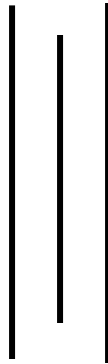


**CREDIT MANAGEMENT OF EVEREST
BANK LIMITED**

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A Thesis Submitted to:
Office of the Dean
Faculty of Management
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***In partial fulfillment of the requirement for the degree of
Master of Business Studies (MBS)***

Kathmandu, Nepal
March 2011

RECOMMENDATION

This is to certify that the thesis

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Viva-Voce Committee

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DECLARATION

I hereby declare that the work reported in this thesis entitled “**Credit Management of Everest Bank Limited**” submitted to Office of the Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the degree of Master of Business Studies (MBS) under the supervision of **Asso. Prof. Ruchila Pandey** of Shanker Dev Campus, T.U.

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ABBREVIATIONS

AD	:	Anno Domini
ATM	:	Automatic Teller Machine
BOD	:	Board of Directors
BS	:	Bikram Sambat
CB's	:	Commercial Banks
CIB	:	Credit Information Bureau
CIC	:	Credit Information Center
CRR	:	Cash Reserve Ratio
DGM	:	Deputy General Manager
DRT	:	Debt Recovery Tribunal
EBL	:	Everest Bank Ltd
ED	:	Executive Director
EPS	:	Earning Per Share
FI	:	Financial Institutions
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
HO	:	Head Office
LC	:	Letter of credit
NBL	:	Nepal Bank Ltd
NGO	:	Non Government Organizations
NIBL	:	Nepal Investment Bank Ltd
NRB	:	Nepal Rastra Bank
P&L	:	Profit and Loss
PNB	:	Punjab National Bank
RBB	:	Rastriya Banijya Bank
SCT	:	Smart Choice Technology
TRs	:	Trust Receipts

CHAPTER - I

INTRODUCTION

The economic development of any nation is highly dependent on the various industrial sectors. This industrial sector comprises public sectors, manufacturing enterprises, tourism, transportation, construction, consulting services, trade, and services. The smooth operations of these sectors certainly have positive results over the economic growth and development of the nation. The failure of only one sector may also retard the economic growth. The level of contribution of these sectors on Gross Domestic Product (GDP) should be increased year by year. The contribution of financial and consultancy services in overall GDP cannot be overlooked. It is the fact that the existence of financial sector in the development of the capital market as well as money market is remarkable. Moreover, the sector has been able to lure a large community to invest in equity shares through primary & secondary market. Whatever may be the position of the sector, one can definitely state that it is one of the major catalysts in removal of backwardness and poverty from the nation. The financial and consultancy services, one of the important industrial sector, comprises banks, development banks, rural development banks, agriculture development banks, finance companies, co-operative with limited banking transactions.

Banking sector plays an important role in the economic development of the country. Commercial banks are one of the vital aspects of this sector, which deals in the process of channel zing the available resources in the needed sectors. It is the intermediary between the deficit and surplus of financial resources. Financial system contains two components viz., depository financial institutions and non-depository financial institutions. Commercial Banks and Finance companies (in Nepalese context) are the examples of depository financial institutions whereas

Employee Providence Fund, Development Bank, Insurance Companies etc, are the examples of non-depository financial institutions. All the economic activities are directly or indirectly channeled through these banks. People keep their surplus money as deposits in the banks and hence banks can provide such funds to finance the industrial activities in the form of loans and advances.

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

Bank came into existence mainly with the objectives of collecting the idle funds, mobilizing them into productive sector and causing an overall economic development. The bankers have the responsibility of safeguarding the interest of the depositors, the shareholders and the society that they are serving.

While talking about financial system there are two important aspects of financial deepening and financial repression. Financial repression is defined as a situation where the government and/ or central bank's regulations distort the operation of financial market. In other words, it means banks are dictated by the central bank

and/or government not to charge more than certain amount of interest and restriction on other activities too. The indicators of such situation are ceiling on the nominal interest rate, mandatory investment in government paper, imposition of reserve requirement limiting their ability to lend and mandatory directed credit in priority and deprived sector. Similarly, financial deepening is defined as the situation where banks are allowed to charge interest on the prevailing market rate. There is negligible restrictions imposed by the central bank and commercial banks have been given total freedom on their activities.

1.12 Evolution of Banking Sector

The origin of modern commercial banking is traceable in ancient times. There is a reference to the activities of moneychangers in the temple of Jerusalem in the New Testament. In ancient Greece the famous temples of Delphi and Olympia served as the great depositories for peoples' surplus funds and these were the centers of money lending transactions. Indeed the traces of "rudimentary banking" are found in the Chaldean, Egyptian and Phoenician history. The development of banking in ancient Rome roughly followed the Greek pattern. Banking suffered oblivion after the fall of the Roman Empire after the death of Emperor Justinian in 565 AD, and it was not until the revival of trade and commerce in the Middle ages was, however, largely confined to the Jews since the Christians were forbidden by the Canon law to indulge in the sinful act of lending money to others on interest. However, as the hold of the Church loosened with the development of trade and commerce about the thirteen century Christians also took to the lucrative business of money-lending, thereby entering into keen competition with the Jews who had hitherto monopolized the business.

As a public enterprise, banking made its first beginning around the middle of the twelfth century in Italy and the Bank of Venice, founded in 1157 was the first public banking institution. Following it were established the Bank of Barcelona

and the Bank of Genoa in 1401 and 1407 respectively. The Bank of Venice and Bank of Genoa continued to operate till the end of the eighteenth century. With the expansion of commercial activities in Northern Europe there sprang up a number of private banking houses in Europe and slowly it spread through out the world. In Nepal, modern banking starts from the establishment of Nepal Bank Limited.

1.13 Evolution of Banking Sector in Nepal

Banking service is the oldest service industry in Nepal. It has gone through the various stages of evolution and development since the Vedic times (2000 to 1400 B.C.). Though the modern banking institution has a very recent origin in Nepal, some crude bank operations were in practice even in the ancient times. In the Nepalese Chronicle, it was recorded that the new era known as Nepal Sambat was introduced by Shakhadhar, a Sudra merchant of Kantipur in 879 or 880 A.D. after having paid all the outstanding debts in the country. This shows the basis of money lending practice in ancient Nepal. Towards the end of 8th century, Gunkam Dev had borrowed money to rebuild the Kathmandu valley. In 11th century, during Malla regime there was an evidence of professional moneylenders and bankers. It is further believed that money-lending business, particularly for financing the foreign trade with Tibet, became quite popular during reign of Mallas. However, in the absence of any regulatory measures, the unscrupulous moneylenders were known to have charged exorbitant rates of interest and other extra dues on loans advanced. These inconveniences led the Prime Minister Ronoddip (1877-1885) to establish Tijarath in Kathmandu, which was a government financial institution supplying credit to the people at 5% rate of interest against security of gold, silver and ornaments. The government servants were also entitled to take loans from Tijarath, repayable from their salary at the source. During the time of Chandra Shamsheer (1901-1929), credit facilities of Tijarath were extended to some other parts of the country by opening its branches. It is believed that the so-called well-to-do persons used to take loans from private money lenders even at higher rate of

interest than those from the government institutions, for they were not prepared to disclose in public anything that was likely to affect their prestige. When they were approached by this type of clients, the professional money lenders used to raise loans in their own names from Tijarath at 5% rate of interest against gold and ornaments, which were not their own but brought to them by their clients as security for the loans to be financed from the funds raised from Tijarath itself. Thus, without any resources of their own and without any risks on their own part, the money lenders could manage very well to exploit their especial type of clients just playing the role of middlemen between their clients and the government institution. To control spurious rates of interest and also to curb unfair practice on the part of the unscrupulous moneylenders, legislative measures were also taken.

Later Tejarath was replaced by the first commercial bank, Nepal Bank Limited, during the time of Juddha Shamsheer. The establishment of Nepal Bank Limited is a great landmark in the history of modern banking as it has solved many problems and difficulties which the trade and commerce have been facing. This bank performed commercial and some of the central banking functions, as there was no central bank until Nepal Rastra Bank was established.

In 1956, the central bank of Nepal, Nepal Rastra Bank was established. It was established with the purpose of developing Banking system in the country to promote industry, trade and agriculture as well as to circulate Nepalese currency all over the country. In 2022 B.S., the second commercial bank of Nepal, Rastriya Banijya Bank, was established with hundred percent equity holding of the government. These two, NBL & RBB, commercial banks enjoyed monopoly till 2041 B.S. With the first joint venture bank, Nepal Arab Bank Limited coming in the scene the monopoly was broken and it paved the way for new joint venture banks to operate in the country.

In 2042 B.S., finance company Act was passed; but private kept stony silence till 2049 B.S. The first break came in the month of Shrawan of that year, when first company Nepal Housing and Development Finance Company came. The second came in the Poush of the same year, Nepal Finance and Saving Company. In the following three years, our financial system has witnessed the emergence of number of such finance companies.

1.14 Nepal's Financial System

The financial system of Nepal consists of a central bank, commercial banks, finance companies, development banks etc. and it is categorized in the following ways:

Organization	No of Institutions
1. Central Bank	1
2. Commercial Bank	26
3. Development Bank	63
4. Finance Companies	77
5. Micro Credit Development Banks	15
6. Non Government Organizations (NGOs)	45
7. Saving and Credit Co-operative	16

Details of list of Banks and Non Banks financial institutions as of mid July 2009 are attached in annexure.

Commercial Bank

Commercial Banks are the major component in the financial system. They work as the intermediary between depository and lenders and facilitate in overall development of the economy, with major thrust in industrial development. The

banking sector in Nepal started with the establishment of Nepal Bank Limited. Today, we got 28 commercial banks in operation.

The Nepal Bank limited was incorporated in 1937 under the Nepal Bank Act of 1937. Its authorized capital was Rs. 100 Lakh. Initially funds were raised from 20 thousand partly paid-up and 5 thousands fully paid-up ordinary shares of Rs. 100 each. By 1949-50, all the 25 thousand shares were full paid-up. It was established as a semi-government institution. Initially, 51% of share was taken by the government and the rest 49% by the general public. As a semi-public enterprise and in the absence of central banking institution, the Nepal Bank was authorized to carry on certain transactions on behalf of the government in accordance with its instruction and order. Thus, prior to the establishment Nepal Rastra Bank received deposits of government money and remitted it through bills of exchange, cheques and hundies in Nepal and foreign countries. Currently, G/N holds 41% of share in Nepal Bank Limited.

In 2022 B.S. an entirely government owned commercial bank, named Rastriya Banijya bank was established under a separate Act with the authorized capital of Rs 1 crore. Being a government owned commercial bank; its objectives and operation are somewhat different from those of the Nepal Bank Ltd. By 2045 B.S., it has expanded to 194 branches throughout the country. Currently, due to its financial position government is given management contract for two years.

The basic objective to allow foreign banks to open a joint venture with Nepal is mainly to develop the banking sector, to create healthy competition in the banking sector, to further develop the already existing old banks and to introduce new technological efficiency in the banking sector. Nepal Arab Bank limited (i.e. Nabil Bank Ltd) is the first foreign bank to be established in 2041 B.S. in Nepal. Initially, 50% of shares were owned by United Arab Emirates Bank, 20% by the

financial institutions and remaining 30% shares are owned by the general public. Five years ago the National Bank of Bangladesh bought the 50% share of United Arab Emirates Bank and later sold it to NB International (Ireland). It was established with the authorized capital of Rs 100 million, issued of Rs 50 million and paid-up capital of Rs 30 million.

Nepal Indoseuz Bank was established as second foreign bank in 2042 B.S. In this bank, 50% share was initially held by Indoseuz Bank of France, 15% share by Rastriya Banijya Bank, 15% by National Insurance Corporation and 20% by the general public. It was established with the authorized capital of Rs. 120 million, issued of Rs 30 million. Currently, its foreign JV partner is Credit Agricole.

Nepal Grindlays Bank was established as the third foreign bank in 2043 B.S. In this bank also 50% share is initially held by ANZ Bank of Australia, 35% is held by Nepal Bank Limited and remaining 15% share held by the general public. It was established with the authorized capital of Rs 100 million, issued of Rs 50 million and paid-up capital of Rs. 30 million. Currently, its JV partner is Standard Chartered Bank.

Himalayan Bank Limited was established in 1992 by the distinguished business personalities of Nepal in partnership with Employees Provident Fund and Habib Bank Limited, one of the largest commercial banks of Pakistan. It is the first commercial bank of Nepal with maximum the Nepalese private sector. Besides commercial activities, the Bank also offers industrial and merchant banking.

Apart from these banks, we already have many more commercial bank like Everest Bank Limited, Nepal Bangladesh Bank Limited, Nepal State Bank of India, Bank of Kathmandu Limited, Nepal Credit & Commercial Bank Limited, Lumbini Bank Limited, Machapuchre Bank Limited, Kumari Bank Limited,

Laxmi Bank Limited, Siddhartha Bank Limited, and Agriculture Development Bank. Apart from Commercial Banks, Finance companies, Development Banks, Co-operatives and NGOs, many non-depository financial institutions like Insurance companies, Mutual Fund etc. are also in our financial system.

1.15 Introduction to Everest Bank Limited

Everest Bank Limited (EBL), which started operations from October 18, 1994 has been established with the objective of extending professionalized banking services to various sections of the society in the kingdom of Nepal and thereby contribute to the economic development of the country.

EBL joined hands with Punjab National Bank (PNB), India as its joint venture partner in 1997. PNB is the latest nationalized bank in India having 110 years of banking history with more than 4500 offices all over India. Of which 1400 branches are interconnected. PNB has over 1000 ATMs spread across India.

Drawing its strength from PNB, EBL has set up strong systems and procedures. EBL thus has the advantage of the banking expertise and financial strength of its partner.

EBL has one of the largest networks among the private sector banks in Nepal having 35 branches across the nation and over 250 correspondents across the globe. The branches are connected through Anywhere Branch Banking System (ABBS) through which the clients can withdraw and deposit money from any branches of EBL.

Based on the audited financial results of FY 2065/066, the Bank's operating profit is Rs. 972.950 million and net profit is Rs.624.068 registering a growth of 35.35% over the previous year. The Bank's credit recorded a growth of nearly 28.30 %

over the last year reaching a figure of Rs 10136.20 million. Similarly, the total deposits of the Bank posted a growth of 38.98 % amounting to Rs 33322.946 million over the preceding year. The bank has one of the lowest non-performing assets (NPA-1.96%) among the commercial banks in Nepal.

Everest Bank limited is the pioneer and front-runner in retail lending introducing Direct Housing Finance, Vehicle Loan Scheme, Education Loan Scheme, and Loan against future lease rentals and scheme for professionals as also the loan against Lease Rentals of the properties.

