qualitative information.

Nawaz and Munir (2012) found that credit risk management effected on the banks' profitability, and they recommended that management should be cautious in setting up a credit policy that might not negatively affect profitability.

6 steps in the lending process are;

1. Finding prospective loan customers,
2. Evaluating a prospective customer's character and sincerity of purpose,
3. Making site visits and evaluating a prospective customer's credit record,
4. Evaluating a prospective customer's financial condition,
5. Assessing possible loan collateral and signing the loan agreement,
6. Monitoring compliance with the loan agreement and other customer service needs,

### **Required Documents**

After identifying the appropriate sources for the borrower funding needs and ensuring one is eligible for the loan, the next step is to collect the necessary document. The document required will vary from one bank to another. Banks can request some or all of the following documents:

- i. Application form

- ii. Valid proof of Applicant's identity (e.g. citizenship/passport)
- iii. Passport size photographs of the applicant, the guarantor
- iv. Loan request details (how much need/how the money used/ loan period)
- v. Audited financial documents (balance sheet, cash flow statement, income statement)
- vi. Business legal documents (business registration, PAN registration certificate)
- vii. Tax returns (personal and business)
- viii. Business plan
- ix. Bank declarations (issued by the customer's bank stating their account number and balance)
- x. Other documents specified by the bank from time to time

Once eligibility requirements are fulfilled and the necessary documents are collected, the borrower can approach the bank for a loan. The rapid increase of demand in credit in commercial banks of Albania during the booming phase who is capable to select the best and successful credit application that help to earn more in the financial institutions (Ciuriak, 2001).

Nepal Rastra Bank (NRB) has raised the lending requirement to 25% for commercial banks towards "productive sectors" that encompasses hydropower, agriculture, tourism, export, small and medium industries, pharmaceuticals, cement, and garments. The updated monetary policy requires commercial banks to allocate 10% of total lending in agriculture, 5% in hydropower, 5% in tourism and remaining 5% in other sectors (NRB directive).

### **2.1.11 Effect of Credit Default on Commercial Bank**

Credit default is the failure or the incapability of a customer to repay the credit as per conditions of a loan as agreed with the lending institution. Credit default occurs when borrowers are unable to meet the required payment or when borrowers are unable to honour the loan agreement. Defaulting on a loan obligation can place a company or individual in financial trouble. Balogun and Alimi (1988) look at credit non-payment as the incapability of a customer to perform his or her loan obligation under a loan agreement when due.

Baku and Smith (1998) states that the loan default has negative impact on the borrower and the lending institutions. The cost of loan default to the lending institutions involves. The lost of loan interest, commitment fees, loan processing fees, other charges in relation to the loan and the opportunity cost of using the principal. To the borrower the cost of loan default includes, the penalties meted out to borrowers who default by the lending institution, the lost of reputation and credit record upon which further loans assessment will be based on. Accordingly Hampel et al (1994) the lending process is the most compound activity in the operations of a bank and the solvency and profitability of the financial institutions depend to a large extend on how effective and efficient default risk will be controlled and managed. This is properly done through efficient credit management process being used by financial institutions. This has caused this survey to effectively and efficiently examine the management of loans of EBL and NIBL.

### **2.1.12 Project Appraisal**

Project appraisal is the structured process of assessing the viability of a project or proposal. It involves calculating the feasibility of the project before committing resources to it. It is a tool that bank's use for choosing the best project that would help them to attain their goal.

Every bank should carefully analyse the loan project when give loan to the customer. It will help for the bank to know about the whether project is suitable or not for bank. Before invested for the customer, bank makes analysis of project from various aspect and angles. The main objective and project of project appraisal is to help to know

about the guarantee of reasonable return from the project. Project appraisal main objective are the following:

- I. To evaluate the project is technically sound
- II. To extract relevant information for determining the success or failure of a project
- III. It helps in arriving at specific and predicted results
- IV. It evaluates the desirability of the projects
- V. It employs existing norms to predict the rate of success or failure of a project
- VI. It verifies the hypothesis framed for the project

Four major criteria in project appraisal

There are four major criteria which have to be studied in project appraisal to ascertain its feasibility. They are:

- i. Technical feasibility
- ii. Economic feasibility
- iii. Financial feasibility
- iv. Managerial feasibility

Source: [www.nrb.org.np](http://www.nrb.org.np)

### **Directive issued by NRB for the commercial bank**

#### **i. Classification of loans/advances:**

(a) Pass: Loans/advances which have not overdue and which are overdue by a period up to three months.

(b) Sub-standard: Loans/advances which are overdue by a period from three months to a maximum period of six months.

(c) Doubtful: Loans/advances which are overdue by a period from six-months to a maximum period of one year.

(d) Loss: Loans/advances which are overdue by a period of more than one year.

The loans which are in pass class and which have been rescheduled/restructured are called as "the performing loan, and the sub-standard, doubtful and loss categories are called non-performing loans.

**ii. provisions relating to pass loans:**

(a) Loans/advances extended against the collateral of gold and silver;

(b) Loans/advances of fixed receipts,

(c) Loans/advances of Government of Nepal securities and loans/advances made against the collateral of Nepal Rastra Bank bonds;

**iii. Provisions Relating to Loss loans:**

(a) The market price of the collateral cannot secure the loans;

(b) The debtor is bankrupt or has been declared to be bankrupt;

(c) The debtor disappears or is not identified;

(d) 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;

(e) Loan is misused;

(f) 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;

(g) Providing loan to a debtor who has been enlisted in the black-list of Credit Information Bureau Ltd;

(h) The Project/business is not in a condition to be operated or project or business is not in operation

(i) The credit card loan is not written off within 90 days from the date of expiry of the deadline;

(j) 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

#### **iv. Provision Relating to Term-Loan:**

In cases of the term loans extended in installments, if the deadline of installment of the principal amount expires, remaining entire loan amount has to be classified based on expiry of the deadline of the installment amount.

#### **v. Provisions Relating to Rescheduling and Restructuring of Loans:**

- (a) Evidence showing that documents relating to loans and security are adequate;
- (b) Bases on which the licensed institution is convinced of the possibility that the rescheduled or restructured loans would be recovered;
- (c) In addition to submission of written plan of actions for rescheduling and restructuring loans at least 25 percent of the interest due to be paid until the date of rescheduling or restructuring of such a loan has been paid;

#### **vi. Provision to be maintained for loan loss**

<b>Classification</b>	<b>Provision</b>
1. Pass Credit	1%
2. Sub Standard Credit	25%
3. Doubtful Credit	50%
4. Bad Credit	100%

#### **Limit of Credit and Advances in a Particular Sector**

- Fund based credit and advances can be issued up to 25% (upper limit) of core capital to a single customer, firm, company and a group of related customers.
- Non –fund based (off balance items) can be issued up to 50% of core capital to a single customer, firm, company and group of related customer.

Note: The core capital includes ( paid up capital+ share premium + non-redeemable preference share + general fund + accumulated profit/loss – goodwill )

## **2.2 Review of related Articles**

In this section, effort has been made to examine and review of some related article, books and thesis.

### **2.2.1 Review of Articles**

Ahmed and Malik (2015), “Credit Risk Management and Loan Performance” in this article study about the credit risk management practices on loan performance while taking the credit terms and policy, collection policy, credit risk control as the dimensions of the credit risk management practices. For statistical evaluation, the primary data in cross sectional form has been taken into consideration. The study is helpful for the management to enhance the LP by focusing on the dimension of the credit risk management practices used in the study. The result of the analysis are showing that the credit terms and client appraisal have positive and significant impact on the LP, while the CP and CRC have positive but insignificant impact on LP.

Zerith (2008), in article “Credit Portfolio Management”, Affirmed that to manage the credit portfolios, bankers must understand not only the risk posed by each credit but also how the risks of individual lending 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. 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.

Han (2015), credit risk has always been the main risk of the banking and financial sectors also is the main object and the core content of financial institutions and regulatory departments to prevent and control. With the continuous development of international financial market, domestic commercial banks will be under the impact of international and domestic factors more, take more internal and external risk. In his article risk are classify as operating, market and moral hazard risk.