Not to be left behind in technological advancement and up gradation, EBL has taken conscious decision to keep pace with the latest technology applicable to the banking sector. It has introduced 365 days banking service and in association with Smart Choice Technology (SCT) is providing ATM services for its customers. EBL Debit Card can be accessed at more than 50 ATMs and over 250 Point of Sales across the nation. The bank has managed the SCT ATM at Tribhuvan International Airport for the convenience of the customers and the travelers, the first and the only bank in Nepal to place ATM outlet at the Airport.

EBL is playing a pivotal role in facilitating remittance to and from across globe. Being the first Nepalese bank to open a representative office in Delhi, India, the Nepalese in India can open account in Nepal from the designated branches of Punjab National bank and remit their savings economically through banking channels to Nepal. The bank has a Drafts Drawing Arrangement with 175 branches of PNB all over India.

With an aim to help Nepalese citizens working abroad, the bank has entered into arrangements with banks and finance companies in different countries which

enable quick remittance of funds by the Nepalese citizens in countries like UAE, Kuwait, Bahrain, Qatar, Saudi Arabia, Malaysia, Singapore and U K.

1.4.1 Capital Structure

The paid-up capital of EBL is Rs 838.821 million (as at FY 2065/066) which includes Rs 200million convertible preference share. Issued capital is Rs 491.6 million. The dividend rate of the preference share is 9%p.a and maturity period is four years. The capital reserve is Rs 47.46 million and retained earning is Rs 108.60 million.

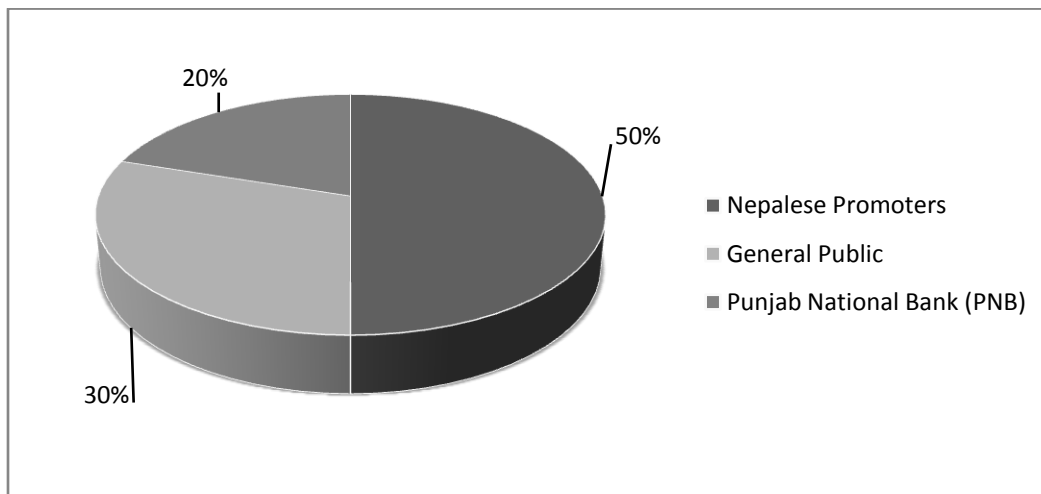
1.4.2 Share Holding Pattern

The present share holding pattern of EBL is as follows.

Table 2.1
Share holding Pattern of EBL

S.N	Sources	Percentage
1	Nepalese Promoters	50
2	General Public	30
3	Punjab National Bank (PNB)	20

Figure 1.1
Share Holding Pattern of EBL



1.16 Statement of the Problem

Financial institutions play a major role in the proper functioning of an economy. These institutions act as an intermediary between the individuals who lend and who borrow. These institutions make the flow of investment easier. It pools the funds scattered in the economy and mobilize them to the productive sector. However, these institutions inherent a large amount of risk, which cannot be, denied either. If a bank behaves irresponsibility, the costs borne by the economy are enormous. A large amount of depositors' money is at stake. And the banks and financial institutions are competing among themselves to advance credit to limited opportunity sectors. Due to unhealthy competition among the banks, the recovery of the bank credit is going towards negative trends. Non-performing credits of the banks are increasing year by year. To control such type of state, the regulatory body of the banks and financial institutions NRB has renewed directives of the credit loss provision. Therefore, it is necessary to analyze the credit management of Credit disbursement recovery provision for loss and write off the credit.

Banking sector exposed to a number of risks. These risks are broadly categorized into two segments:

- **Portfolio or On- Balance Sheet Risks**

Portfolio risks arise from various unanticipated changes in the terms of balance sheet. The size and composition of a bank's balance sheet are important determinants of its risk (variability in return) and return (profitability) profile. The most important balance sheet items are deposits, borrowings, advances and investments, which are affected by changes in interest rates, in deposit flow and loan demand, and in the ability of borrowers to repay loans. These unanticipated changes generate three basic portfolio risks namely interest rate risk, liquidity risk and credit risk. Apart from these three, there are capital risk and operational risk.

- **Off-Balance Sheet Risks**

Off-balance sheet activities risk refers to those which come in the form of contingent claims and commitments to a bank. These risks take the form of balance sheet risks only on realization of some contingency. Today due to intense competition, banks resort to off-balance sheet activities, which increase the earnings and at the same time do not lower (nominal) bank capital ratio, though they do raise risk-based capital requirement.

Such risks in excessive form had led many banks to go bankrupt in a number of countries. But due to their central role in economy, governments and the central banks try their best to rescue banks from such situations. The impact of macroeconomics conditions on the banking system requires special attention for two reasons. First, a well-functioning banking system is important for the effectiveness of the macroeconomic policies, and second, weakness that emerges in the banking system, if left unattended, could pose a threat to macroeconomic stability. Prevention of stress in a banking system requires well-balanced institutional and regulatory structures, as well as macroeconomic policy mix that is sensitive to bank's financial soundness.

The financial sector at present comprises the central bank, commercial bank, finance companies, co-operatives and (Non Government Organizations) NGOs with the limited banking activities. These banks and financial institutions have a nationwide network providing financial services. In spite of the fact that the financial sector has been enlarging rapidly in recent year, a large portion of credit demand is being met by unorganized sector i.e.: private money lender, merchant, traders, individuals, landlords at very high rate of interest which is 2-3 times higher than that of the institutional source.

In recent years, the liquidity position of banking sector are increasing year by year and it is rated as high as 24% but the still the productive sector of the economy are starved by the credit crunch. This has created a paradoxical situation in the banking sector.

Other Problem faced by banks can be pointed as follows:

- Due to limited investment sectors, banks are competing unfairly in the limited area.
- Due to poor credit administration, the credit recovery process is slow.
- Non-performing credit is going upward.
- Writing off the non-performing assets is not satisfactory.
- The legal process in recovery of credit is lengthy and ineffective.
- Clear-cut objectives and policy of the credit management is lacking.

1.17 Objectives of the Study

The financial institutions plays very vital role in the economic development of the nation. The efficient performance of the banks and financial institutions give shape to economic indicators of the nation. The failure of these sectors will certainly ruin the other sector of the economy. The hurdles lying in this sector should be identified as far possible so that it could run smoothly. The study is aimed to find those all obstacles lying and furnish them in relative to the understudied banks. Therefore, the main objective of the study is to evaluate and find out the credit management position of the Everest Bank Limited. The study try to identify the strengths and weaknesses associated in them. Besides, the above general objective, some specific objectives of the study are:

- a. To examine the information procedure in controlling the credit policies and practices of Everest Bank limited

- b. To identify norms laid by Nepal Rastra Bank with regard to loan/credit management of the bank.
- c. To know in what extent of relationship between the deposits collected and loan flowed by the banks exist.
- d. To identify the non-performing assets of EBL.
- e. To know the performance of EBL
- f. To analyze the trend of EBL.

1.18 Significance of the Study

Banking sector plays an important role in the economic development of the country. Commercial Banks are one of the vital aspects of the vital resources in the need sectors. Bank came into existence mainly with the objectives of collecting the idle funds, mobilizing them into productive sector and causing an overall economic development. The bankers have the responsibility of safeguarding the interest of the depositors, the shareholders and the society they are serving.

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

In sum, its importance can be presented as mentioned below:

a) Individual

Any individual, interested to know about the banking sector of the nation, finds a variety of information in the study. The study will supply extremely valuable facts about the banks to the depositor, loan clients, and shareholders and even to the students.

b) Organization

Every organization is interested to know about the financial condition of the Everest bank before initiating any kind of deal. The corporate client of the respective banks must know the financial situation of the banks. Every bank has a keen concern with their competitor's financial statements as it plays a vital role in plan, policy and strategy formulation.

c) Society and Government

Every government's prime responsibility is to regulate directly and indirectly to the organization operating the territory of the nation. The government has to monitor that whether the organization are exploiting the society or not. For it, it has to go through the financial statement of the organization. The study, that has analyzed the financial data of the Everest Bank Limited bank, will be benefited to the society and the government to some extent.

1.19 Focus of the Study

This study confirms the analysis of credit advances (i.e. Credit disbursed and recovery) of Everest Bank limited. The present study analytically discloses the strengths and weakness of the commercial banks in relation to credit disbursed and their recovery.

1.20 Research Questions

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

1.21 Limitation of the Study

This mini-research, conducted within a limited time constraint, is simply carried out for the partial fulfillment of the requirement of MBS. Every study has to be carried out under the domain of certain areas to make it meaningful. This study has also laid some hypothetical boundaries that are as below:

- The study mainly focuses on the importance and role of the credit management of Everest bank Limited.
- The study is associated only to the financial performance of Everest Bank Limited.
- In this study, only selected financial tools and techniques are used.
- The data of last five years i.e. FY 2061-2066 are taken for our purpose so the conclusions are drawn on basis of the period.
- The study is limited to only Everest Bank Limited. Findings or outcome of the study may not be generalized with any other banks.

1.22 Organization of the Study

The dissertations are found to be difficult to understand and create confusion if it has not partition into various heads. For our convenience, the entire thesis has been segregated into five parts. They are mentioned as below:

Chapter – I Introduction

Chapter first has been entitled as "Introduction" which deals with the general ideas about the banking sectors, general background of the study, Introduction of EBL, statement of the problem, significance of the study, objectives of the study, research questions, scheme of the study.

Chapter – II Literature Review

Part two is "Literature Review" which gives the knowledge about the literature that has been studied during the course of the preparation of the thesis. This part

portrays about the literature available in the study. It includes review of NRB articles, review of related studies, review of financial journals & economic articles and review of books.

Chapter – III Research Methodology

Third chapter is "Research Methodology" which comprises all the tools and techniques those have been adopted in the study. This chapter furnishes about the research design, source of data, population & samples, method of data analysis employed in the study.

Chapter – IV Data Presentation and Analysis

In the fourth chapter entitled "Data Presentation & Analysis", the data collected from the various sources are presented and process it in readable and understandable form. The graphs, bar Diagram, pie chart are drawn from the data obtained in this part of the study. The major findings, for which the study had been carried, are also the subject matter of this chapter.

Chapter – V Summary, Conclusion and Recommendations

The last chapter is "Summary, Conclusion, recommendation" in which the entire study is summed up. The conclusions acquired from the study are presented in the part of the chapter. After conducting the study, the researcher provides extremely vital recommendations to the scholars, relevant organizations and government in this part. Besides, above chapters, bibliography and appendixes are also included.

CHAPTER - II

LITERATURE REVIEW

The review of literature is a crucial aspect of planning of the study. The main purpose of literature review is to find out what works have been done in the area of research problem under the study and what has not been done in the field of the research study being undertaken. For review study the researcher uses different books, reports, journals, and research studies published by various institutions, unpublished dissertations submitted by master level students have been reviewed. It is divided into two headings:

- Conceptual Review
- Review of related studies

2.2 Conceptual Review

The review of textbooks and other references materials such as newspapers, Magazines, research articles, journals and past thesis have been included in this topic. Credit administration involves the creation and management of risk assets. The process of lending takes into consideration the people and system required for the evaluation and approval of loan requests, negotiation of terms, documentation, disbursement, administration of outstanding loans and workouts, knowledge of the process and awareness of its strength and weakness are important in setting objectives and goals for lending activities and for allocating available funds to various lending functions such as commercial, installment and mortgage portfolios.

The central focus of commercial banking concerns the acquisition and servicing of loans. A bank mobilizes deposits and lends to businesses. Banks lend or invest up

to 75 – 80% of their deposits. Indeed, commercial banks are the primary, if not only, source of loans for most small and medium-sized business firms and provide vital service to business organizations and to the community as a source of loans. Banks also have a responsibility to those depositors who have entrusted their funds for safekeeping. Banks also have responsibility to those who have provided debt and equity capital; thus banks are expected to operate profitably. It is through returns to equity holders in the of dividends and through retained earnings that banks are enable to continue in operation and to grow along with the communities they serve. Accordingly the well managed bank must institute loan policies designed to ensure that adequate control exists in the approval and disbursement of loans and that outstanding loan are monitored so as to ensure compliance with terms of the loan and ultimate repayment of principal and interest.

The business mainly borrows from the bank to acquire/create assets, to meet cash flow gap, to optimize return on shareholders' capital and to manage tax.

2.1.1 Types of Credit

Bank extends loan facilities by a way of fund-based facilities and non-fund based facilities. The fund-based facilities are usually allowed by way of term loans, cash credit/overdraft, and bills discounted/purchased, demand loans, overdrafts, trust receipt etc. Further, the bank also provides non fund-based facilities by way of issuance of inland and foreign letters of credit, issuance of Bid Bonds/guarantees, deferred payment guarantees etc.

- **Overdrafts/Cash Credit Accounts**

These are advances for financing current assets or advances against Bank's deposits, government securities, approved shares and debentures of companies, personal security etc. Generally the limit is fixed after assessment of the needs of the borrower, a minimum margin is prescribed and drawing power is allowed

periodically to control the withdrawals in the account. The various types of securities against which cash credits/overdrafts are allowed are pledge/hypothecation of goods or produce, pledge of documents of title to goods, mortgage of immovable property, book debts, trust securities, etc. In cash credit/overdrafts accounts the borrower is allowed to draw on account within the prescribed limit/drawing power, as and when required.

- **Demand Loans**

A demand loan account is an advance for a fixed amount and no debits to the account are made subsequent to the initial advance except for interest, insurance premium and other sundry charges. As an amount credited to a demand loan account has the effect of permanently reducing the original advance, any further drawings permitted in the account will not be secured by the demand promissory note taken to cover the original loan. Normally, demand loans are allowed against the Bank's own deposits, government securities, approved shares and debentures of companies, life insurance policies, pledge of gold/silver ornaments, and mortgage of immovable property.

- **Term Loans**

Term loans are sanctioned for acquisition of fixed assets like land, building, plant/machinery, office equipment, furniture-fixture, etc., for purchase of transport vehicles and other vehicles, for purchase of agricultural equipment, machinery and other movable assets e.g. tractors, pump sets, cattle etc. under various schemes of agricultural advances introduced from time to time, for purchase of house, consumer durables, etc. and loans under Special Schemes introduced from time to time.