Alshatti (2015), This research aims at examining the effect of “Credit risk management on financial performance” of the Jordanian commercial banks during the period (2005-2013), thirteen commercial banks have been chosen to express on the whole Jordanian commercial banks. Two mathematical models have been designed to measure this relationship, the research revealed that the credit risk management effects on financial performance of the Jordanian commercial banks as measured by ROA and ROE. The research further concludes that the credit risk management indicators considered in this research have a significant effect on financial performance of the Jordanian commercial banks.

Timsina (2014) Determinants of bank lending in Nepal.. The main objective of the study is to test and confirm the effectiveness of the determinants of commercial bank lending behaviour in Nepal by using time series Ordinary Least Square regression approach for empirical analysis. From the regression analysis, it was found that Gross Domestic Product and liquidity ratio of banks have the greatest impacts on their lending behaviour As there is significant positive relationship between GDP and private sector credit of commercial banks.

Haneef, Riaz and Mansoor (2012) examined the impact of risk management on non-performing loans and profitability of banking sector of Pakistan. The study used sampling technique where it selected five commercial banks for inclusion in the study. The result of this study revealed that there was no proper mechanism for risk management in banking sector of Pakistan. Study also concluded that non-performing loans were increasing due to lack of risk management which threatened the profitability of banks.

**Table 2.1 Summary of Empirical Review**

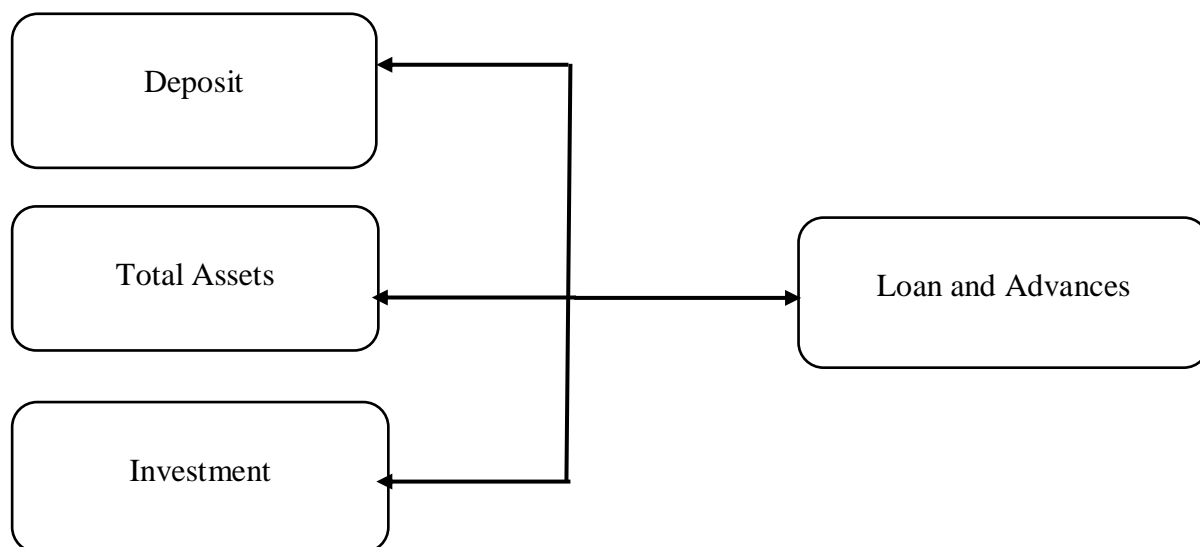
Article	Topic	Objective	Methodology	Finding
1 Malla,2017	Credit Portfolio Management in Nepalese Commercial Banks	Status of loan portfolio management and techniques adopted by Nepalese commercial banks	Sample size-6 commercial bank SPSS analysis (both qualitative & quantitative)	The portfolio management concentration of the banks have been studied by analysing security wise loan, product wise and sector wise concentration of loans
2 Ndubuisi, Chinyere and Beatrice,2017	Loan Management and Financial Performance of Quoted Deposit Money Banks in Nigeria	Determine the relationship that exists between loan management and financial performance	Sample size-15 commercial bank Panel sampling method and regression coefficient correlation	Loan management has a positive and statistically significant relationship with ROA, EPS and DPS at 1,5&1% level of significance
3 Han,2015	Credit Risk Management of Commercial Banks	To prevent and control of credit management risk	-	-
4 Okungu, Nyongesa and Momanyi,2014	Effect of Commercial Bank Loans on Financial Performance of Saving and Credit Co-operative Societies in Kisumu, Kenya	Investigate the effect of commercial bank loans on the financial performance of saving and credit	Sample size-370 respondents Chi-square and correlation test	Commercial bank loans have not grossly affected the saving and lending volumes of the SACCO
5 Ahmed and Malik, 2015	Credit Risk Management and Loan Performance	Evaluate the influence of credit risk management practices on loan performance	Sample size-157 managers Descriptive and inferential statistical techniques	the credit term has significant positive impact on loan performance
6 Nazaj and Meka, 2012	Loan Management and its Role the Lending Process	To evaluate the role of lending process in controlling and monitoring the bank performance	Sample size-16 commercial bank Correlation test	Improving internal lending practices and procedures along with modern risk management principle

7 Ohuko, Muganda and Musiega, 2015	Effect of Credit Risk Management on Loan portfolio quality of Tier one Commercial Banks in Kenya	To determine the effect of credit risk management on loan portfolio quality of commercial bank	Sample size- 5 banks Descriptive statistics and SPSS analysis	Loan pricing had significant positive on the level of NPA.
8 Kattel, 2015	Study of credit risk identification techniques followed by commercial banks in Nepal	To explore the current credit risk identification techniques used by Nepalese commercial banks	Sample size-9 commercial bank Descriptive statistics and ANOVA analysis	Bank is always trying to improve their credit risk identification techniques in their credit policy for quality of lending and various measures are undertaken to follow the effective credit management system.
9 Mercylynne and Omahwa, 2017	Credit risk management and financial performance of selected commercial banks in kenya	To determine the effect of loan appraisal process, lending requirement, debt recovery process and credit policy on financial performance	Sample size- 5 bank Multiple linear regression and SPSS	Debt recovery process does not significantly affect bank performance whereas loan appraisal process and credit policy were found to have a significant effect on bank performance.
10 Alshatti, 2015	The effect of credit risk management on financial performance of the Jordanian commercial bank	To examine the effect of the credit risk management indicators on the financial performance of commercial bank	Panel regression model	There is a positive effect of non-performing loans and negative effect of leverage ratio on the banks financial performance but no effect on the capital adequacy ratio
11 Konovalova ,kristovska and Kudinska, 2016	Credit Risk Management in Commercial Banks	To determine the level of risk represented by different groups of retail clients in order to reduce and prevent credit risk in the future and improve the management of	Sample size-100 clients SPSS analysis	When lending to individual the most significant factors affecting the value of the average income of the borrower, the loan amount and the loan

		banking risks.		term
12 Timsina,2014	Determinants of bank lending in Nepal	To test and confirm the effectiveness of the determinants of commercial bank lending behaviour in Nepal	Least square regression	Commercial banks' lending is mostly determined by the gross domestic product of the country and liquidity ratio to be maintained by the commercial banks.
13 Bhattarai,2014	Determinants of non-performing loans: perception of Nepali bankers	Perception of Nepalese bankers regarding the determinants of non-performing loan in Nepalese commercial banks	Sample size- 10 commercial banks SPSS analysis(five Likert scale)	If the bank is government owned the chances of having non- performing loan increases.

### 2.3 Conceptual Framework

Conceptual framework is a scheme of concept (variables) which the researchers operationalize in order to achieve the set objective. A variable is a measure characteristic that assumes different values among subject. The conceptual framework is the foundation on which the entire thesis is based. It is a logically developed, described, and elaborated network of associations among variables that have been identified through such processes as interviews, observations, and literature survey. These variables are deemed relevant to the problem situation (Sekaran and Bougie, 2013). Independent variables are variable that researcher manipulates in order to determine its effect of influence on another variable. Dependent variable attempts to indicate the total influence arising from the influence of the independent variable (Mugenda, 2003).

**Independent Variables****Dependent Variable****2.3 ResearchGap**

The purpose of this research is to develop some expertise in one's area, to see what new contribution can be made and to receive some ideas, knowledge and suggestions in relation to loan management of Everest Bank and Nepal Investment bank. Thus, the previous studies can't be ignored because they provide the foundation and some important information, idea for the present study. This research tries to fill the gap by analysis and identify the impact of loan management on the financial performance of commercial banks in Nepal.

This study made on impact of loan management on financial performance of the bank. Hence the researcher had attempted to fill this gap by measuring the loan management of EBL and NIBL and by studying their loan management system and effect on financial performance. This study also aims to find out the organizational structure of EBL and NIBL for the proper implementation and compliance of NRB Directives and to manage the credit. This research is selected to complete this research work: many books, journals, articles and various published and unpublished dissertations are followed as guideline to make the research easier and smooth. In this regard, here we are going to analyze the different procedure of loan management, which is considered on EBL and NIBL. Our main research problem is to analyze whether the EBL and NIBL has right level of liquidity as well as is able to utilize its resources effectively or not.

To achieve this main objective, various financial and statistical tools are used. This study aimed to not only study about loan management system and financial performance but also to report and fill the knowledge gap among Nepalese bank account holders and researchers. This research also provides recommendations to how to manage loan and deposit. So this study try to fulfilled those interested parties, scholars, teacher, student, business men, society and government for academically as well as policy perspectives.

## CHAPTER– III

### RESEARCH METHODOLOGY

#### 3.1 Introduction

Kothari (2009) says research methodology is a way to systematically solve the research problem. Thus, research methodology is a systematic way to solve a problem. It is the specific procedures or techniques used to identify, select, process, and analyze information about a topic. It is also defined as the study of methods by which knowledge is gained. Its aim is to give the work plan of research. The methodology section answers two main questions: How was the data collected or generated? How was it analyzed?

#### 3.2 Research Design

Research design is a master plan specifying the methods and procedures for collecting and analyzing the needed information (Zikmund, 2013). A research design is a framework or blueprint for conducting the marketing research project. Research design is to ensure that requisite data in accordance with the problem at hand is collected accurately and economically. The research design, depending upon the needs of the researcher may be a very detailed statement or only furnish the minimum information required for planning the research project. The basic element of a research design are: the problem, the methodology, data gathering, data analysis and report writing. In this study descriptive and explanatory research design have followed.

#### 3.3 Population and Sample

Population refers to the entire group of people, events, or things of interest that the researcher wishes to investigate. The researcher cannot normally survey everyone in the population; but through sampling techniques it can be confident that only a small part of the total population is taken to represent the total population. Hence, a sample is only a portion or subset of the universe or population. A sample is define as a collection of items or element from a population. Baskota (2004) sample is any

number selected to represent the population according to some rule. Selecting a sample means selecting elements from target population.

Here population refers the total numbers of commercial banks that means, the population is 28 commercial bank and Everest bank ltd and Nepal investment bank ltd has been selected as sample for the study. One bank from joint venture and another from private. Similarly, financial statement of these bank for 8 years have been taken as sample for the same purpose. The use of convenience sampling technique is used to collect the required data.

### **3.4 Sources of the Data**

There are two sources of data collection. They are primary sources and secondary source. Necessary data collected from both sources: primary and secondary. Even though adequate data are collected from secondary sources.

#### **a) Primary source**

#### **b) Secondary sources**

Generally, this research is based on secondary data. Secondary data are collected from secondary sources. Secondary data are mostly used for this research purpose. So the major sources of secondary data are as follows

- ❖ Annual report and their websites of the concerned bank
- ❖ National newspaper, journals and magazine and reports of Central Library of TU
- ❖ Internet
- ❖ NRB directives
- ❖ thesis

### **3.5 Method of Data Analysis Technique**

Data analysis consists of categorizing data, coding them, tabulating and then drawing statistical for the fulfilled of objectives of this research. It includes closely related operations like summarizing the collected data and organizing in such a manner that they will yield answers to the research questions. This study has used percentage, graphs, tables, charts, correlation and regression analysis for analysis of data

collected. SPSS software is used for the results of correlation coefficient and regression.

### **3.5.1 Financial methods**

#### **Ratio Analysis**

A ratio is a quotient of two numbers and the relation expressed between two variables. Ratio analysis is a very powerful analytical tool useful for measuring performance of an organization. The ratio analysis concentrates on the interrelationship among the figures appearing in the financial statements. Ratio analysis allow interested parties like shareholders, investors, creditors, Government and analysts to make an evaluation of certain aspects of a firm's performance

#### **1. Liquidity ratio**

A liquidity ratio is an indicator of whether a company's current assets will be sufficient to meet the company's obligations when they become due. Liquidity ratios are most useful when they are used in comparative form. The ratio measures the company's ability to pay its short-term debts. A high ratio indicates a company with a low risk of default.

#### **Cash reserve ratio**

The cash reserve ratio refers to a certain percentage of total deposits the commercial banks are required to maintain in the form of cash reserve with the central bank. The objective of maintaining the cash reserve is to prevent the shortage of funds in meeting the demand by the depositor. CRR is generally define as a particular minimum amount of deposits that needs to be maintained as a reserve by every commercial bank according to the requirement of the NRB. The latest monetary policy introduce by NRB had slashed CRR to 4% for the commercial bank.

$$\text{Cash Reserve Ratio} = \frac{\text{Cash and bank balance}}{\text{Total Deposit}}$$

#### **2. Assets Management Ratio**

Assets management ratio measures the proportion of various assets and liabilities in balance sheet. Every commercial bank should manage its assets and liabilities

properly to earn profit in competitive environment. Assets management ratio measures its efficiency in performing assets. Some of the various assets management ratio are calculated in this research, which measure the lending strength and effective use of assets.

**i. Loan and Advances to Total Deposit Ratio**

The main sources of banks lending is its deposit. This ratio help to measure to find out the banks are utilizing their deposits on loan and advances for profit generating activities.

$$\text{Loan and advances to total deposits ratio} = \frac{\text{Cash and bank balance}}{\text{Total Deposit}}$$

**ii. Loan and Advances to Total Assets Ratio**

Loan and advances to total assets ratio is the ratio that represents the financial position of the bank and the bank's ability to meet all its financial requirements. It is also one of the indicator of credit risk.

$$\text{Loan and advances to total assets ratio} = \frac{\text{Cash and bank balance}}{\text{Total assets}}$$

**iii. Interest spread ratio**

The ratio measure the contribution made by investment in total loan and advances. interest spread ratio is the difference between interest earned on loans, securities, and other interest-earning assets and the interest paid on deposits and other interest-bearing liabilities. The low ratio indicates the mobilization of funds in safe area and vice versa.

$$\text{Interest spread rate} = \frac{\text{Interest Income}}{\text{Loan and advances}} - \frac{\text{Interest Expenses}}{\text{Deposits}}$$

**3. Profitability Ratio**

A profitability ratio is a measure of profitability, which is a way to measure a bank's performance. It measure the overall performance of the company in terms of the total revenue generated from its operations. Profit is essential for the survival of bank so it

is regarded as the engine that drives the banking business and indicates economic progress. Lending is one of the major function of the commercial bank so to know about their credit situation and their management profitability ratio would help by analysing the following ratio.