- **Bills Finance**

Advances against Inland Bills are sanctioned in the form of limits for the purchase of bills or discount of bills or advance against bills sent for collection, to borrowers for their genuine trade transactions. Bills are either payable on demand or after **usance** period. Demand Bills which are payable on demand or at sight, are purchased from the parties who are sanctioned bills purchase limits and Usance Bills which are payable on maturity after a certain period of time as per terms of contract are discounted for parties who are sanctioned discount of bills limit.

- **Packing Credit (Pre-shipment)**

Packing credit is an advance given to an exporter for financing the purchase, processing or packing of goods against an export letter of credit of an approved Bank received from the buyer. Packing credit advances are generally allowed separately for each Letter of Credit to comply with the guidelines issued by NRB/EBL.

- **Trust Receipts (TRs)**

Trust receipts are used to finance the import of goods wherein the Bank releases the Bill of Lading or Airway Bill to the customer for exchange of TR signed by a customer. By signing this document, the customer gives certain undertakings to the bank. Thus, he undertakes to hold the documents, the goods represented thereby and the net proceeds thereof as Trustee for the Bank; and also undertakes to pay the proceeds of all sales to the bank and to give to the bank on request authority receive from the buyers the sale proceeds of the goods.

- **Inland Letter of Credit**

Letter of credit (LC) is issued by the bank at the request of its customer in favor of a third party informing him that the Bank undertakes to accept the bills drawn on its customers up to the amount stated in the LC subject to the fulfillment of the

conditions stipulated therein. When Bank issues a LC, it assumes responsibility to pay its beneficiary on production of bills drawn in accordance with the terms and conditions of the LC.

- **Bid Bonds**

Bank issues Bid Bonds in lieu of the security deposit/earnest money deposit/tender deposit to fulfill the requirements of the bids being made by the contractors. The terms and conditions of these Bid Bonds are based on the requirement of the tender document.

- **Guarantees**

Guarantee is a contract to perform the promise, or discharge the liability of a third person in case of his default. In the ordinary course of business, Bank often issues guarantees on behalf of its customers in favor of third parties. When Bank issues such a guarantee, it assumes a responsibility to pay the beneficiary, in the event of default made by the customer.

2.1.2 Objective of the Sound Credit Policy

The purpose of a written credit policy is:

- To assure compliance by lending personal with the bank's policies and objectives regarding the portfolio of credits and
- To provide personnel with a framework of standards within which they can operate.

2.1.3 Principle of Credit Policy

Good credit policy is essential to carry out the business of lending more effectively. Some policies are as follows:

- **Principle of Safety Fund**

Banks should look the fact that there is not any unproductive or speculative venture or dishonest behavior of the borrower.

- **Principle of Liquidity**

Liquidity refers to pay on hands when it is needed without having to sell long term assets at loss in unfavorable market. A banker has to ensure that money will come in as on demand or as per agreed terms of repayment.

- **Principle of Security**

It acts as cushion to grant advances and credits. Adequate values of collaterals ensure the recovery of credit correctly at the right time. Accepted security should be readily marketable, handy and free from encumbrance.

- **Principle of Purpose of Credit**

Generally, credit request for productive sector only be accepted rejecting credit request for speculation, social functions, pleasures trips, ceremonies and repayment of prior credit as they are unproductive.

- **Principle of Profitability**

Profitability denotes the value crested by the use of resources is more than the total of input resources. Bank should provide to such project that can provide optimum amount of return. For such purpose, bank should take a little bit risk by providing credit to venturous project.

- **Principle of Spread**

Portfolio of advances is to be spread not only among many borrowers of same industry but across the industries in order to minimize the risk of lending keeping. “Do not put your all eggs in the same basket”.

- **Principle of National Interest**

In lending and granting advances, interest of nation should not be distorted (if undermined). Priority and deprived sector of the economy and other alarming sector should be given proper emphasis while extending advances.

2.1.4 Lending Consideration

The first step of lending consideration is the availability of supporting application and other relevant documents from the customer and then processing of credit file. Prior to processing the credit file questions such as given below must be raised to the perspective customer. This is the second step of lending consideration and is called “Interviewing the customer”. While analyzing the loan application which should be include the assessment of the person(s) involved in the economy and the appraisal of the company’s performance. The analysis should revolve around the below mentioned canons of lending considerations:

- **Character**

Character is the analysis of the applicant as to his ability to meet the obligations put forth by lending institutions. The legal status of the enterprises should be noted. The historical background of the company will also help to some extent. Prior to adjoining the company’s performance it is equally important in refer to ‘controller’ of the business. It is the controller’s character and ability that needs to be closely assessed, though it’s difficult, yet it is of crucial importance as the

controllers are the cornerstone of the enterprise, and key to success of the venture. Particularly in Nepal proper assessment of the controller is very important as effective and critical analysis of the company is very difficult due to unavailability of adequate data, genuine financial statements, market surveys etc.

- **Ability**

Ability Describes about whether company achieve what is promised. It is measured by people behind the business have the managerial capability to run the business or not and whether the company have the expertise, experience, drive and past energy needed to make the business a success and justify the bank's support. For this an interview with applicant's customers/suppliers will further clarify the situation.

- **Margin**

Interest margin set the interest rate to reflect the risk, the purpose of the credit facility/ies, the period of the credit facility/ies and security. The administration cost associated with the running the credit portfolio and the associated investment in people and assets are tremendous. These investment must be paid for and yield a good return.

- **Purpose**

Purpose is to find why the facility/ies are needed. Are the reasons given satisfactory or need closer and deeper study. Example: working capital loan facility must be utilized to take care of the working capital requirement and not for financial fixed assets. To finance trading, identify specifically the loan is needed to finance more debtors, more stock, changing stock mix, slow moving stock etc. Traders who are involved in local trading only i.e. non-involvement of import/export activity mainly require revolving credit which can be an Overdraft, a Pledge Loan or a Demand Loan.

- **Amount**

Amount must be related to purpose and repayment.

- **Repayment**

Repayment mainly means to find out the income sources of the borrower. The income sources can be calculated from the sale of assets and profits from the unit.

- **Insurance**

Security should not be the sole reason for agreeing or not agreeing a loan/credit. But it does not also mean that the bank should not secure its loan. Hence, while appraising the loan application the bank must always keep in mind what will happen if things go wrong. Thus, for safety reasons it is highly desirable to obtain adequate collateral for the coverage of the credit risk.

2.1.5 Project Appraisal

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

The purpose of project appraisal is to achieve the guarantee of reasonable return from the project. Generally, following aspects need to be scrutinized and analyzed while appraising the project.

1. Financial aspect
2. Economic aspect
3. Marketing aspect
4. Technical aspect
5. Management aspect
6. Legal aspect

2.1.6 Credit Risk

Credit risk is the risk of default by borrower due to inability and/or unwillingness to repay his debts in accordance with the agreed terms and conditions. The credit risk of bank's portfolio depends on external as well as internal factors. The external factors can be economy wide as well as company specific. Some of the economy wide factors are:

- State of the economy
- Wide swings in commodity prices
- Fluctuations in foreign exchange rates and interest rates.
- Trade restrictions.
- Government policies, etc.

Some company external factors are

- Management expertise
- Company policies
- Labor relations

The internal factors within the bank, influencing credit risk for a bank is:

- Deficiencies in loan policies/administration.
- Absence of prudential credit concentration limit.
- Inadequacy defined lending limits for loan officers/credit committees.
- Deficiencies in appraisal of borrowers' financial position.
- Excessive dependence on collateral without ascertaining its quality/reliability.
- Lack of risk pricing mechanisms.
- Absence of loan review mechanisms.
- Ineffective system of monitoring of accounts.

While the bank can influence and control the internal factors to improve quality of its credit portfolio, the risk due to external factors can be minimized by proper diversification across industries and by initiating necessary changes in the loan portfolio in anticipation of adverse developments. Development of effective risk assessment and monitoring systems will help in improving the quality of credit decisions thereby reducing loan losses on an ongoing basis and thus gradually improving the quality of loan portfolio.

2.1.7 Management

Management is a process of achieving an organization's goals and objectives by judiciously making use of resources of men, materials, machines, money, methods, messages and moments. While making use of resources management should have clear vision of the future goals to be got accomplished and have the ability to effectively and efficiently coordinate the existing resources. It refers to the kind of tasks and activities that are performed by managers. The specific nature of the activities is determined by such managerial functions such as planning, organizing, directing, leadership and controlling. All managers, regardless of their level of functional area, perform these functions to some degree, although perhaps with varying emphasis.

According to F.W Taylor, "Management knows exactly what you want people to do and then seeing that they do it in the best and cheapest way".

According to Parker Follet, "Management is art of getting things done through people".

- **Planning**

Planning is the process of deciding in advance the courses of action or strategies to be followed, and when and how to undertake these, for achieving the goals and objectives of the organization.

- **Organizing**

Organizing refers to the formal grouping of people and activities to facilitate achievement of the firm's objectives. It deals with a quantitative and qualitative aspect of manpower in terms of placement, the roles they play and the relations amongst them, with the aim that they work together effectively towards accomplishing the goals, objectives and targets of the organization. It is needed for assigning responsibilities, jobs and hierarchy among personnel.

- **Controlling**

Controlling is the means of checking the progress of plans and correcting any deviations that may occur along the way. It helps to evaluate the performance, highlights abnormal deviations, and guides a manager to take specific corrective actions.

- **Directing**

Directing is the way activating plans, structure and group efforts in the desired direction. It is needed for the implementation of plans by providing desired leadership, motivation and power communication.

Management can also be grouped into three hierarchical levels named as – top, middle and lower levels. Top management establishes the policies, plans and objectives of the organization as well as a budget framework under which various departments will operate. Middle or tactical management has the responsibility of implementing the policies and overall plans of the top management. Lower or operational management has the responsibility of implementing day-to-day

operations and decisions of the middle management to produce goods and services to meet the revenue, profit and other goals, which in turn will enable the organization to achieve its overall plans and objectives.

Level of management is important because information needs tend to be different at different levels of management and amount of time required for any function varies considerably with each group.

2.1.8 Management

NRB is the authorized monitoring and supervising body that simultaneously evaluates the financial health of financial institutions. Every financial institution is liable to send their periodic financial statements as mentioned by it in prescribed formats. NRB weigh the weakness and strengths relating to them on basis of these statements. The appropriate directions are given to the concerned financial institutions for the correction of the faults and mistakes made by them. There exist various measurements for the evaluation of their financial status.

Performance Rating

Under this Method, each and every five components of CAMEL are assigned certain numerical value for Quantitative Rating. This method is also referred as Component Rating System because of the different rating of each component. During course of rating, these components are assigned maximum scale of 5 and minimum scale of 1 according to their position & condition. If any component of any financial institutions is found the excellent then number 1 is provided for it. The number 1 indicates the very strong performance of the understudied aspect. Similarly, number 5 is given to the components whose performances are very unsatisfactory and need of immediate corrective action to check it from bankruptcy.

CAMEL Rating

It is the most popular method of supervising financial institutions. The method is prescribed by BIS (Bank for International Settlement) and adopted world widely.

The full form of the word “CAMELS” is:

C- Capital Adequacy

A- Asset Quality

M- Management Quality

E- Earnings

L- Liquidity –SLR and CRR

S- Sensitivity to Risk.

a) Capital Adequacy

Every financial institution must be sound in term of capital base for its stability. The adequate capital ensures the deposit holders from the possible risk associated with the business. The sufficient capital base also enables financial institution for the additional loan out flow in various prescribed sectors. In sum, the capital adequacy promotes the depositor holders’ and creditors’ (if any) confidence on the financial institutions; loan availing capacity; enable to afford large portion of nonperforming asset and also uphold to enhance their goodwill and fame.

According to “The Basel Capital Accord” prepared by Basel Committee, the capital adequacy is measured by classifying capital in two levels: Primary Capital & Secondary Capital. The norms in term of capital laid by NRB are revised time to time.

b) Asset Quality

Investments, Loan & Advances are the prime asset of any financial institutions. The major source of income of these financial institutions is generated from the

returns obtained from these investments, loan & advances. Thus, they must be conscious about insolvency and bankruptcy.

c) Management Quality

The success and failure of any organization are determined by efficiency and capability of its management set-up. Management team not only formulates optimum policy and organizational plans but also implements for the achievement of short term and long term objective. The structure of BOD, quality of human manpower, operational cost, management information system, internal control system, decision making procedure, adoption of directives are important determinants of the qualitative management.

d) Earning

The earning & income status of any financial institution is indication of their success. The optimum utilization of the available fund, the recovery of principle and interest, return of the investment affects the earning position of financial organizations. The earning status also guarantee for the organizational stability. The earning position can be assessed by examination of the financial statement prepared at the end of the fiscal year. In this connection, the earning generation capacity and its future trend of various variables can be also evaluated from it. The earning ascertains dividend to shareholders, bonus to employee and tax to government. Every CB's are directed to allocate certain amount of income in General Reserve for the gradual increment in Capital fund.

e) Liquidity

The liquidity position of any financial institutions determines their capacity to meet their current financial obligations without any difficulty. Every financial institution must be enabling to refund the deposited amount to every deposit holders as per the demand made by them. These financial institutions are bound to

maintain statutory liquid asset as per the direction of central bank i.e. NRB. The liquid asset maintained by these financial institutions is examined by the central bank by below mentioned ways: i) On-Site Inspection ii) Special Inspection iii) Follow up Inspection iv) Off-Site Inspection

2.1.9 Spread Rate

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

Method of Calculation of the Spread as prescribed by NRB

- a. The interest spread has to be calculated on the basis of the interest paid on all deposits in Nepalese Rupee as well as Foreign Currency and Interest earned on Nepalese Rupee and Foreign Currency lending, investments, money at call as well as balance held in foreign nostro accounts.
- b. For the purpose of obtaining average weighted deposit rate, the interest expenses for the particular period shall be divided by the monthly average deposit of the same period with the quotient multiplied by 100. Similarly, for the purpose of obtaining average weighted loan rate, the interest income from lending, investment, money at call and foreign nostro account for a particular period shall be divided by the monthly average balances (of loan, investment, money at call and foreign nostro accounts) of the same period with the quotient multiplied by 100.

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

Interest Spread Rate= WALR- WADR

Where WALR= Weighted Average Lending Rate

WADR= Weighted Average Deposit Rate

2.2 Review of Related Studies

2.2.1 Review of Articles

Srnivasan and Yung (1988), in their well read article, "*A Case Study of Corporate Credit Management*", explained an expert credit granting system prototype in designing expert financial systems. Credit granting process in the participating corporation considered of two distinct phases (1) a customer evaluation phase, where the customer's credit worthiness is evaluated based on a variety of criteria; and ii) a credit limit determination phase, where the conclusions of the analysis are transformed into a credit limit or the customer. System design was therefore, split into two phase, (i) development of an appropriate data base and knowledge base to support the customer evaluation process and (ii) development of an appropriate model to support the credit limit determination phase.