**i. Interest Income to Loan and Advances Ratio**

The ratio measure by dividing interest income by loan and advances. It measures the proportion of interest income and efficiency of the bank.

$$\text{interest income to loan and advances ratio} = \frac{\text{interest income}}{\text{loan and advances}}$$

**ii. Return on Total Assets Ratio**

This ratio measures the earning capacity of the commercial bank through it fund mobilization as total assets. The return on total assets (ROTA) is a ratio that measures a company's earnings before interest and taxes (EBIT) relative to its total net assets. The ratio is considered to be an indicator of how effectively a company is using its assets to generate earnings before contractual obligations must be paid.

$$\text{Return on total assets} = \frac{\text{Net Profit}}{\text{Total assets}}$$

**iii. Return on Loan and Advances Ratio**

This ratio measures the earning capacity of the commercial bank through it fund mobilization as loan and advances. Higher ratio indicated greater success to mobilize fund as loan and advances and vice versa. Mostly loan and advances includes cash, credit, bank overdraft, bills purchased and discounted.

$$\text{Return on loan and advances} = \frac{\text{Net Profit}}{\text{Loan and advances}}$$

**iv. Operating profit to loan and advance ratio**

Operating profit to loan and advances ratio measure the earning capacity of commercial bank. Operating profit to loan and advances ratio is calculated by dividing operating profit by loan and advances.

$$\text{Operating profit to loan and advances ratio} = \frac{\text{Operating profit}}{\text{Loan and advances}}$$

**v. Earning per share**

Earnings per share (EPS) is the portion of a bank's profit allocated to each share of common stock. Earnings per share serves as an indicator of a bank's profitability. It is common for a company to report EPS that are adjusted for extraordinary items, potential share dilution. It only measures the overall operational efficiency of bank. EPS is a financial ratio, which divides net earnings available to common shareholders by the average outstanding shares over a certain period of time. The EPS formula indicates a bank's ability to produce net profits for common shareholders.

$$\text{Earning per share} = \frac{\text{Profit after tax}}{\text{No. of common share}}$$

**vi. Price earning ratio**

The price earning ratio (P/E) is a valuation method used to compare a bank's current share price to its per-share earning. It is the relationship between a bank's stock price and earnings per share (EPS). It is a popular ratio that gives investors a better sense of the value of the bank. The P/E ratio shows the expectations of the market and is the price you must pay per unit of current earnings (or future earnings, as the case may be). Higher ratio shows the higher efficiency of the management and lower ratio shows the lower efficiency of the management.

$$\text{Earning per share} = \frac{\text{Earning per share}}{\text{Market value per share}}$$

**4. Lending Efficiency Ratio**

A bank efficiency ratio a measure of a bank's overhead as a percentage of its revenue. This ratio is concerned with measuring the efficiency of bank. This ratio also shows the utility of available fund.

## **I. Loan loss provision to total loan and advances ratio**

A loan loss provision is an expense set aside as an allowance for uncollected loans and loan payments. This provision is used to cover a number of factors associated with potential loan losses including bad loans, customer defaults and renegotiated terms of a loan that incur lower than previously estimated payments. Loan loss provision to total loan and advances describes the quality assets that a bank holding. The provision for loan loss reflects the increasing probability of non-performing loan.

The low ratio indicates the good quality of assets in total volume of loan and advance: High ratio indicates more risky assets in total volume of loan advances.

$$\text{Loan loss provision to total loan and advances} = \frac{\text{Loan loss provision}}{\text{Total loan and advances}}$$

## **II. Interest expenses to total deposit ratio**

Interest expenses to total deposit ratio calculated for to know about the effectiveness of interest expenses on total deposit. Deposit its main sources for the loan. But bank pay certain interest on deposit so that interest expenses should manage for better mobilization of deposit.

$$\text{Interest expenses to total deposit ratio} = \frac{\text{Interest expenses}}{\text{Total deposit}}$$

## **5. Growth Rate**

Growth rate help to know about the increasing or decreasing position of different factors of bank. Increasing rate indicated better financial mobilization but some time decreasing rate also prefer for the bank.

### **i. Growth rate of total deposit**

### **ii. Growth rate to loan and advances**

### **iii. growth rate of net profit**

### 3.5.2 Statistical Method

For supporting this research statistical tool are also used. Under this analysis collection, examination, summarization, manipulation, and interpretation of quantitative data to discover its underlying causes, patterns, relationships, and trends.

#### i. Arithmetic Means (average)

The arithmetic mean, also called the average or average value, is the quantity obtained by summing two or more numbers or variables and then dividing by the number of numbers or variables. This is commonly known as average. The average of a given set of numbers is called the arithmetic mean, or simply, the mean of the given numbers.. It is calculated as:

$$\bar{X} = \frac{1}{n} \sum_{i=1}^n X_i$$

Where,

$\bar{X}$ =mean value of arithmetic mean

$$\sum_{i=1}^n X_i = \text{sum of the observation}$$

N = number of observation

#### ii) Correlation Coefficient (r)

Correlation coefficient is used in statistics to measure how strong a relationship is between two variables. It is a statistical measure that calculates the strength of the relationship between the relative movements of the two variables. These variables are said to be correlated when the change in the value of one results change in another variable. Here Karl person's measure used for this research, which is known as Karl person correlation coefficient between two variable series x (x1 and x2) r can be obtained as:

$$r_{x_1x_2} = \frac{N\sum X_1X_2 - (\sum X_1)(\sum X_2)}{\sqrt{[N\sum X_1^2 - (\sum X_1)^2]} \sqrt{[N\sum X_2^2 - (\sum X_2)^2]}}$$

Whereas,

$r$  = correlation of coefficient

$N$  = no. of year

$r_{x_1x_2}$  = Correlation between  $X_1$  and  $X_2$

$N\sum X_1X_2$  = No. of Product observation and Sum of product  $X_1$  and  $X_2$

$\sum X_1\sum X_2$  = Sum of Product  $X_1$  and sum of Product  $X_2$

Condition	Decision
When $r=1$	There is positive correlation
When $r=-1$	There is negative correlation
When $r$ lies between "0.7 to 0.999"	There is high degree of positive correlation
When $r$ lies between "0.5 to 0.6999"	There is moderate degree of correlation
When $r$ is 0	There is no correlation

### iii) Probable Error

The probable error of the coefficient of correlation helps in interpreting its value. With the help of probable error, it is possible to determine the reliability of the value of the coefficient in so far as it depends on the conditions of random sampling. The probable error of the coefficient of correlation is obtained as follows:

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

Here,  $r$  = Correlation coefficient

$N$  = Number of pairs of observations

If the value of 'r' is less than the probable error, there is no evidence of correlation, i.e., the value of 'r' is not at all significant. Then, if the value of 'r' is more than six times of the probable error, the coefficient of correlation is practically certain, i.e., the value of 'r' is significant.

#### iv) Multiple Regression Analysis

Regression analysis is a set of statistical processes for estimating the relationships among variables. It includes many techniques for modeling and analyzing several variables, when the focus on the relationship between a dependent variable and one or more independent variables (or ‘predictors’). More specifically, regression analysis helps one understand how the typical value of the dependent variable (or ‘criterion variable’) changes when any one of the independent variables is varied, while the other independent variables are held fixed. This study the main objective of estimating impact the value of dependent variable (loan and advances) from the value of multiple independent variables (total assets, total deposit and investment).

Regression equation of Y (loan and advances) on Deposit, Total Assets and Investment.

##### Model 1

It has used to test the relationship between independent variables and dependent variable

$$y = a + b_1D + b_2TA + b_3I + \dots + e_i \quad \text{Eqn. 1}$$

Where,

$b_1D$  = Total Deposit

$b_2TA$  = Total Assets

$b_3I$  = Investment

## CHAPTER–IV

### RESULTS

In the chapter, the data collected from various sources have been analyzed and major findings of the study are presented systematically. Data have been analyzed according to the research methodology as mentioned in third chapter. Data analysis was done using IBS SPSS 21 with the main analysis tools being ratio analysis, descriptive statistics, correlation and regression analysis. The purpose of this chapter is to introduce the mechanics of data analysis and interpretation. With the help of this analysis effort have been made to highlight credit management of Everest Bank Limited and Nepal Investment Bank Limited.

#### **Financial Analysis**

Financial statement are the single most important external information source when making a credit decision. A financial analysis is an assessment of how viable, stable, solvent, and profitable a bank is. The term may refer to an assessment of how effectively funds have been invested. A financial analysis looks at many aspects of a bank from its profitability and stability to its solvency and liquidity. Financial analysis is done using EXCEL program in computer.

#### **4.1 Measuring Liquidity Position of the Bank**

Liquidity refers to how much cash a bank has or how quickly it could access cash. A bank's liquidity tells us how easily a bank can pay its customer. A commercial bank must maintain its satisfactory liquidity position to satisfy the credit needs to meet demands for deposit withdrawal, pay maturity obligation in time.

##### **4.1.1 Cash Reserve Ratio**

The Cash Reserve Ratio refers to a certain percentage of total deposits the commercial banks are required to maintain in the form of cash reserve with the central bank. The objective of maintaining the cash reserve is to prevent the shortage of funds in meeting the demand by the depositor. The amount of reserve to be maintained depends on the bank's experience regarding the cash demand by the depositors. Nepal

Rastra Bank (NRB) has revised the cash reserve ratio (CRR) for commercial banks from 6 percent to 4 percent.

**Table No. 4.1**

**Cash Reserve Ratio**

<b>Fiscal year</b>	<b>CRR % EBL</b>	<b>CRR% INBL</b>
2009/10	15.53	7.77
2010/11	9.55	7.76
2011/12	17.22	13.6
2012/13	15.19	16
2013/14	16.91	19.2
2014/15	24.27	12
2015/16	16.61	7.2
2016/17	14.69	10.5
Mean (X)	16.246	11.754

(Sources: Annual Report of EBL and NIBL)

Table no. 4.1 show the cash reserve ratio of EBL and NIBL. According to NRB CRR should maintain 4%. Here both bank CRR higher then 4%. The ratio is highest in EBL that 24.27% in FY 2015/16 and lowest is 9.55% in FY 2010/11. But in case of NIBL highest ratio is 19.2% in FY 2013/14 and lowest ratio is 7.2% in FY 2015/16. On an average EBL has highest ratio than NIBL. Both bank CRR is good but according to this data EBL CRR better than NIBL. This concludes that EBL has better liquidity position.

#### **4.2 Assets Management Ratio**

Asset management ratios compare the assets of a bank to its revenue. Asset management ratios indicate how successfully a bank is utilizing its assets to generate revenues. They indicate the ability of a bank to translate its assets into the revenue. Asset management ratios are also known as asset turnover ratios and asset efficiency ratios. Asset management ratio measures the efficiency of the bank. By the help of the following ratios, asset management of EBL and NIBL has been analyzed.

#### 4.2.1 Loan and Advances to Total Deposit Ratio

loan and advances clearly state that it is the assets of the bank and total deposit is the liability. So, this is the ratio between assets and liability. This helps to show the ratio of Loan & advances to total deposit. We can also conclude that what part of the loan and advances is initiated against total deposit.

**Table No. 4.2**

#### **Loan and Advances to Total Deposit Ratio**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio % NIBL</b>
2009/10	76.24	81.74
2010/11	76.98	83.54
2011/12	73.22	75.3
2012/13	76.57	76.4
2013/14	78.01	72.4
2014/15	66.63	74.7
2015/16	73.52	80.1
2016/17	82.32	84.9
Mean (X)	75.44	78.64

(Sources: Annual Reports of EBL and NIBL)

From the above table shows that ratio of EBL and NIBL is in fluctuating trend. The highest ratio of EBL is 82.32% in FY 2016/17 and lowest is 66.63% in FY 2014/15. However, in case of INBL highest ratio is 84.9% in FY 2016/17 and lowest ratio is 72.4% in FY 2013/14. Ratio of both bank are fluctuating but the on an average of INBL has highest ratio to compare to EBL. Highest ratio means the better mobilization of deposit as a loan and advance.

#### 4.2.2 loan and Advances to Total Assets Ratio

Loan and advances to total assets shows the bank mobilization on its total assets. It measures the total loan and advances outstanding as a percentage of total assets. The higher this ratio indicates a bank is loaned up and its liquidity is low. In other words, high ratio indicates good performance of the bank in mobilizing its fund by the way of lending function. Similarly, higher the ratio, the more risky a bank may be to higher defaults.

**Table no. 4.3****Loan and Advances to Total Assets Ratio**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio % NIBL</b>
2009/10	68.04	71.45
2010/11	68.50	71.77
2011/12	65.6	65.30
2012/13	67.23	65.20
2013/14	68.80	62.04
2014/15	55.84	64.87
2015/16	60.51	67.04
2016/17	67.20	70.7
Mean (X)	65.16	67.30

(Sources: Annual Reports of EBL and NIBL)

Above table explains that highest ratio of EBL is 68.8% in FY 2013/14 and its average is 65.16%. However in case of NIBL highest ratio is 71.77% in FY 2010/11 and its average is 67.30%. Both bank ratio were fluctuating. Moreover on an average NIBL has highest ratio as compare to EBL. Thus it means NIBL has better performance in mobilizing its fund by the way of lending activities and also excessive high ratio is risky which may with higher defaults.

**4.2.3 Interest Spread Ratio**

The ratio measures the contribution made by investment in total loan and advances. The low ratio indicates the mobilization of funds in safe area and vice versa.

**Table no.4.4****Interest Spread Ratio**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio % NIBL</b>
2009/10	4.78	4.36
2010/11	4.60	4.06
2011/12	5.32	4.5
2012/13	5.68	5.5
2013/14	5.69	4.8
2014/15	4.76	4.6
2015/16	4.89	4.7
2016/17	4.48	4.3
Mean (X)	5.025	4.6025

Source: Annual report of EBL and NIBL

Total shows that the interest spread ratio of EBL is in fluctuating trend. The highest ratio is 5.69% in FY 2013/14 and lowest ratio 4.48% in year 2016/17. The mean ratio is 5.025% this indicates the mobilization of funds in FY 2013/14, 2014/15, 2015/16 and 2016/17 respectively. These indicate the mobilization of funds in the better area. This indicates the mobilization of funds in safe area. In the case of NIBL the highest ratio is 5.5% in FY 2012/13 and lowest ratio 4.3% in 2016/17. The mean ratio is 4.6025% this indicates the mobilization of funds in FY 2012/13, 2013/14 and 2014/15 respectively. Thus, loan management is in good position of EBL as compare to NIBL.

### 4.3 Profitability Ratio

Profitability ratios are very helpful to measure the overall efficiency in operation of a financial institution. In the context of banks, no bank can survive without profit. Profit is one the major indicators of efficient operation of bank. The banks acquire profit by providing different services to its customers or by providing loan and advances and making various kinds of investment opportunities. A higher profit ratio shows the higher efficiency of a bank. The following ratios are calculated:

#### 4.3.1 Interest income to loan and Advances Ratio

This ratio measures the volume of gross income. Bank's main sources of income is interest income from the lending. The high ratio measure the higher efficiency of the bank and lower ratio indicates the lower efficiency of the bank.

**Table no. 4.5**

<b>Interest Income to Total Loan and Advances Ratio</b>		
<b>Years</b>	<b>Ratio %EBL</b>	<b>Ratio %NIBL</b>
2009/10	9.95	11.4
2010/11	12.20	13.60
2011/12	13.30	13.84
2012/13	10.49	12.90
2013/14	10.11	10.9
2014/15	8.76	8.20
2015/16	6.94	7.50
2016/17	8.19	8.4
Mean (X)	9.99	10.84

(Sources: Annual Report of EBL and NIBL)

From the above table shows that the interest income to total loan and advances ratio of EBL and NIBL both are fluctuating trend. The highest ratio of EBL in FY 2011/12 and INBL also in FY 2011/12. The mean ratio of EBL and NIBL 9.99% and 10.84% respectively. By analysis this table both bank ratio in FY 2015/16 were lowest. Here both bank in FY 2011/12, 2012/13, 2013/14, 2014/15 and 2015/16 indicate that high contribution made by lending and investing activities. But in FY 2010/11 and 2011/12 is not made by lending and investing activities. Here both bank credit management is in a good position.

#### 4.3.2 Operating Profit to Loan and Advances Ratio

Operating profit to loan advances ratio measures the earning capacity of commercial bank. Operating profit to loan and advance ratio is calculated by dividing operating profit by loan and advances.

**Table no. 4.6**

#### **Operating Profit to Loan and Advances**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio % NIBL</b>
2009/10	4.52	4.7
2010/11	4.5	4.3
2011/12	4.9	3.16
2012/13	5.4	4.50
2013/14	5.15	5.40
2014/15	4.36	3.76
2015/16	4.11	4.20
2016/17	4.06	4.4
Mean (X)	4.625	4.30

(Sources: Annual Report of EBL and NIBL)

From the above table the highest ratio of EBL is 5.4% in FY 2012/13 and lowest ratio is 4.06% in FY 2016/17. In the case of NIBL highest ratio is 5.40% in FY2013/14 and lowest ratio is 3.16% in FY 2011/12. The mean ratio is EBL and NIBL is 4.626% and 4.30% respectively. This shows the better profitability position of EBL to compare the NIBL, because its mean is highest as well as NIBL fluctuating trend is more than EBL. But both banks are in good position in loan management.

### 4.3.3 Return on Loan and Advances Ratio

This ratio measures the earning capacity of commercial banks through its fund mobilization as loan advances and vice-versa. This ratio shows effective of net profit on loan and advances.