This article has assumed to describe an expert credit granting prototype designed for a fortune 500 corporation. The focus has been on the conceptual process undertaken for designing the prototype. The model base and rules that comprise the prototype are combination of normative prescriptions and managerial preferences presented in a user-friendly environment issues that need conscious recognition in implementing such

Expert systems in corporate finance were also brought forth. The progress in

computer and information technologies has provided financial researcher an opportunity to affect a transfer of the expertise contained in normative model to practicing managers through the medium of intelligent computer systems. This is a modest attempt to provide a conceptual foundation to this notion and illustrate its feasibility.

Shaw and Gentry (1988), in their well read article, “*Managing and Recommending Business Loan Evaluation (Marble) System*”, generalized expert system that minimize the lending expertise of several banking and finance professionals. The objectives of MARBLE are to help lending officer, credit analysis, and loan review committees to improve the evaluation of loan applicants and to learn how expert system operate. Based on the knowledge base and the information provided on the loan applicant, MARBLE synthesizes the information and estimates the likelihood that the loan will be repaid. Knowing that the conclusion recommended by MARBLE reflects the judgments of lending experts, management can use it to assist in the lending decision. The MARBLE system has the capability of learning from decision examples. Examples were used to show the value of inductive inference in the knowledge acquisition process. This learning capability makes it possible to build an intelligent decision support system. An empirical study shows encouraging result for incorporating inductive learning in MARBLE for loan evaluation.

Duchassi, Shawk, and Seagle (1988), in their well read article, “*A Knowledge-Engineered System for Commercial Loan Decisions*”, have showed Commercial Loan Analysis Support System (CLASS). This article describe an expert system, commercial loan analysis support system (CLASS) is an expert system designed to evaluate a company's financial posture, recommend

commercial loan decision and pertinent components, and document the loan analysis. Like a loan officer, CLASS constitutively synthesizes a large number of detailed facts into a loan recommendation.

CLASS has been designed to seek out any potential weakness in the prospective borrower and conduct an extensive detailed analysis of each weakness. Weaknesses may be over analyzed but none will be overlooked. This approach is consistent with the general notion in commercial lending that one is primarily concerned with weaknesses instead of strong points which are taken for granted. In addition to the limited validation conducted by the expert a more comprehensive validation can be implemented in two ways. First, the system can be empirically tested with a large sample of historical loan decisions. Second field tested can be conducted in which loan officer use CLASS while making actual loan decisions. Their judgments can be compared to those of CLASS at each step in the analysis. By building CLASS, it was demonstrated that financial knowledge can be represented and applied to a complex financial problem. It is hoped that the approach described here will pave the way for building expert systems that address other important financial problems.

Keith (1999), in his well read article, "*An Evaluation of Bank Credit Policies for Farm Loan Portfolios using the Simulation Approach*", stated that when many borrowers are combined to form a portfolio, borrowers may be graded on a common basis through the expected loss spectrum for default risk and security risk using a two-dimensional risk classification matrix structure. The extent to which unexpected losses on individual loan securities are correlated defines systematic risk while the remaining portfolio risk constitutes unsystematic risk. Systematic risk among loan securities occurs as a result of correlation of loss probabilities between different types of borrowers. Since the probability of default of

borrowers is directly related to their income distributions, correlations of loss distributions occurs as a result of a common set of exogenous factors affecting income distributions of borrowers in different regions and industries. Beta risk on loan securities is therefore assessed on the basis of securities classified for regional and industry segmentations.

Ghimire (2003), in his article, "*Credit Sector Reform and NRB*", has tried to highlight the effects of change or amendment in NRB directives regarding loan classification and loan loss provisioning. Although the circumstances leading to financial problem or crisis in many Nepali banks differ in many respects, what are common across of the most banks, which increased size of non-performing assets (NPA)? To resolve the problem of the losses or likely losses of this nature facing the industry, NRB as the central bank, amended several old directives and issued many new circulars in the recent years.

Since majority of the loans of most of the commercial banks of the country at present falls under substandard, doubtful and even loss categories, loan loss provisioning now compared to previous arrangement would be dramatically higher. The new classification and provisioning norms are very lenient as they help to strengthen banks financially. He added that the old system remained in force from 1991 to 2001, which was probably the most volatile decade of the business operation of the country. He has indicated that loan loss provisioning as a percentage of total credit of April 1, 2001 is 5.2% but as April 13, 2003, it has jumped to 18.39%. If only private banks are considered, it is 2.12% of April 2001 where as it is 6.30 % as of April 13, 2003. The total increment in loan loss provision is Rs 11,328.11 million and the total increment in credit is only Rs 7,976.70. He has also stated that tightening provisioning requirements on NPL is essential to ensure that banks remain liquid even during economic

downturns.

NRB has worked for management and reform of the credit of the financial institution more seriously and NRB has adopted reforms aimed not just at dealing with problem banks but also at strengthening banking supervision to reduce the likelihood of future crisis. All prudential directives of NRB in connection of credit sector reform have been made revised on after April 2001. To adapt to such changes there can be some difficulties and for a better and harmonized reform, NRB should continue to be supportive, proactive and also participative to take opinions of bankers for a change in regulation/policy taking place in the future.

Satyaj (2005), in his article, "*Entrepreneur-Friendly Credit Policy*", has reviewed the present credit policy with main focus of the credit decision being based on the collateral. He argues that only collateral should not be considered as the basis of the credit decision.

Access to finance is vital element for entrepreneurship development in the country. Without it, one cannot think of starting business of any sort. It's mainly due to this reason; most of the students after completing there single-mindedly look for employment opportunity. No other options, no matter how attractive it would be enter into their mind. It has created huge pressure in the labor market. In the absence of entrepreneurial activities in the country, employment opportunity will be very limited and even qualified and competent people do not get job. The established notion of the Nepalese bankers that money lent to the wealthy people based on collateral is safe. But is not actually a safe assumption in the face of greater difficulty in loan recovery form these people. Also, this particular segment of market is already over-banked. With the worsening business performance of the Nepalese corporate sector mostly

due to the poor management compounded by other factors like sluggish economic conditions and political instability, banks must now explore newer market segment for their sustained growth and success. Under this backdrop, Nepalese commercial banks must change their policy and must understand that event the people living in the low and middle level of economic pyramid can potentially be lucrative market.

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

Garg (2006), in his well read article, “*Principles of Lending and Credit Culture at Rastriya Banijya Bank*”, has concluded that banks credit culture is the unique combination of policies, practices, experience, and management attitudes that defines the lending environment and determines the lending behavior acceptable to the bank. Loans are not be made unless there is a demonstrated capability for repayment. Lending culture can take cash flows as opposed to security. Every credit must be subject to rigorous analytical scrutiny of the customer’s repayment capability prior to approval, and on an ongoing basis following approval. There can be no exceptions to the basics principles of lending.

Dhungana (2006), in his well article, “*Problems of NPL’s and the Need of Financial Discipline in the Nepalese Banking System*”, has concluded that poor

credit management and deterioration in the quality of loans give birth to non-performing assets. The internal measures play significance role to control the growth of NPL. Best credit practices, culture and policies are required to strengthen the internal factors. The banks should have a proper system and competency on risk management and should insure that risk are accurately identified, assessed and controlled properly. A proper risk management is undoubtedly an important tool for a good banking and NPL management.

He further states that it can be expected that the financial sector reforms will lower down the level of NPL from the existing level and strengthening the banks and financial institution internally to manage the credit portfolio efficiently and support will be continued to make a good credit culture in the system.

Bhandari (2007), in his well read article, “*Etiology and Strategy of Loan Repayment*”, has concluded that lending agencies should adopt several strategies for achieving their target of credit repayment. However, before enforcing coercive actions against entrepreneur and the enterprise, the banks and the lending agencies should follow a series of liberal strategies for recovering their loans.

Zerith (2008), in her article well read 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. Now, many banks view the credit portfolio in its segments and as a whole and consider the relationships among portfolio segments as well as among loans. These practices provide management with a more complete picture of the bank’s credit risk profile and with more tools to analyze and control the risk.

Zerith further concluded that effective credit portfolio management begins with oversight of the risk in individual loans. Prudent risk selection is vital to maintaining favorable lending quality. Therefore, the historical emphasis on controlling the quality of individual credit approvals and managing the performance of lending continues to be essential. But better technology and information systems have opened the door to better management methods. A portfolio manager can now obtain early indications of increasing risk by taking a more comprehensive view of the credit portfolio.

2.2.2 Review of Thesis

Regmi (2005), submitted thesis named “*Credit Management of Commercial Banks with reference to Nepal Bangladesh Bank and Bank of Kathmandu*”. His research major objectives relevant to my research are:

- Role of credit management in financial institutions of Nepal.

Major findings:

- Both Nepal Bangladesh and Bank of Kathmandu have utilized most funds in the form of credit and advances. Almost 80% of total deposits of the bank have been forwarded to customers as a credit and advances.
- Provisions for credit loss have been increasing year by year for both the banks.
- Equity portion of total sources of the bank is slightly increasing in the recent years because NRB has issued directives to the entire bank to increase its paid up capital.

Recommendation:

- Banks should avoid extending credits merely based on oral information presented at the credit interview. Historical financial and trade records, as

well as realistic cash flow projections should be obtained for proper assessment of the proposal.

- Banks should regularly follow the credit customer to confirm that whether the customers have utilized their credit for the same purpose committed at the time of taking credit from the bank.
- Some customers are unsatisfied with the service charges and interest of credit; therefore banks should decrease service charges and interest charges.
- Bank's efficiency should be increased to satisfy the demand of depositors at low level of cash and bank balance.

Singh (2005), the thesis entitled *"A Comparative Evaluation of Financial Performance of Nepal Arab Bank Ltd. And standard chartered Bank Nepal Ltd."* showed that liquidity position of both the banks is below the standard. To evaluate the income and expenditure of the both banks was the prime objective of the researcher. The conclusions drawn from the study were:

- NABIL had been capable to maintain better liquidity position as comparative to SCBNL.
- The turnover ratio showed that NABIL is more efficient in utilizing its sources than SCBNL. NABIL's (investment & advance)/deposit ratio was 57% whereas later was 41%.
- The profitability ratios of those banks were found to be satisfactory. However, figure showed that SCBNL had higher profitability ratios than NABIL.
- NABIL seemed to be more efficient in utilizing its capital for generating interest income.

Ghale (2006), thesis entitled *"A Study on Comparative Analysis of Financial Performance of Joint Venture Banks in Nepal: NABIL & NBBL"* was intended to

evaluate the financial performance of NABIL and NBBL. The researcher has been able to find the mentioned facts relevant to those banks:

- Liquidity Position of NABIL was higher than that of NBBL.
- The profitability ratios showed that both banks were able to earn significantly. However, EPS ratio of NABIL bank was higher than NBBL. The reason behind the less earning of NBBL was its low capital base. The DPS trend of NABIL was positive and greater than NBBL.
- The composition of the operating expenditure showed that NBBL was paying more of its income in paying interest, commission and general expenses.

Parajuli (2006), entitled "*A Comparative Study of Financial Performance of Joint Venture Banks in Nepal*" is the topic of the thesis intended to evaluate effectiveness of monitoring and collecting policy of banks. The study was limited between Nepal Arab Bank and Standard Chartered Bank Nepal Ltd. among various joint venture banks. The researcher has able to conclude the following points:

- The liquidity ratio portrays that the liquidity position is relatively higher in case of NABIL.
- NABIL had better performance than SCBNL in term of the activity ratio. The researcher pointed the reason behind it that NABIL might have comparatively better lending policy than SCBNL.
- Profitability ratios (Net Profit to Total Asset, Net Profit to Total Deposit, Net Profit to Total Capital Employed, EPS) were found higher than NABIL but DPS was higher in case of NABIL.

Bohara (2007), thesis entitled, "*A Comparative Study of Financial Performance of Nepal Arab Bank Ltd. and Nepal Investment Bank Ltd.*" was aimed to highlight

the function and policies of joint venture banks especially those banks that are under study. The findings of the study were:

- Both banks had enough current asset to settle its current liability but so far as comparative analysis is concerned, the current Ratios of NIBL were higher than NABIL.
- Profitability ratios of NABIL were obtained higher than the later one. The researcher further discovered that it was the result of adoption of the better lending portfolio by the particular bank.
- DPS provided by NIBL was high enough to satisfy its shareholder properly than that of NABIL.

Sejuwal (2007), in his Master's Thesis, "*A Comparative Study on Credit Management of Commercial Banks; with Special Reference to NABIL and SCBNL*", has the main objective to explore the credit efficiency or inefficiency and its management in commercial banks. The specific objectives of the study are;

- a. To assess credit practice of selected commercial banks.
- b. To explore the credit efficiency of selected commercial banks.
- c. To explore the relationship with loan and advances, non-performing loan and net profit of selected commercial banks.

His research findings are;

- a. The credit practices of NABIL in terms of total loans to deposit ratio is found to be more than SCBNL (i.e. $0.6298 > 0.3660$). It indicates that NABIL has been strong to mobilize its total deposit as loan.
- b. In terms of interest income to loan and advances ratio, Nabil has mean score of 0.0932 and SCBNL has the mean score of 0.0858. From this point, NABIL Bank has the best performance in earning interest income.
- c. Lending policy of SCBNL with regard to non-performing loan to total loans and advances was found to be the lowest with the mean value with 0.0351

- as compare to NABIL Bank. The result indicates that if non-performing loan increases, the overall banking business will be negatively affected.
- d. The ratio of loans and advances to total assets was found greater in NABIL in comparison with SCBNL which shows the good lending performance of NABIL, whereas in terms of loan and advances to current assets ratio, NABIL has highest mean than that of SCBNL, this meant that NABIL has relatively better practice in short term lending.
 - e. Lending policy of SCBNL in terms of loan loss provision to total loans and advances was found relatively better than that of NABIL.

Adhikari (2008), in her Master's Thesis, "*Credit Management of Siddhartha Vikash Bank Limited*", has the main objective to analyze the credit management of the SVBL. The specific objectives of the study are;

- a. To analyze the trends of deposit collection and credit lending.
- b. To assess total amount of loan.
- c. To evaluate the performance of SVBL in terms of liquidity, profitability, sector wise loan, and non-performing loan.
- d. To analyze the capital adequacy of SVBL.

The major findings of the study are;

- a. Deposit collection of SVBL has significantly increasing trend. There is continuous increasing trend from 10 percent to 100 percent.
- b. In all year total fixed deposit has more contribution than other deposit. Then more contribution of saving deposit than that of current and call deposit.
- c. Correlation between deposit and loan disbursement is 0.99. This indicates that these two variables relation is highly positive.
- d. Capital adequacy of the SVBL has sufficient against NRB standard. It indicates that the lending capacity of SVBL is high.
- e. The highest risk of SVBL is in credit risk.

Neupane (2009), in his Master's Thesis, "*Credit Policy Analysis of Commercial Bank with Special reference to Everest Bank Limited*", has the main objective to find out the credit management position of Everest Bank Limited.

The specific objectives of the study are;

- a. To evaluate the various financial ratios of the EBL.
- b. To determine the impact of deposit in liquidity and its effect on lending practices.
- c. To analyze trend of deposit utilization towards loan and advances and net profit.

The major findings of the study are;

- a. Cash and bank balance to current deposit of the bank shows the fluctuating trend during the study period. Similarly, cash and bank balance to interest sensitive ratio of EBL is also in fluctuating trend.
- b. Credit and advance to fixed deposit ratio of EBL is fluctuating trend. The mean ratio is 2.26 times in the study period. However, non-performing assets to total assets of EBL is in declining trend, whose mean ratio is 0.978%.
- c. The debt to assets ratio of EBL is excessively high or in other words they have excessively geared capital structure. On an average 93% of assets is financed through debt capital that is outsiders cost bearing fund.
- d. Return on loan and advances of EBL is also in fluctuating trend. The mean ratio is 2.2%. This shows the normal earning capacity of EBL.

2.3 Research Gap

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 credit management of Everest Bank. Thus, the previous

studies can't be ignored because they provide the foundation to the present study. In other words, there has to be continuity in research. This continuity in research is ensured by linking the present study with the past research. This continuity in research is ensured by linking the present study with the past research studies. Here, it is clear that the new research cannot be found on that exact topic, i.e. Credit Management: A study on Everest Bank limited. Therefore, to fulfill this gap, this research is selected. To complete this research work: many books, journals, articles and various published and unpublished dissertations are followed as a guideline to make the research easier and smooth. In this regard, here we are going to analyze the different procedure of credit management, which is considered only on Everest Bank. Our main research problem is to analyze whether the Everest Bank limited has the 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. Similarly, trend analysis of investment and profit are reviewed to make this research complete. Therefore, this study is useful to the concerned bank as well as different persons: such as shareholders, investors, policy makers, stock brokers, state of government etc

CHAPTER - III

RESEARCH METHODOLOGY

“Research Methodology refers to the various sequential steps to adopt by a research in studying a problem with certain objective in view” (Joshi, 2001). Methodology is the research method used to test the hypothesis. Every study is intended towards the analysis, discover and actual position of any situation. The findings are possible only with help of certain tools and techniques. The research oriented task ask for serious consideration on research design; sample size; sources of data; data collecting instruments and procedure; data tabulation; data analyzing techniques to be adopted and study limitation in term of tools unavailable. The basic objective of this study is to highlight the role and importance of credit management in Everest Bank Limited. This study tries to answer the following research questions;

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

In order to achieve the pre-determined objectives of this study certain research methodology has been applied. So the purpose of this chapter is to present and explain the research methods applied in this study.

3.2 Research Design

Research design is the plan, structure and strategy of investigation conceived so as to obtain answers to research questions and to control variance (Wolff & Pant, 1999). It is the task of defining path for solution of the research problem. In other words, it is the outline of a plan to test the hypothesis and should include all the procedures that follow. The basic objective of research design is just to check the researcher for deviate from actual course of action. The basic objective of the study is to examine the existing policies and practices of credit management of Everest Bank Limited, its role, its effectiveness in decision making and to provide suggestion for better information system.

According to the type of the research design, this thesis falls under descriptive and analytical design. It lies under analytical design as it tries to analyze the financial data to reach at conclusion. At the sometime, it also represents descriptive research design as it describes much more about the efficiency of the understudied banks. The research will mainly base on the primary data and information provided by the bank. On the basis of qualitative and quantitative information the analytical framework will be drawn. After the evaluation of this information the interpretation will be presented as an outcome. The study after its conclusion, recommendation has been given in the end based on the findings.

3.2.1 Sample Size

A Sample is that part of the universe which we select for the purpose of investigation (Mr. Gupta, 1995). Sampling technique is very much essential for conducting any research. It allows the researcher more time to make an intensive study of the research problem. When the study of whole population is not possible, the sampling technique is adopted. The ideal sampling represents the whole universe accurately and independently. For the study purpose too, sampling is done while extracting data required. The study of financial data of some banks

from very beginning period makes the study lengthy and vague. Thus, the financial data of recent six years are taken as sampling for the study.

There are twenty six commercial banks operating in the political boundary of the nation. Among them, Everest Bank Limited has been selected as sample for the present study. Similarly, financial statements of EBL for 7 years i.e. FY 2059-2066 have been taken as samples for the same purpose.

3.2.2 Sources of Data

The sources of the information required for any study will be either primary or secondary data. The data possessing original character and collected from actual field by the researcher or through agent for the first time is known as primary data. The data are utilized when secondary data are not accessible easily. The data compiled by previous researchers for their purpose is known as secondary data. The use of secondary data reduces the considerable amount of time and tension of collecting information from the actual workplace. The data obtained from these sources are unstructured. Secondary data is collected or applied for the study will be obtained form journals, books, web sites, newspapers and other sources. Official records and publications on related field are also used for the study. The sources of data selected are authentic and reliable and cross checking of data has been done. The secondary data used are internal reports, annual reports and published materials of EBL, Nepal Rastra Bank directives and other sources.

3.2.3 Data Analysis Tools & Techniques

The data and information, obtained from the related field, are found in rude form and need further processing to make it readable and understandable. The data should be analyzed by the use of various tools and techniques. The adopted tools may be statistical, financial or banking tools.

3.2.3.1 Financial Analysis

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

“Ratio, in general, refers to the quantitative relationship between two sets of arithmetical data” (Rana, 2000). Although there are various ratios relating to the evaluation of firm’s performance, few ratios are merely taken into consideration for our purpose. The study covers those ratios that are relating to our subject matter. Financial ratios can be grouped into following types:

- a. Liquidity Ratio
- b. Credit Ratio
- c. Stability Ratio
- d. Deposit Composition
- e. Credit Composition
- f. Investment Composition
- g. Trend Analysis

a) Liquidity Ratios

Liquidity ratios measure the firm’s ability to meet term financial obligation out of current or liquid assets. These ratios basically concentrate on current assets and liabilities and used to ascertain immediate commitments made by the firms.

i) Cash Reserve Ratio (CRR)

$$\text{Cash Reserve Ratio} = \frac{\text{Cash in Vault} + \text{NRB Balance}}{\text{Total Deposit}}$$

The ratio attempts to explain about the liquidity position of any financial institutions. NRB, as a regulatory body, has directed to financial institutions to

maintain certain percentage (%) of CRR. Further, NRB regularly analyze the financial statement submitted by financial institutions to know their financial health along with CRR. NRB will levy penalty in case of unable to maintain prescribed level of CRR.

ii) NRB Balance to Total Deposit

$$\text{NRB Balance to Total Deposit} = \frac{\text{NRB Balance}}{\text{Total Deposit}}$$

Every CB has to maintain their account in NRB and keep their surplus deposit at their nostro account maintained with NRB. The deposit maintained with NRB can be treated as liquid fund. Thus, the larger amount of deposit maintained with NRB account is preferable from the liquidity point of view.

iii) Cash in Vault to Total Deposit

$$\text{Cash in Vault to Total Deposit} = \frac{\text{Cash in Vault}}{\text{Total Deposit}}$$

The certain amount of cash should be maintained to meet immediate demand of customers and meet day to day expenses. The cash maintained at their vault are liquid fund and should be at optimum point. The maximum amount of cash in vault is preferable from liquidity point of view but it may be dangerous from the point of view of profitability and security.

b) Credit Ratio

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

i) Total Credit to Total Deposit

$$\text{Total Credit to Total Deposit} = \frac{\text{Total Credit}}{\text{Total Deposit}}$$

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

ii) Total Credit to Fixed Deposit

$$\text{Total Credit to Fixed Deposit} = \frac{\text{Total Credit}}{\text{Fixed Deposit}}$$

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

iii) Total Credit to Saving Deposit

$$\text{Total Credit to Saving Deposit} = \frac{\text{Total Credit}}{\text{Saving Deposit}}$$

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

c) Stability Ratio

The solvency position of any financial institutions is measured by their capital. The huge accumulated capital ensures about the longer and safe of these financial institutions. Their capital bases are matter of concern of outsiders, insiders and regulatory bodies. Relatively, higher capital instills confidence in the mind of

depositors & creditors. In certain long term project financing, preference is placed on capital funds to deposit. It is evaluated by the use of the below mentioned ratios:

i) Capital to Total Deposit

$$\text{Capital to Total Deposit} = \frac{\text{Capital}}{\text{Total Deposit}}$$

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

ii) Capital to Total Credit

$$\text{Capital to Total Credit} = \frac{\text{Capital}}{\text{Total Credit}}$$

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

iii) Capital to Total Risk Asset

$$\text{Capital to Total Risk Asset} = \frac{\text{Capital}}{\text{Total Risk Asset}}$$

The ratio tells about the comparative position of capital and total risk asset. The solvency position of any financial institutions will be in danger if the capital is

very less than the total risk asset. The ratio having higher value is preferable in comparison to lower ratio. The higher ratio ensures about the greater amount of capital.

d) Other Ratios

There are so many other ratios that are key indicator of the performance of any financial institutions. The other ratios are:

i. Earning Per Share(EPS)

EPS is one of the most widely quoted statistics when there is a discussion of a company's performance or share value. It is the profit after tax figure that is divided by the number of common shares to calculate the value of earnings per share. This figure tells us what profit the common shareholders for every share held have earned. A company can decide whether to increase or reduce the number of shares on issue. This decision will automatically affect the earnings per share. The profits available to the ordinary shareholders are represented by net profit after taxes and preference dividend. Symbolic expression of EPS is given below.

EPS = Net Profit After Tax / Number of Common Stock Outstanding

ii. Price Earning Ratio (P/E Ratio)

The P/E ratio is widely used by the security analysis to evaluate the firm's performance as expected by investors. It shows the price currently paid by the market for each rupee of currently reported earning per share. It is also called multiplier. Here, the expression takes place as follows:

$$\text{P/E Ratio} = \frac{\text{Market Price Per Share}}{\text{Earning Per Share}}$$

CHAPTER - IV

DATA PRESENTATION AND ANALYSIS

This chapter deals with the presentation, analysis and interpretation of relevant data of EBL in order to fulfill the objectives of this study. To obtain the best result, the data have been analyzed according to the research methodology as mentioned in third chapter. “A report can be worthless if interpretation is faulty, even if valid and reliable data have been collected.”

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

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

4.7 Credit Management of EBL

In order to enhance and strengthen the credit management of the Bank, Everest Bank Limited has implemented various credit policies and practices with consent to NRB rules and regulation before the credit proposal or appraisal is being made and after the credit exposure has been sanctioned to the borrower.

Credit proposals in favor of borrowers will be considered by various officers of the Bank in accordance with the broad guidelines laid down in this circular. Nepal Rastra Bank's guidelines/norms regarding lending by Bank's in Nepal have been kept in view while formulating the guidelines.

Table 4.1
Showing Capital Adequacy Ratios

Rs. in Thousand

Particulars	Aashad 2062	Ashad2063	Aashad 2064	Ashad 2065
Core Capital	597,009	663,269	815,567	92,75,50
Capital Fund	684,163	766,879	1,24,75,62	1,39,13,39
Total risk Assets	5,707,030	6,924,807	9,195,588	11,29,11,37
Core Capital/Total risk Assets	10.46%	9.58%	8.88%	8.21%
Capital/ total Risk Assets	11.99 %	11.07 %	13.57 %	12.32%
Excess in Total Capital Fund	1.99%	0.07%	2.57%	1.32%
Excess in Core Capital	5.46%	4.08%	3.38%	2.71%

Source: EBL's Annual Report

In table, CAR (Capital Adequacy Ratio) in Core Capital of EBL has been found 10.46%, 9.58%, 8.88% & 8.21% of total risk asset in Aashad 2062-Aashad 2065 respectively whereas the Capital Adequacy Ratio in terms of capital fund has been found 11.99%, 11.07%, 13.57% and 12.32% of total risk asset in Aashad 2062-Aashad 2065. Nepal Rastra Bank earlier provided that the Capital Adequacy ratio should be 8%. This has since been increased to 11% (which is further increased to 12% from the financial year 2063/064). The EBL Capital Adequacy ratio stands at 12.32%, inclusive of provision of 20% dividend as bonus share. In order to improve Capital Adequacy ratio, the board of EBL decided to issue debentures of Rs 30 crore. This was subscribed overwhelmingly and allotment completed. These debentures are also listed on the Nepal Stock Exchange Ltd. It clearly gives sense that EBL has complied NRB directive of capital adequacy ratio in all four year.

Table 4.2

The classification and provisioning of Non-performing Assets of Everest Bank limited for the period of 5 years (FY 2062-2066) as per the NRB guidelines is as under

S. No.	Particulars	Ashadh 2062			Ashadh 2063		
		Amount	%age	Provision	Amount	%age	Provision
1	Pass Loan	37493.55	92.71	374.94	46284.17	91.66	462.84
2	Sub-Standard Loan	157.41	0.39	39.33	254.70	0.50	63.67
3	Doubtful Loan	175.83	0.43	87.91	140.94	0.28	70.47
4	Loss Loan	79.77	0.20	79.77	346.72	0.69	346.72
5	Rescheduled Loan	2535.72	6.27	316.96	3469.26	6.87	499.92
	Total of (2+3+4+5)	2948.73	100.00	898.91	4211.62	100.00	1443.62
	GRAND TOTAL	40442.28		1273.85	50495.79		1906.46

S. No.	Particulars	Ashadh 2064			Ashadh 2065			Ashadh 2066		
		Amount	%age	Provision	Amount	%age	Provision	Amount	%age	Provision
1	Pass Loan	55834.36	91.59	558.34	74235.70	93.97	742.35	97265.03	95.96	
	Bills Purchased	0.00	0.00	-	296.35	0.38	2.96	306.95	0.30	
	Hotel Oriental	142.09	0.23	1.42	162.16	0.21	0.00		0.00	
		55976.45	91.83	559.76	74694.21	94.55	745.31	97571.98	96.26	975.71
2	Sub-Standard Loan	110.83	0.18	110.83	44.09	0.06	44.09	106.69	0.11	31.69
3	Doubtful Loan	404.95	0.66	404.95	19.77	0.03	19.77	6.84	0.01	6.84
4	Loss Loan	531.78	0.87	531.78	1224.22	1.55	1224.21	1178.83	1.16	1178.83
	Total NPA :-	1047.56	1.72	1047.56	1288.08	1.63	1288.07	1292.36	1.27	1217.36
5	Rescheduled Loan	3934.40	6.45	491.80	3018.61	3.82	377.32	2498.24	2.45	312.28
		Additional prov.		18.06	Additional prov.		403.48	Additional prov.		844.12
	Total of (2+3+4+5)	4981.96	100	1557.42	4306.69	100	2068.87	3790.60	100	2373.76
	GRAND TOTAL	60958.41		2117.18	79000.90		2814.18	101362.58		3349.47

Source: EBL's Annual Report

- Gross non-performing assets (including substandard, doubtful, loss and rescheduled accounts) constitute 3.74% of the total credit as against 5.45% of Aashad 2065, 8.17% of Aashad 2064, 8.34% of Aashad 2063, 7.29% of Aashad 2062, 6.80% of Aashad 2061. This shows that the percentage of non-performing assets of the total credit is in decreasing trend and low.
- The Gross Non performing Assets excluding rescheduled accounts is 1.27% as against 1.63% for the year ended Aashad 2065, 1.72% for the year ended Aashad 2064, 1.47% for the year ended Aashad 2063, 1.02% for the year ended Aashad 2062 and 5.95% for the year ended Aashad 2061.
- Against the non performing Assets of Rs 413.01 Lacs the provision have made of Rs 207.01 Lacs i.e. 50.12% for the period of Aashad 2062. Non performing Assets of Rs 742.36 Lacs the provision have made of Rs 480.86 Lacs i.e. 64.77 % for the period of Aashad 2063. Non performing Assets of Rs 1047.56 Lacs the provision have made of Rs 1047.56 Lacs i.e. 100 % for the period of Aashad 2064. Non performing Assets of Rs 1288.08 Lacs the provision have made of Rs 1288.07 Lacs i.e. 100 % for the period of Aashad 2065 and Non performing Assets of Rs 1292.36 Lacs the provision have made of Rs 1217.36 Lacs i.e. 94.20 % for the period of Aashad 2066. As per the NRB guidelines Loan loss provision of 25% on Substandard Loan, 50% on Doubtful Loan and 100% on Loss Loan, the figure shows that Ebl has followed the NRB guidelines.
- The ratio of Net-Non performing Assets (All NPA-provision) and Net-credit (total credit-provision) was 1.45 %(including rescheduled accounts) in FY 2066, 2.94% in FY 2065 and 5.82% in FY 2064.
- The EBL has made provision of Rs 402.25 Lacs for Non Banking Assets as per NRB guidelines (i.e. Total Non Banking Assets=Rs 476.61 Lacs, provision =Rs 402.25 Lacs).