**Table no.4.7**

#### **Return on Loan and Advances**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio % NIBL</b>
2009/10	3	3.09
2010/11	3	2.81
2011/12	3	2.42
2012/13	3.33	4.01
2013/14	3.2	3.63
2014/15	2.84	2.9
2015/16	2.51	3
2016/17	2.56	2.92
Mean (X)	2.93	3.09

(Sources: Annual Report of EBL and NIBL)

From the above table the highest and lowest ratio of EBL is 3.33% and 2.51% respectively in FY 2012/12 and 2015/16. The mean ratio is 2.93%. In the case of NIBL the highest and lowest ratio is 4.01% in FY 2012/13 and 2.42% in FY 2011/12. The mean ratio is 3.09%. Both bank ratio in fluctuating trend but NIBL is more than EBL. EBL in FY 2009/10 to 2011/12 is normal earning capacity and in the case of NIBL not show the normal earning capacity due to the more fluctuating trend of NIBL.

### 4.3.4 Earning Per Share

Earnings per share is an important financial measure, which indicates the profitability of a bank. It is calculated by dividing the bank's net income with its total number of outstanding shares. It is a tool that market participants use frequently to gauge the profitability of a bank before buying its shares. The objective of computing this ratio is to measure the profitability of the firm on per equity share basis.

**Table no. 4.8**  
**Earnings Per Share**

<b>Years</b>	<b>EPS (Rs) EBL</b>	<b>EPS (Rs) NIBL</b>
2009/10	100.16	52.55
2010/11	83.18	39.10
2011/12	88.55	27.60
2012/13	91.88	46.20
2013/14	86.04	40.70
2014/15	78.04	30.9
2015/16	65.97	29.3
2016/17	44.32	29.3
Mean (X)	79.77	36.96

(Sources: Annual Report of EBL and NIBL)

From the above table EBL earnings per share in increasing trend in FY 2010/11 to 2012/13 and then also increasing in every two years. Highest in FY 2009/10 and lowest in FY 2016/17 that is Rs 100.16 and Rs 44.32 respectively. In the case of INBL earnings per share is more fluctuating. The highest and lowest EPS in FY 2009/10 and 2011/12 that is Rs 52.55 and Rs 27.60 respectively. The mean of EBL and NIBL is Rs 79.77 and Rs 36.96 respectively. By the analysis of these table EBL is shows better profitability for the shareholder and also loan management is in good position.

#### **4.3.5 Price Earning Ratio**

The price to earnings ratio (PE Ratio) is the measure of the share price relative to the annual net income earned by the firm per share. The P/E ratio tells how much the market is willing to pay for a bank's earnings. A higher P/E ratio means that the market is more willing to pay for the earnings of the bank. Higher ratio measures the higher profitability of the firm lower ratio measures lower profitability of the firm. This ratio shows the relationship between earning per share and market value per share.

**Table no. 4.9**  
**Price Earning Ratio**

<b>Years</b>	<b>PE Ratio (time) EBL</b>	<b>PE Ratio(time) NIBL</b>
2009/10	16.27	13.40
2010/11	13.15	10.5
2011/12	11.67	18.50
2012/13	17.32	17
2013/14	30.58	23.60
2014/15	27.17	22.80
2015/16	51.31	35.50
2016/17	30.53	26.30
Mean (X)	24.75	20.95

(Sources: Annual Report of EBL and NIBL)

From the above table highest price earning ratio of EBL 51.31 times in FY 2015/16 and NIBL is 35.50 times in FY 2015/16. Lowest ratio of EBL is 11.67 times in FY 2011/12 and NIBL is 10.5 times in FY 2010/11. The mean ratio of EBL and NIBL is 24.75 times and 20.95 times respectively. Here EBL PE ratio better than NIBL because higher PE ratio indicates that the market has high hope for the future of the share and therefore it has bid up the price. On the other hand, a lower price to earnings ratio indicates the market does not have much confidence in the future of the share.

#### **4.4 Lending Efficiency Ratio**

The efficiency of firm depends largely on the efficiency with which its assets are managed and utilized. This ratio is concerned with measuring the efficiency of bank. This ratio also shows the utility to available fund. The following are the various type of lending efficiency ratio:

##### **4.4.1 Loan Loss Provision to Total Loan and Advance Ratio**

Control of loan loss is an important part of loan management and bank always try to minimize it. Banks has to make provision as per NRB directive. It is money a bank sets aside to cover potential losses on loans. Increase in loan loss provisions decreases

in profit result to decrease in dividends but its positive impact is that strength financial conditions of the banks by controlling the credit risk and reduced the risks related to deposits. Therefore, it can be said that banks suffer it only for short-term loan while the good financial conditions and safely of loans will make bank's prosperity resulting increasing profit for long term.

**Table no. 4.10**

**Loan Loss Provision to Total Loan and Advance Ratio**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio % NIBL</b>
2009/10	2.13	1.54
2010/11	1.91	1.89
2011/12	1.93	1.40
2012/13	1.82	1.17
2013/14	1.81	2.69
2014/15	1.60	2.17
2015/16	1.39	1.78
2016/17	1.27	1.93
Mean (X)	1.7325	1.82

(Sources: Annual Report of EBL and NIBL)

It is observed from the above table that ratio of EBL highest in FY 2009/11 that is 2.13% but after 1 year it is in decreasing trend. Moreover, lowest ratio is in FY 2016/17. In the case of NIBL the ratio is more fluctuated in every year. Sometime it is increasing and some time it is an decreasing trend. Highest ratio is 2.69% in FY 2013/14 and it is lowest in FY 2012/13. However, on average EBL has lowest loan loss provision ratio than NIBL. It is single of low credit risk, good lending policy and good loan management.

#### **4.4.2 Interest Expenses to Total Deposit Ratio**

The ratio measures the percentage of total interest against total deposit. Commercial banks are dependent upon its ability to generate cheaper fund. The cheaper fund has more the probability of generating loans and advances and vice-versa.

**Table no.4.11****Interest Expenses to Total Deposit Ratio**

<b>Years</b>	<b>Ratio % EBL</b>	<b>Ratio% NIBL</b>
2009/10	4.26	5.1
2010/11	6.16	7.22
2011/12	5.74	6.69
2012/13	3.77	4.44
2013/14	3.64	3.82
2014/15	2.54	3.1
2015/16	1.95	2.63
2016/17	3.16	3.55
Mean (X)	3.90	4.56

(Sources: Annual Report of EBL and NIBL)

Table no 4.13 shows that interest expenses to total deposit ratio of EBL and NIBL is in fluctuating trend. The highest ratio of both bank in FY 2010/11 that is 6.16% and 7.22% respectively. Similarly, lowest ratio of both bank in FY 2015/16. The mean value of EBL is 3.90% and NIBL is 4.56%. EBL ratio shows does not indicate higher interest expenses on total deposit. EBL ratio is less than NIBL that means EBL is able to create cheaper interest expenses and better in loan management.

#### **4.5 Analysis of Growth Rate**

It examines and analyzes the growth of the various research variables over the period of time. It analyzes growth rate of deposit, loan and advances, net profit and investment. Growth rate are directly related with fund mobilization and investment decisions of the bank.

##### **4.5.1 Growth Rate of Deposit**

Deposit is main source of fund for the bank. Bank uses fund collected from deposit to provide loan and make investment.

**Table no. 4.12**  
**Growth Rate of Deposit**

(Rs 000,000)

<b>Years</b>	<b>Deposit (Rs) EBL</b>	<b>Deposit (Rs) NIBL</b>
2009/10	36932	50094
2010/11	41128	50138
2011/12	50006	57010
2012/13	57720	62428
2013/14	62108	73831
2014/15	83094	90631
2015/16	93735	108626
2016/17	95094	125669

(Sources: Annual Report of EBL and NIBL)

Above table show that the EBL and NIBL total deposit has increasing trend. Both bank deposit collection are in increasing trend but trend is increasing more faster in NIBL than EBL. So we can conclude that NIBL has good performance than EBL.

#### **4.5.2 Growth Rate of Loan and Advances**

Loan and advances are principle function of a commercial bank and contribute highest income in the form of interest to the bank.