4.1.1 Total Credit % to be invested in Priority Sector

Circular No.Bai.Bya.Pa.Pa. 92/059 dated 2059.9.8/December 23, 2002 has provided the requisite proportion of Priority Sector lending (Deprived Sector remains unchanged) as follows:

Table 4.3
Total Credit % to be invested in Priority Sector

Fiscal Year		Minimum Percent of Total Credit to be invested in Priority Sector
2061/62	2005/06	7%
2062/63	2006/07	6%
2063/64	2007/08	4%
2064/65	2008/09	2%
2065/66	2009/10	2%

Source: NRB Directives Manual

Effective FY 2064/65 (2007/08), investment in Priority Sector shall not be compulsory. Required Lending to Deprived Sector (Amended by Circular No.Bai.Bya.Pa.Pa. 58/057 dated 2057.3.5).

Table 4.4**Priority Sector Lending and Deprived Loans of EBL on FY 2062 to FY 2066**

Rs in Lacks

	Ashadh 62		Ashadh 63		Ashadh 64		Ashadh 65		Ashadh 66	
	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount
Priority Sector	1003	4982.84	1178	5506.1	1028	6199.5	965	7186.01	887	8506.32
(A) Direct Investment	993	3965.84	1167	4313.84	1017	4682.9	953	5249.81	873	5688.88
.Agriculture	220	285.64	224	368.87	139	237.82	73	180.47	15	67.16
Cottage Industries	223	1583.44	222	1734.66	244	2020.3	219	1822	242	2216.57
Services	544	2077.73	712	2178.88	634	2424.8	661	3247.34	614	3393.66
Energy base										
Machine & Import of	6	19.03	9	31.43					2	11.49
Raw materials										
(B) Indirect Investment	10	1017	11	1192.26	11	1516.6	12	1936.2	14	2817.44
Deprived Loans	299	1136.29	309	1310.19	306	1728.5	204	2251.24	158	3208.44
(A) Direct Investment	289	119.29	298	117.93	295	211.74	193	315.04	144	391
Agriculture	156	42.56	142	30.48	123	30.82	72	115.61	56	213.38
Cottage Industries	6	0.91	1	0.16	1	0.3	2	0.38	0	0
Services	127	75.82	155	87.29	171	180.62	119	199.05	88	177.62
(B) Indirect Investment	10	1017	11	1192.26	11	1516.8	11	1936.2	14	2817.44
Total	1302	6119.13	1487	6816.29	1334	7928	1169	9437.25	1045	11714.76

Source: EBL's Financial Publications

- The Priority Sector Lending of EBL is in increasing trend compared to Ashadh 2062. It has increased by 10.50% in FY Aashad 2063, 24.42% in FY Aashad 2064, 44.22% in FY 2065 and 70.71% in FY 2066. EBL has fulfilled their lending in Priority Sector as directed by NRB.

- The Deprived Sector Lending of EBL is in increasing trend compared to Ashadh 2062. It has increased by 15.30% in FY Aashad 2063, 52.12% in FY Aashad 2064, 98.12% in FY Aashad 2065 and 182.36% in FY 2066. EBL has fulfilled their lending in Priority Sector as directed by NRB.

Figure 4.1
Priority and Deprived Lending of EBL

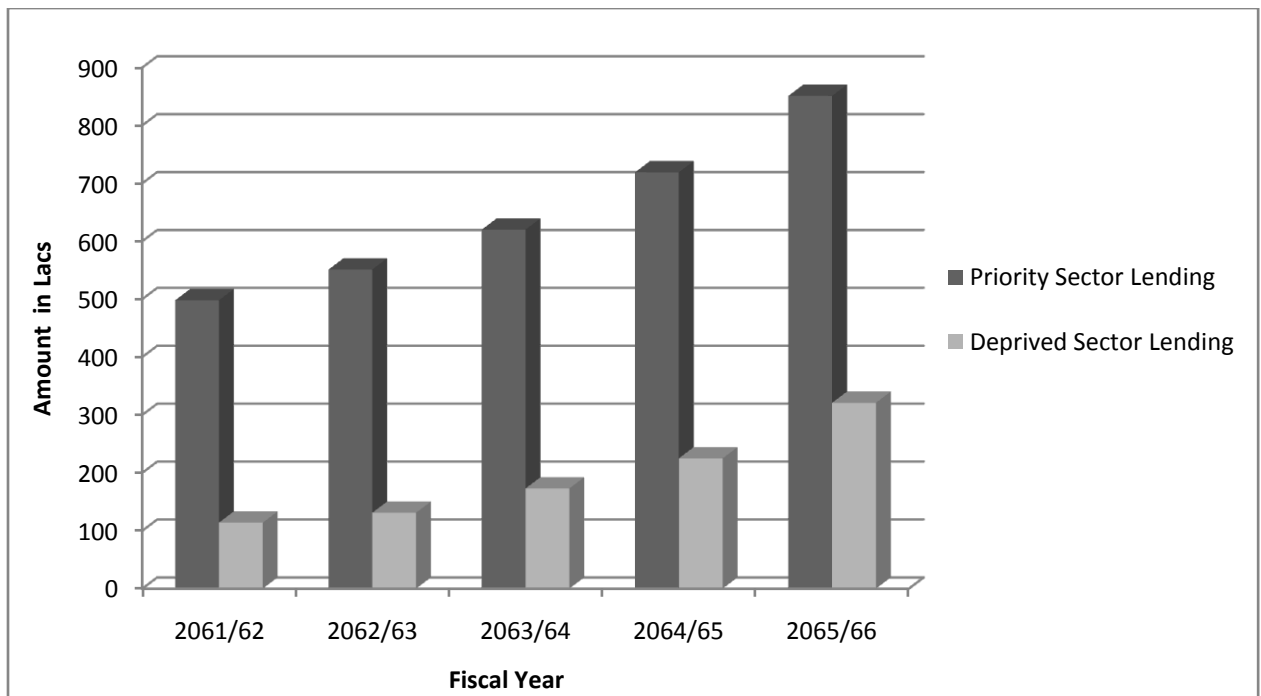


Table 4.5

Test of Priority & Deprived Sector Lending on Aashad 2062 to Aashad 2066

Particulars(Rs in Lacs)	FY 2062	FY 2063	FY 2064	FY 2065	FY 2066
Priority sector lending	6119.13	6816.29	7927.98	28558.33	11714.77
Deprived sector lending	1136.29	1310.19	1728.52	2251.24	3208.44
Total Loan & Advances	40442	50496	60958	79000	101362
Actual % of lending on	15.13	13.50	13.01	36.15	11.56
Priority sector lending	12%	12%	12%	12%	12%
Actual % of lending on	2.81	2.59	2.84	2.85	3.17
Deprived sector lending	3%	3%	3%	3%	3%

Source: EBL Financial Publications

The Prescribed % of Lending by NRB: on Priority Sector and 3% on Deprived Sector. The above table shows that EBL has floated merely 11.56% of its lending on priority sector and 3.17% of lending in deprived sector. In both cases, EBL has compile the standard directed by NRB. Therefore the NRB target for Priority sector advances and Deprived Sector lending was achieved by EBL.

**4.1.2 Retail Lending Position of Everest Bank as on Aashad end 2066
(15.07.2009)**

The performance of the Everest Bank in the area of retail lending as on Aashad end 2066 is as under.

Table 4.6
Retail Lending Position of EBL

Rs in Lac

Retail	Ashadh 62-63		Ashadh 63-64		Ashadh 64-65		Ashadh 65-66		Yield in %	
Lending Schemes	No	Amt.	No	Amt.	No	Amt.	No	Amt.	Ash 62	Ash 63
Housing Loan	676	3490	1036	6879	1383	10593	1801	15464	9.4	9.12
Car Loan	265	1561	401	2210	584	3524	849	5727	8.78	8.29
Education Loan	71	260	113	484	194	905	342	1605	10.29	10.15
Future lease rental	4	36	3	31	6	124	7	117		10.09
Professional Loan	Na	Na	7	38	8	38	12	75		9.87
Flexi Loan	Na	Na	45	702	225	3981	446	8986	8.75	8.82
Home Equity	Na	Na	7	64	37	192	87	366	8.1	8.56
Total Retail Lending	1016	5347	1612	10408	2437	19357	3544	32340		
Gross Credit	50533		60991		79000		101362			
% of Retail lending	10.58%		17.06%		24.50%		31%			
							Average Yield		9.17	8.94

Source: EBL Financial Publications

Total retail lending of Everest Bank as per above table is Rs 32340.00 Lac as on Ashadh end 2066 against total loan portfolio of Rs 101362.54 Lacs. It is 31.00% to total loan portfolio of the bank. The amount wise net retail lending was Rs 12983.00 Lacs during the fiscal year 2065/066 as against Rs 8951.00 Lac in FY 2064/065. There is growth of 145% compared to last fiscal year's net growth of Rs 8951.00 Lacs. There is net growth of 46.00% in housing loan, 62.00% in Vehicle Loan, 77% in Education Loan & 125.00% in Flexi Loan respectively.

4.8 Analysis of Cost of Deposit Fund

The interest rate spread is one of the indicators of financial intermediation efficiency of any CB's. Every financial institution pays certain prevailing interest rate on deposits and receive higher rate of interest from lending. The differential interest margin is basic incentive to FI's to cover their operational costs and contribute to the worth of equity holders. The determination of interest rate of the deposits and lending used to determine by government before 1989. Nowadays, these interest rates are more or less governed by the market forces. But it can't be neglected the fact that the differential rate is mostly influenced by operational efficiencies and profit margin of FI's. NRB had issued various directives relating to interest rate spread to be maintained by CB's. In Sept. 1993, NRB directed the CB's to keep the spread below 6 % and again in July 1998, NRB gave directive to CBs to lower their weight interest rate spread within 5 %. The interest rate spread shows the efficiency of CB's in term of cost of capital, Operational cost, Profit margin mentality etc. The higher interest rate spread indicate that depositors were getting low interest rate while borrowers were being punished with high interest charge curtailing the flow of loans to the export and industrial sectors or other productive projects. This situation retards the pace and process of economic development. The level of the spread also portrays the structural characteristics of the financial system of the nation. The structural characteristics comprise

prudential norms laid by NRB such as CRR, Priority sector lending program, NPAs of the banking system etc.

The interest-spread rate can be studied on two heads.

- a. Unweighted interest spread rate
 - b. Weighted interest spread rate
- a. Unweighted interest spread rate: It is the easiest way to find out and no need of further calculation. The difference between interest rate on deposit and lending gives the idea about unweighted interest spread rate.
 - b. Weighted interest spread rate: The weighted interest spread rate is the basis for the comparison of efficiency of any CB's. Generally, spread rate means weighted interest spread rate. Those banks are termed as efficient bank that has lower weighted interest spread rate.

Table 4.7
Showing Cost of Deposit of EBL

(Rs in million)

Basis	2061-062	2062-063	2063-064	2064-065	2065-066
Deposit	6695	8064	10098	13802	18186
Interest Expenses	308	316	300	401	517
Cost of Deposit (%)	4.60	3.92	2.97	2.91	2.84%
Lending	5050	6096	7900	10136	14082
Interest Income	520	657	719	903	1144
Cost of Lending (%)	10.30	10.78	9.10	8.91	8.12%
WACD (%)	5.70	6.86	6.13	6.00	5.28%

Source: EBL Financial Publications

The table 4.7 shows the cost of deposit, lending rate and weighted spread interest rate of Everest Bank Limited for five years from FY 061-62 to FY 065-66.

The figure portrays that the deposit rate and lending rate of EBL had reduced to some extent. On comparison of cost of deposit & cost of lending of EBL, the weighted average interest rate spread has been found to be in decreasing trend except in FY 062-063 which was little increased to 6.86%. From general public's point of view, it is better situation when FIs provide higher interest rate in deposit and charging lower interest rate on loan & advances. In fact, it is idle situation that is desired by society & government. NRB on behalf of government attempted to do on this regard. But now, the matter of interest-spread rate has been completely deregulated by NRB since our economy is facing toward market economy. It is believed that FIs will be in severe difficult situation when they charge higher interest on lending & provide lower interest on deposit i.e. higher interest spread rate.

4.9 Analysis of Deposit, Loan & Advances and Investments

The deposit of banks and FIs are raw material that is essential for the operation of its basic functions. The deposit must be sufficient to meet the demand of the loan seekers. Inadequate level of deposit hinders the growth of the particular financial institutions so various deposit schemes are introduced by various banks to get rid from deposit crunch.

Table 4.8
Showing Deposit & Loan Position of Everest Bank Ltd.

Rs in Million

Year	2061/062	2062/063	2063/064	2064/065	2065/066
Deposit	6694.96	8063.90	10097.69	13802.40	18186.20
Loan & Advances	5049.58	6095.84	7900.00	10136.20	14082.70
Investments	1653.98	2535.66	2128.93	4200.50	4984.30

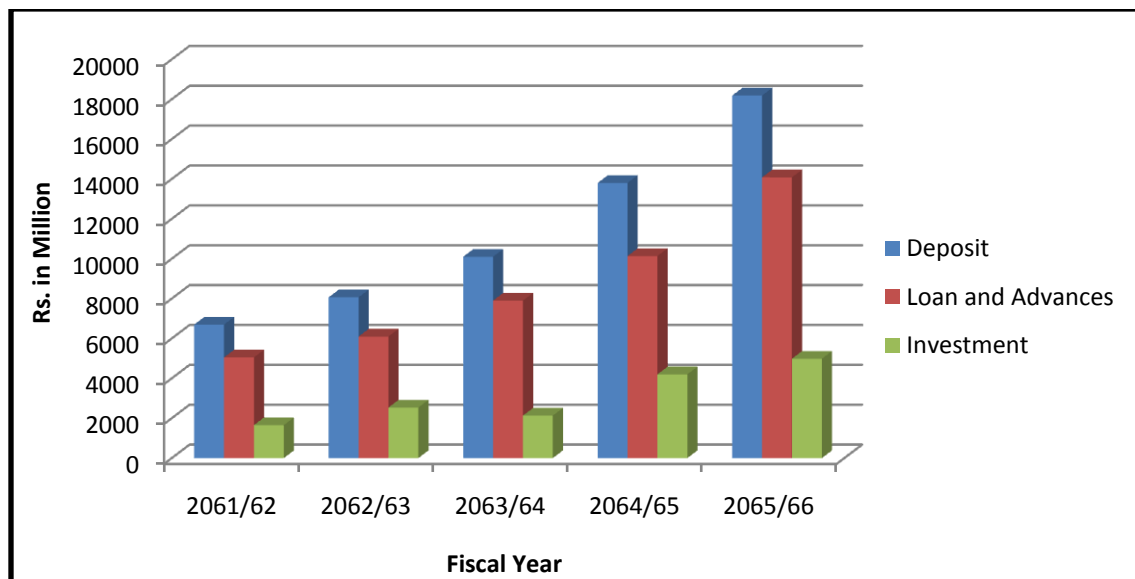
Source: EBL Financial Publications

The Deposit, Loan & Advances and Investment of EBL are rising over the studied period as shown in table 4.12. Its deposit rose from Rs. 6694.96 million in

2061/062 to Rs. 18186.20 million till 2065/066 which was increased by 11491.24 million in five years. The lending of the bank also regularly increased from Rs. 5049.58 million to Rs. 14082.70 million till 2065/066 which was increased by 9033.12 million in five years. Similarly the investments are also rising from Rs 1653.98 million in 2061/062 to Rs. 4984.30 million till 2065/066 which was increased by Rs 3330.32 million in five years. The Deposit, Loan & Advances and Investment of EBL are in increasing trend despite the recession in prevailing economy.

Figure 4.2

Bar Diagram of Deposit, Loans & Advances and Investment Position of EBL



The above bar diagram, drawn on basis of table 4.11, reveals the comparative position of deposit and lending of EBL in respective years.

4.10 Analysis of Growth Rate of Deposit, Loan & Investments

It is essential to know the growth rate of various important variables to evaluate the performance of any organizations. The deposit, lending and Investments are key variables of banking sector and they have serious impact over the profitability of the FIs. Profitability can't be imaged without adequate amount of lending and

lending is made on basis of capital base and its deposit accumulated. The data of deposit collected by EBL is given below:

Table 4.9
Showing Deposit & Loan and Advances Growing Rate of EBL

(in million)

	2061/062	2062/063	2063/064	2064/065	2065/066
EBL's Deposit (Rs.)	6694.96	8063.90	10097.69	13802.40	18186.20
Growth Rate	22.47%	20.45%	25.22%	36.69%	31.76%
EBL's Loan & Advances	5049.58	6095.84	7900.00	10136.20	14082.70
Growth Rate	24.86%	20.72%	29.60%	28.31%	38.93%

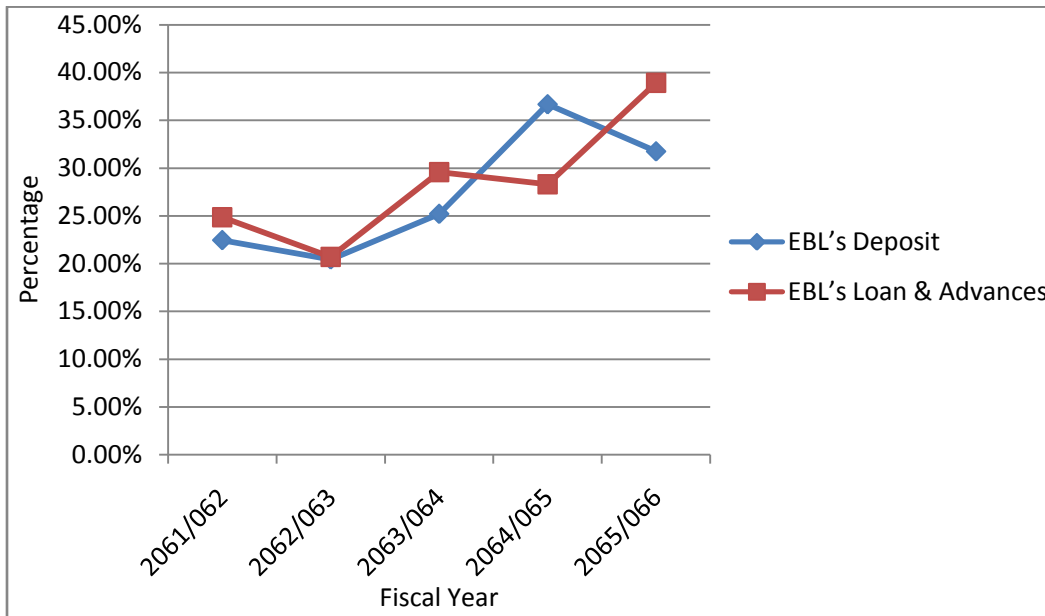
Source: EBL Financial Publications

The deposit of EBL is growing steadily in the above studied period of time. Its growth rate in 2064/065 found highest i.e. 36.69% and lowest in 2062/063 i.e. 20.45%. It seems that EBL has performing best in terms of Deposit and satisfy their depositors and performing above the average performance of the banking sector in this regard. Thus, EBL's deposit is increasing at higher in rate than the overall banking sector. As against the system's growth of 16.23% during the FY 2064/065, EBL's growth was 36.69%.

The amount of loan & advances of EBL is increasing per year and its rate of increment is fluctuating over the period of time. The rate is highest in 2065/066 i.e. 38.93% whereas the lowest in 2062/063 i.e. 20.72%. The aggregate loan & advance of banking sector is increasing per year and its rate is fluctuation over the period of time. As against the system's credit growth of 10.47% during the 2065/066, EBL's credit growth was 28.13% has got great success to increase its deposit, in another hand is has incresed its loan and advances.

Figure 4.3

Growth of Deposit and Loan and Advances of EBL



The growth rate of EBL is in fluctuating trend. The growth rate loan and advances is higher than deposit in F/Y 065/066.

4.11 Ratio Analysis

• Credit Ratio

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

$$\text{Credit to Total Deposit (i.e. CD Ratio): } \frac{\text{Total Credit}}{\text{Total Deposit}}$$

$$\text{Credit to Fixed Deposit (i.e. CD Ratio): } \frac{\text{Total Credit}}{\text{Fixed Deposit}}$$

$$\text{Credit to Saving Deposit (i.e. CD Ratio): } \frac{\text{Total Credit}}{\text{Saving Deposit}}$$

Table 4.10**Showing Credit Ratios of Total Credit and Total Deposit**

Rs in Millions

Fiscal Year	Total Loan& Advances	Total Deposit	Ratio(%)
2061/062	5049.58	6694.96	75.42
2062/063	6095.84	8063.9	75.59
2063/064	7900.0	10097.69	78.24
2064/065	10136.2	13802.4	73.44
2065/066	14082.7	18186.2	77.44
Total	43264.32	56845.15	76.10

Source: EBL Financial Publications

The CD ratios found higher in EBL over the studied period. EBL has floated more than 70% of its deposit as loan & advances .The highest ratio in EBL was 78.24% in FY 2061/062 and lowest 73.44% in FY 2062/063. In general, 70%-80 % credit deposit ratio is assumed to be appropriate considering in to market demand and internal strength of a particular bank. So the EBL CD ratios as per the standard prescribed. Thus, EBL is efficiently deploying its deposit fund so that it could earn more profit.

Table 4.11**Showing Credit Ratios of Total Credit and Fixed Deposit**

Rs in Millions

Year	Total Loan & Advances	Fixed Deposit	Ratio(times)
2061/062	5049.58	2788.48	181.09
2062/063	6095.84	2902.85	210.00
2063/064	7900.00	3403.96	232.08
2064/065	10136.20	4242.35	238.93
2065/066	14082.70	5626.70	250.28
Total	43264.32	18964.34	228.13

Source: EBL Financial Publications

The credit as a ratio of fixed deposit is higher in EBL in each year. It shows the credit floated in relative to fixed deposit collected is higher in EBL. It also furnish that growth rate of credit outflow is higher in comparison to fixed deposit growth in EBL. In case of EBL, the ratio recorded lowest in FY 2061/062 i.e. 181.09 times and highest in FY 2065/066 i.e. 250.28 times.

Table 4.12
Showing Credit Ratios of Total Credit and Saving Deposit

Rs in Millions

Fiscal Year	Total Loan & Advances	Saving Deposit	Ratio (times)
2061/062	5049.58	2757.95	183.09
2062/063	6095.84	3730.61	163.40
2063/064	7,900.00	4806.83	164.35
2064/065	10136.20	4242.35	238.93
2065/066	14082.70	9029.30	155.97
Total	43264.32	24567.04	176.10

Source: EBL Financial Publications

The **credit as a ratio of saving deposit** is higher in every studied period. The growth rate of credit outflow is higher than the growth rate of saving deposit in EBL. The highest ratio recorded in FY 2064/065 and lowest at FY 2065/066.

4.12 Stability Test

Table 4.13
Showing Stability Ratios of EBL

Ratios	Everest Bank Limited (EBL)				
	061/062	062/063	063/064	064/065	065/066
Capital to Total Deposit	10.22	9.51	12.35	10.08	10.54
Capital to Total Credit	13.55	12.58	15.79	13.73	13.91

Source: EBL Financial Publications

Stability test of any bank is carried to ascertain the sustaining capacity in long run. The test is carried by studying capital position in relative to various variables. Capital to total deposit ratio of EBL is found decreased in 062/063 & 064/065 and increased in 063/064. It means that both the capital's position in relative to deposit is improving and maintaining around 10.54% average in four year and enhancing its stability position.

Another ratio "Capital to total Credit" found stable in EBL in all four years. EBL has maintained around 13.91 in average Capital to total Credit in all four years. It means both the capital and total credit are increasing in EBL; the improvement made by EBL in building up its stability position is remarkable. It is due to higher growth rate of capital in comparative to growth rate of credit floated

Other Ratio

i. Shareholder's Income Per Share

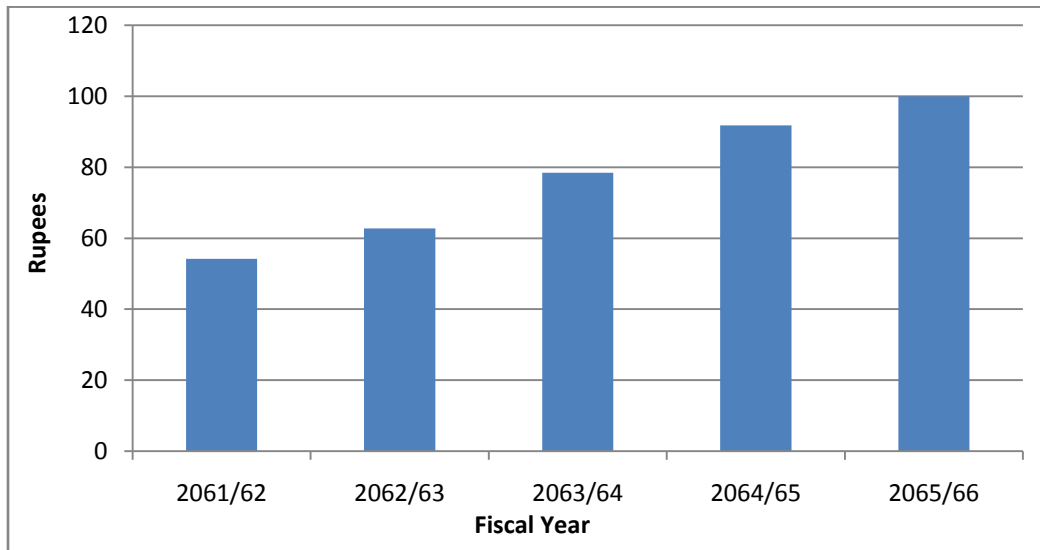
Table 4.14

Shareholder's Income Per Share

Fiscal Year	Earnings Per Share (Rs.)
2061/62	54.22
2062/63	62.78
2063/64	78.42
2064/65	91.82
2065/66	99.99

(Sources: Annual Report of EBL)

Figure 4.4
Earning per Share of EBL



The above graph shows that the earning pershare of EBL is in increasing trend as it has increased Rs 54.22 to 99.99 in five years. That’s EBL has been able to satisfy its shareholders.