**Table no. 4.13**  
**Growth Rate of Loan and Advances**

(Rs 000,000)

<b>Years</b>	<b>Loan and Advances (Rs) EBL</b>	<b>Loan and Advances (Rs) NIBL</b>
2009/10	28156	40948
2010/11	31662	41887
2011/12	36617	42907
2012/13	44198	47700
2013/14	48450	53458
2014/15	55364	67690
2015/16	68912	87009
2016/17	78285	106683

(Sources: Annual Report of EBL and NIBL)

Above table shows that loan and advances of both bank are in increasing trend. This show that both bank are better in their performance.

#### 4.5.3 Growth Rate of Net Profit

The actual profit after working expenses not included in the calculation of gross profit have been paid is called net profit. The profit of a bank after operating expenses and all other charges including taxes, interest and depreciation have been deducted from total revenue. Also called net earnings or net income. If expenses and charges exceed revenue, the company incurs a net loss. Net profit (net income) increases the stockholders' equity from the operations of a business.

**Table no. 4.14**  
**Growth Rate of Net Profit**

(Rs 000,000)

Years	Net Profit (Rs)	
	EBL	NIBL
2009/10	832	1265
2010/11	931	1176
2011/12	1091	1039
2012/13	1471	1915
2013/14	1549	1939
2014/15	1574	1962
2015/16	1730	2550
2016/17	2006	3114

(Sources: Annual Report of EBL and NIBL)

Above table show that growth rate of EBL is increasing trend but NIBL is fluctuated trend. That means NIBL net profit decrease in FY 2011/12 but after increasing year by year. That indicated not effective position. But EBL net is increasing in same ratio that indicated the good operating position. In last year net profit of NIBL is higher than EBL.

#### 4.6 Statistical Analysis

Statistical analysis is a component of data analytics. The goal of statistical analysis is to identify trends. It help Explore the relation of the data to the underlying population.

#### 4.6.1 Coefficient of Correlation and Regression Analysis

The statistical tool, coefficient of correlation has been studied to find out whether the two available variables are inter-correlated or not. If the result falls within the correlated point, the two variables are inter-correlated otherwise not. Regression coefficient tells how much the dependent variable is expected to increase (if the coefficient is positive) or decrease (if the coefficient is negative) when that independent variable increase by one. In this research both correlation and regression result are directly obtained through **SPSS software**.

#### 4.6.2 Correlation between Total Assets to Loan and Advances

**Table no. 4.15**

**Relationship between Total Assets to Loan and Advances**

Banks	R	R square	P.E
EBL	0.978	0.956	0.010844
NIBL	0.898	0.807	0.00311

**Table no. 4.16**

Banks	Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
EBL	1 (Constant) Assets	4.684	4.129	0.978	1.134	0.300
		0.581	0.051		11.421	0.000
NIBL	1 (Constant) Assets	17.133	9.665	0.898	1.773	0.127
		0.445	0.089		5.010	0.002

(Sources: Annual Report of EBL and NIBL)

From above table the correlation coefficient between loan and advances to total assets are high degree of positive correlation of both EBL and NIBL. The value of r in EBL and NIBL is significant as it is greater than six time of probable error. However, by application of coefficient of determination the value  $r^2$  is 0.956 of EBL and 0.807 of NIBL which indicated that total assets has only 95.6% and 80.7% role in loan and advances and rest is by other unforeseeable factor. This explain that when total assets increase loan and advances also increase.

From the above table 4.18 we can conclude that regression coefficient 'b' is positive i.e. 0.581 for EBL which indicates that one percentage increase in total assets leads to 58.1% increase in loan. In case of NIBL regression coefficient is also positive i.e. 0.445 which shows that one percentage increase in deposit leads to 44.5% increase in loan.

EBL: T-tab < T-cal value, so there is significant relation between Assets and Loan and Advances.

NIBL: T-tab < T-cal value, so there is significant relation between Assets and Loan and Advances.

#### 4.6.3 Loan and Advances to Total Deposit

**Table no. 4.17**

##### **Relationship between Total Deposit to Loan and Advances**

Banks	R	R square	P.E
EBL	0.976	0.953	0.007589
NIBL	0.989	0.978	0.0052

**Table no. 4.18**

Banks	Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
EBL	1	-0.002	4.691	0.976	-0.01	1.000
	(Constant) Deposit	0.753	0.069			
NIBL	1	-4.550	4.228	0.989	-1.076	0.323
	(Constant) Deposit	0.848	0.052			

This table shows there is high degree of positive correlation of EBL and NIBL. Coefficient of determination r square of EBL is 0.953 which indicates that deposit has only 95.26% role in loan and rest is by other sector. Similarly, Coefficient of determination r square of NIBL is 0.9781 which indicates that deposit has 97.81% role in loan and rest is by other sector. Here r is more than 6 times of P.E of both bank that is considered as significance.

From above table 4.20 regression coefficient 'b' is positive i.e.0.753 for EBL and 0.848 for NIBL.

EBL: T-tab <T-cal value, so there is significant relation between Deposit and Loan and Advances.

NIBL: T-tab <T-cal value, so there is significant relation between Deposit and Loan and Advances

#### 4.6.4 Loan and Advances to Total Investments

**Table no. 4.19**

##### **Relationship between Total Investments Total Loan and Advances**

Banks	R	R square	P.E
EBL	0.760	0.577	0.100
NIBL	0.923	0.852	0.01247

**Table no.2.20**

Banks	Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
EBL	1	18.613	11.481	0.760	1.621	0.156
	(Constant) Investment	2.973	1.039		2.862	0.029
NIBL	1	16.337	8.414	0.923	1.942	0.100
	(Constant) Investment	2.741	0.467		5.869	0.001

(Sources: Annual Report of EBL and NIBL)

This table shows the value of r is 0.76 and 0.923 of EBL and NIBL respectively. So that there is high degree of positive correlation of EBL and NIBL. Coefficient of determination r square of EBL is 0.5776 which indicates that investment has only 57.76% role in loan and rest is by other sector. Similarly, Coefficient of determination r square of NIBL is 0.85129 which indicates that deposit has 85.12% role in loan and rest is by other sector. Here r is more than 6 times the coefficient of correlation of both banks that is considered as significant. But NIBL value of r is close to perfect correlation.

From above table 4.22 regression coefficient 'b' is positive i.e.2.973for EBL and 2.741 for NIBL.

EBL: T-tab <T-cal value, so there is significant relation between Investment and Loan and Advances.

NIBL: T-tab <T-cal value, so there is significant relation between Investment and Loan and Advances.

#### 4.6.5 Multiple Regression Analysis

##### Model

It has used to test the relationship between independent variables and Loan and Advances

$$y = a + b_1 MB + b_2 IB + b_3 ATM + \dots + e_i$$

Table 4.21 Regression results of Loan and Advance on Assets, Deposit, Investment

Banks	Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
EBL	(Constant)	8.420	7.786		1.081	0.340
	Assets	1.168	0.873	1.964	1.337	0.252
	Deposit	-0.541	1.123	-0.700	-0.481	0.656
	Investment	-1.299	0.484	-0.332	-2.681	0.055
NIBL	(Constant)	-11.21	3.021		-3.711	0.021
	Assets	0.194	0.065	0.390	2.990	0.040
	Deposit	1.151	0.102	1.342	11.298	0.000
	Investment	-2.196	0.559	-0.739	-3.931	0.017

a. Dependent Variable: Loan and Advances

According to the finding shows in table 4.21, in the case of EBL only assets had statistically significant impact on loan and advance. On the other hand, between the two independent variables used in this study, no one variable has significant impact on dependent variable. From the p value of all independent variables there is no

significant relationship between loan and advances. Because p value is more than 0.05.

Similarly, NIBL assets and deposit had statistically significant impact on loan and advances. But p value of assets, deposit and investment had less than 0.05. that mean there is significant relationship between independent and dependent variable.

#### **4.7 Major Findings of the Study**

Major findings of the study can be presented as follows.

1. On an average EBL has a highest CRR than NIBL. Thus it is found that EBL is very consider to manage its reserve. As NIBL has maintained the cash reserve ratio considerably lower than EBL, it is recommended to increase cash and bank balance to meet loan demand.
2. Assets management ratio of both banks in fluctuating trend but on an average NIBL has highest ratio as compare to EBL. So NIBL has been able to mobilize its deposit efficiency as compare to EBL. But in Nepal there is no any standard ratio of loan to deposit ratio so it is very difficult to say which is better. So that both bank ratio is near to each other, it means both bank are good but NIBL has been able to manage its assets effectively due to the higher ratio.
3. NIBL has highest interest income to loan and advances ratio during entire study period than EBL. It is found that in case of NIBL, interest income has highest contribution in total loan and advances than EBL. Both bank ratio is fluctuating trend but NIBL has higher in average. But in the case of EPS and PE ratio EBL has highest during the entire study period than NIBL.
4. It is found that EBL and NIBL have been able to maintain the loan ratio. From the analysis of loan loss provision to total loan ratio, NIBL has highest loan loss provision as compare to EBL. Thus, credit management is in good position because there is no more different in both bank ratio.
5. Growth ratios of deposit of both banks are in increasing trend but comparatively NIBL has been able to collect deposit than EBL. Similarly, growth of loan and advances of both banks are in increasing trend but comparatively NIBL has provided more loan than EBL during eight-year

study period. But growth of net profit EBL is in increasing trend during eight-year study period. But in the case of NIBL decrease in FY 2009/10 to 2012. From the analysis of this growth rate EBL has better in earning to profit than NIBL.

6. From the correlation analysis there is high degree of positive correlation between Assets to loan and advances. Here the r value of EBL and NIBL is 0.987 and 0.898. which indicates the direction taken by total loan with the changes in the volume of total assets. From the finding of Ndubuisi & Chinyere, 2017 there is negative relationship between assets and loan and advances which show contradictory with this finding. From the article of Mercylynne and Omagwa, 2017 'r' value of 0.723 indicating that there is strong positive relationship that show this article supportive with this finding.
7. There is high degree of positive correlation between deposit to loan and advances. Which shows the bank will be unable to provide large volumes of loan if it does not receive adequate and sufficient deposit in a timely basis. Ndubuisi & Chinyere, 2017 concluded that there is positive and significant relationship between deposit and loan and advance which is supportive with this finding. Mercylynne and Omagwa, 2017 indicating that there is strong positive relationship that show this article supportive with this finding.
8. There is also high degree of positive correlation between investment to loan and advances. Similarly, in the article of Ndubuisi & Chinyere, 2017 and Mercylynne and Omagwa, 2017 concluded that there is positive and significant relationship between investment and loan and advance which is supportive with this finding.
9. Multiple regression analysis shows there is significant relationship between assets, deposit, investment on loan and advances of NIBL. But in the case of EBL there is no significant relationship between any independent variables on dependent variable. In the finding of Ndubuisi & Chinyere, 2017 show there is also significant relationship between dependent and independent variables which show supportive with this finding. Ahmed and Malik, 2014 show regression investigation pin point the significance of influence between dependent and independent variables. Which is also supported for this finding.

## CHAPTER-V

### CONCLUSIONS

This final chapter involves summary, conclusions and recommendation of the research work. This chapter briefly explains the summary of the study, tries to strengthen the financial position of the Everest bank limited and Nepal Investment Bank Limited.

#### 5.1 Summary

Loans are the way a bank makes money. Loans are the lifeblood of a bank. Banks make money by taking in funds from depositors and other sources and then lending money out to customers. So lending is one of the most important function of a commercial bank and the composition of loan and advances directly affects the performance and profitability of the bank. To strengthen, the economy of any country both the private and public sector bank should play a great role, which contributing to our nation. The banking system plays an important role in the modern economic world. The banking system facilitates internal and international trade. A large part of trade is done on credit. Banks act as advisers, counsellors and agents of business and industrial organisations. They help the development of trade and industry. There are special types of banks which provide facilities to different kinds of economic activities. Now-a-days in every country there is a central bank which controls the activities of all other banks, endeavours to keep the price level steady, and controls the rates of foreign exchange. All the economic activities of each and every country are greatly influenced by the commercial banking business of the country. The role of bank remains central in financing economic activity and its effectiveness could exert positive impact on overall economy as a sound and profitable banking sector is better able to withstand negative shocks and contribution to the stability of the financial system (Althanasoglou, 2005).

The review of literature shows that there are so many factors that are related to the loan management of commercial bank. But in this study the real relationship shows between the loan management and financial performance of the bank. Generally, there

is positive relationship between deposit, total assets, investment and loan and advances. Which is shown by the tactical analysis.

In this study, to answer the research question, the financial tools ratio viz liquidity, assets management, profitability and lending efficiency ratio are calculated to find out the lending strength and weakness of this commercial bank. Also growth ratios, statistical tools are conducted for analysis and interpretation of the data. The financial statements of eight years (2009/10 to 2016/17) were selected for the study. In this research, randomly sampling method was adopted by utilizing data collected of Nepalese commercial banks.

## **5.2 Conclusion**

From the analysis of relevant data of sample banks under the study; using various statistical tools mentioned in chapter three and from their finding following conclusion have drawn.

1. From the analysis of liquidity ratio, the bank's ability to pay its short term debts is sufficient. But compare the both CRR ratio EBL has more efficient in management of loan management.
2. Similarly, assets management ratio mainly shows the proration between loan and advances to deposit, investment, total assets. By analysis from this ratio there is NIBL in good position to compare of EBL. But in an average both bank ratio near to each other. So it can be concluded that both bank are in good position of loan management.
3. From the analysis of the profitability ratio, the EPS and PE ratio shows there is high potential growth in profitability of EBL. When EPS is high investor are interested to invested. That mean EBL is able to satisfy the shareholder. Similarly, in other ratio NIBL has highest profitability position.
4. Growth ratio of both bank increasing trend which show both bank in good position in their financial management as well as loan management.
5. From the correlation analysis EBL and NIBL 'r' value lies between 07 to 0.999 which shows high degree of positive correlation. That mean when the increasing in one variable (assets, deposit and investment) will have positive impact towards the loan and advance.

6. From the regression analysis there is significant relationship between dependent variable to independent variable.

Finally, the study concludes that commercial bank financial performance influence by the effective loan management. When bank are able to manage their credit in effective way that also positive impact on financial performance of the bank.

### **5.3 Implications**

These findings may be useful for them who are concerned directly or indirectly with the credit policy of the bank. On the basis of above analysis and findings of the study, following implications are made.

#### **5.3.1 Implication**

1. From the ratio analysis liquidity, assets management, profitability and efficiency ratio measure the bank financial position. In which both bank position is good but to earn more profit EBL and NIBL should be invested their liquid assets in profitable sector.
2. Now commercial bank's interest rate is too fluctuated, which directly affect the perception of customer toward the bank.
3. EBL and NIBL needs to increase its net profit by increasing deposits, decreasing cost and expanding more branches. As the net income of both bank is fluctuating, the bank should try to keep it at stable point.
4. It is recommended to follow the NRB directives which will helps to reduce credit risk arising from defaulter, lack of proper credit appraisal, defaulter by blacklisted borrowers and professional defaulter. Government has established credit information bureau, which will provide suggestion to commercial bank. So EBL and NIBL is suggested to collect as much information about borrowers and only lend to non-risky area and to non-defaulter.
5. Although it is a profit oriented bank, it should not forget the social responsibility. So, the bank should render its services in rural area to promote and mobilize small investors.

6. The bank should also maintain present sound management and extend more facilities to its customers to increase its customers to increase its transactions.
7. As the key to success for any bank and good financial position, this is possible only by proper decision making of loan management. So all the commercial banks are supposed to set proper and practical interest charge for the customers.
8. EBL and NIBL is suggested to formulate and implement sound and effective financial and non-financial strategies to minimize their operational expenses to meet required level of profitability.

### **5.3.2 Recommendation for future researchers**

1. Future researchers are recommended to focus into non-financial performance indicators such as job satisfaction, services quality performance, customer's satisfaction, stakeholders support, government rating, supervisor's teamwork, human resource development, human resource management, job satisfaction etc.
2. Primary data are not taken while studying the subject so the future researcher are recommended to take the primary data also if possible to get more accuracy in the results.
3. This study only taken sample 2009/10 to 2017/18 for this study so future researcher are recommended to take more than eight years data to get better result.
4. Loan management is main concerned of this study, whereas other factor also could be taken in near future.

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