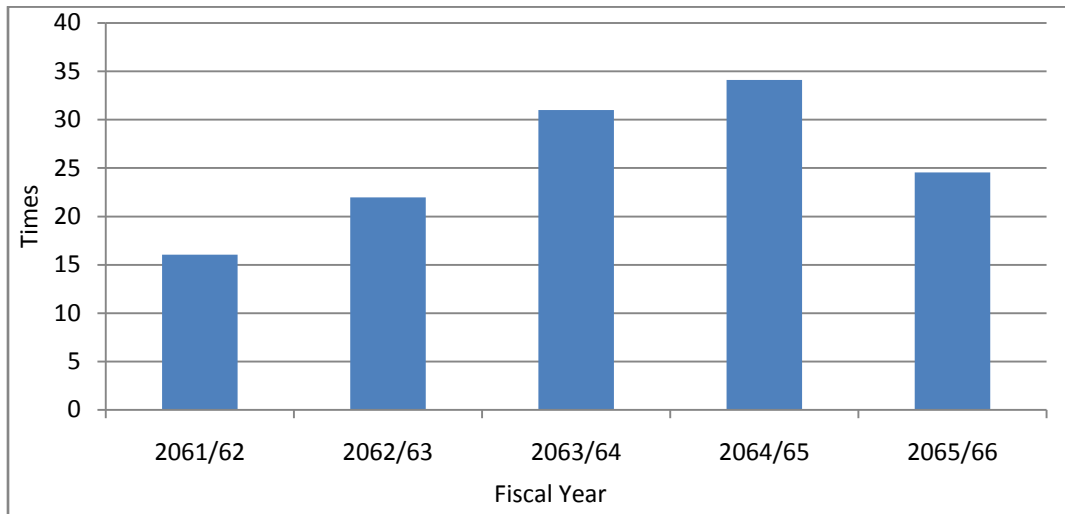
i. Price Earning Ratio

Table 4.15
Showing Price Earning of EBL

Fiscal Year	Price Earning Ratio
2061/62	16.04
2062/63	21.97
2063/64	30.99
2064/65	34.11
2065/66	24.55

(Sources: Annual Report of EBL)

Figure 4.5
Price Earning of EBL



The above table and graph show, the Price Earning Ratio of EBL has increased up to 34.11 in the year 2064/65, but in 2065/66 it has decreased to 24.55 times. The change in the economy and the whole sharemarket influence by global economy and national political unstability played the main role for caused the decrease in P/E ratio of the F/Y 2065/66,

ii. Operating and Net Profit of EBL

Table 4.16
Operating Profit and Net Profit of EBL

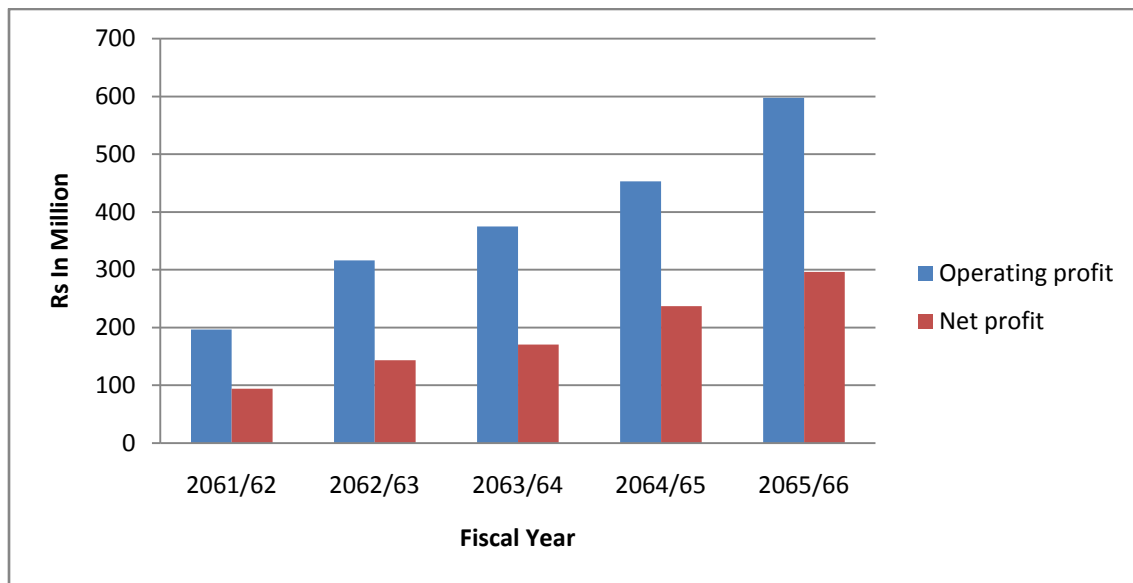
Rs in Million

Fiscal Year	Operating Profit	Net Profit
2061/62	196.7	94.2
2062/63	316.4	143.6
2063/64	375.1	170.8
2064/65	453.1	237.2
2065/66	597.5	296.4

(Sources: Annual Report of EBL)

The operating profit and the net profit is increasing trend. In F/Y94.2 Million net profit where as is has reached to 296.4 Million on 065/066. Therefore it has increased more than 200% increment in last four year's net profit.

Figure 4.6
Operating Profit and Net Profit of EBL



4.7 Statistical Analysis

i. Coefficient of Correlation Analysis

The statistical tool, coefficient of correlation has been studied to find out whether the two available variables are inter-correlation or not. If the result falls with in the correlated point, the two available variables are inter-correlated otherwise not. Now to find out the correlation coefficient between total loan and advances and total deposit the widely used method of Karl Pearson's Coefficient of correlation has been used.

$$\text{Coefficient of Correlation (r)} = \frac{N \sum xy - (\sum x)(\sum y)}{\sqrt{N \sum x^2 - (\sum x)^2} \sqrt{N \sum y^2 - (\sum y)^2}}$$

Here,

N = Number of pairs of x and y observed.

x = Total Loan and Advances

y = Total Deposit

r = Karl Pearson's Coefficient of Correlation

Table 4.17
Computation of Correlation Coefficient between Total Loan and Advances and Total Deposit of EBL

(Rs in Billion)

Fiscal Year	Total Loan and Advances (X)	Total Deposits (Y)	x²	Y²	XY
2061/62	7.9	10.1	62.41	102.01	79.79
2062/63	10.14	13.8	102.8196	190.44	139.932
2063/64	14.08	18.19	198.2464	330.8761	256.1152
2064/65	18.84	23.98	354.9456	575.0404	451.7832
2065/66	24.47	33.32	598.7809	1110.222	815.3404
N=5	∑X=75.43	∑Y=99.39	∑X ² =5689.6849	∑Y ² =9878.372	∑XY=7496.988

Here

N=5, ∑X=75.43, ∑Y=99.39, ∑X²=5689.6849, ∑Y²=9878.372, ∑XY=7496.988,

Now,

$$\text{Coefficient of Correlation (r)} = \frac{N \sum xy - (\sum x)(\sum y)}{\sqrt{N \sum x^2 - (\sum x)^2} \sqrt{N \sum y^2 - (\sum y)^2}} = 0.698662$$

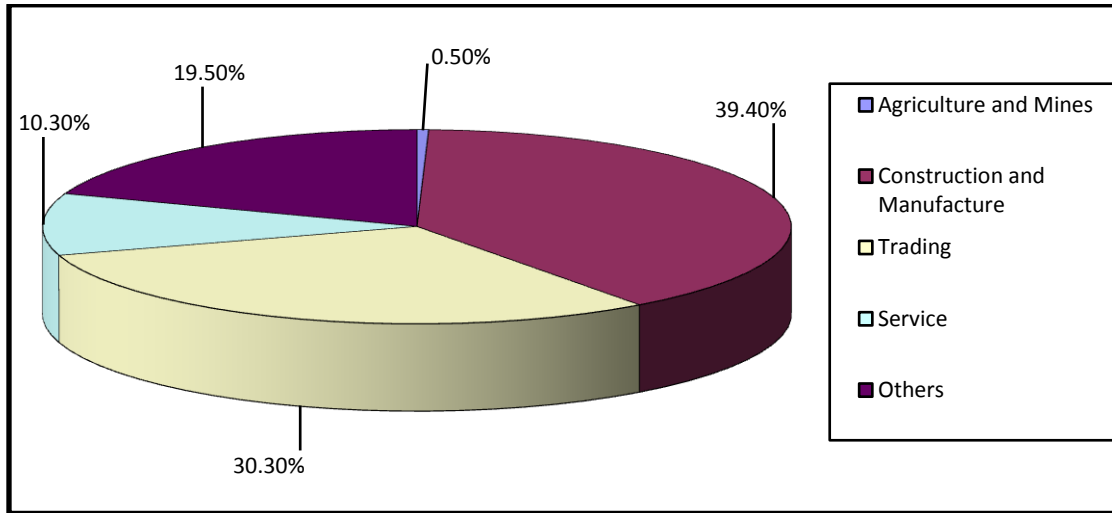
Thus this evaluations shows that the Total Loan and Advances and Total deposits are positively correlated in the period of 2061/62 to 2065/66.

Sector wise Distribution of Credit as on FY 2065/66

Out of total loan & advances EBL has made lending in Trading by 30.30%, Construction & Manufacture 39.40%, Service 10.30%, Agriculture & Mines 0.50% and Others 19.5%.

Figure 4.7

Sector wise Distribution of Credit of EBL in FY 2065/066



The above mentioned table highlights the increasing trend of loan and advances of Everest Bank Limited as a whole. In fiscal year 2062/63 the loan and advances has increased by 20.72% compared to the corresponding period of Last fiscal year, in FY 2063/64 – 29.59%, in FY 2064/65 – 28.31% and in FY 2065/66 -38.93%.

The increase in the figure of loan and advances has resulted increase in the interest income of the Bank. The loan and advances of the bank shows the direct relation with the interest income of the bank. Increase in loan and advances have led the bank's increase in interest income.

There is high chance of increase in the non performing loan as the loan and advances of the bank increases. In this regard the bank has to monitor the loan closely and scrutinized the loan proposal meticulously and strictly. The non

performing loan of the bank is in decreasing trend however the loan and advances is increasing. The bank has maintained the lowest gross non performing loan ratio of 0.91% for the year ended Aashad 2066 in comparison to other commercial banks.

The total deposit of the EBL is also in increasing trend. In fiscal year 2062/63 the deposit has increase by 20.45% compared to the corresponding period of Last fiscal year, in FY 2063/064 -25.22%, in FY 2064/65 -36.69% and in FY 2065/066 -31.76% amounting to Rs 1818.62 millions.

The total operating profit and net profit is also in increasing trend. In fiscal year 2062/63 the operating profit has increased by 60.85% compared to the corresponding period of Last fiscal year, in FY 2063/064 -18.55%, in FY 2064/065-20.79% and in FY 2065/066 -31.95%. Likewise the net profit of EBL is also in increasing trend. In fiscal year 2062/063 the net profit has increased by 52.44% compared to the corresponding period of Last fiscal year, in FY 2065/066 -18.94%, in FY 2064/065 -38.88%.

4.7.1 Trend Analysis

Under this section, the impact of capital structure on profitability of the bank has been measured and the trend value of debt equity ratio and the net profit for the forthcoming four fiscal years have been estimated.

4.7.1.1 Relationship between D/E ratio and NPAT

It is obtrusive that the net profit of the bank somewhat depends on the capital structure, but to what extent is just dilemma. Thus, to measure the impact of debt equity ratio on net profit, the correlation coefficient and regression analysis have been performed.

Table 4.18

Relationship between D/E ratio and NPAT

Bank	r	P.E.	6 P.E.	Regression	Remark
EBL	-0.5003	0.2261	1.3569	NPAT = 701.77 – 1262.49 D/E	Insignificant

(Source: Appendix - I)

The table depicts that the D/E ratio has very low positive relationship with NPAT of EBL, as the correlation coefficient between the variable -0.5003 in EBL. The correlation coefficient indicate that EBL should decrease D/E ratio to increase net profit, which means decrease in long term debt capital or increase in shareholders' equity.

Further, the regression analysis shows that with 1% increase in D/E ratio leads to Rs. 1262.49 millions decline in net profit of EBL. However, the net profit is not solely dependent on the D/E ratio, since the calculated correlation coefficient between the variable is lower than the 6 P.E. of the corresponding bank. Thus, it can be assumed that the relationship between D/E ratio and net profit is statistically insignificant, and thus it is not obligatory that net profit should increase/decrease with the increase/decrease of D/E ratio.

4.7.1.2 Relationship between Debt Ratio and NPAT

To measure the impact of debt ratio on profitability of the bank, the net profit has been considered as the dependent variable on debt ratio.

Table 4.19

Relationship between Debt Ratio and NPAT

Bank	r	P.E.	6 P.E.	Regression	Remark
EBL	0.1869	0.2911	1.7466	NPAT = -4438.03 + 51.22 DR	Insignificant

(Source: Appendix I)

Clearly there is low positive correlation between total debt to total assets ratio and net profit of each bank. The correlation coefficient between the variable is 0.1869 in EBL. The positive relationship indicates that an increment in total debt capital can cause net profit to increase. Also the regression analysis enlightens that 1% increase in total debt to total assets can increase Rs. 51.22 millions net profit in EBL, if the variable -4438.03 remains stable. Comparatively, the effect of total deposit to total assets on net profit is higher in EBL. However, the relationship between the variable is statistically insignificant, since the 'r' value is lower than the 6 P.E. and thus the net profit may not increase in the same way as the regression analysis suggests.

4.7.1.3 Trend Analysis of D/E ratio

To estimate the value of debt equity ratio in the forthcoming four fiscal years, the debt equity ratio has been considered as the dependent variable (Y) on the time period (X).

Table 4.20
Trend Analysis of D/E ratio

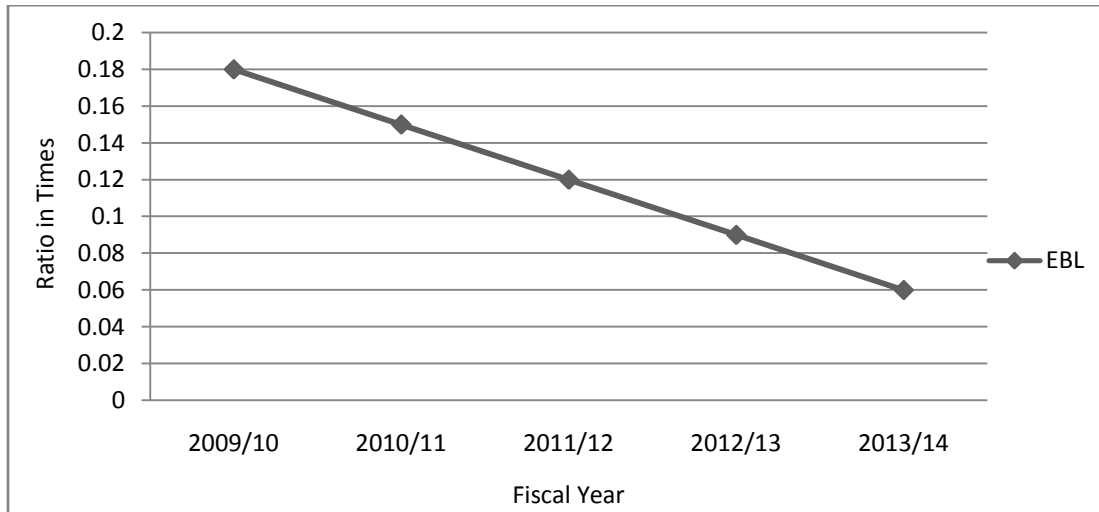
FY	EBL
2009/10	0.18
2010/11	0.15
2011/12	0.12
2012/13	0.09
2013/14	0.06
Regression	D/E ratio = 0.37 – 0.03X

(Source: Appendix II)

The table shows that EBL will prefer to decrease the debt-equity ratio. EBL will decrease by 0.03 times in each forthcoming years, if the other variables remain constant. By the end of the fiscal year 2013/14, the estimated value of D/E ratio of

EBL will be 0.06 times, which indicates almost ten times greater usage of equity capital than long term debt.

Figure 4.8
Trend Analysis of D/E ratio



4.7.1.4 Trend Analysis of NPAT

Let net profit after tax be the dependent variable on time period. Then the estimated value of net profit for the forthcoming periods and the regression equation of net profit on time period have been presented in the table below.

Table 4.21
Trend Analysis of NPAT

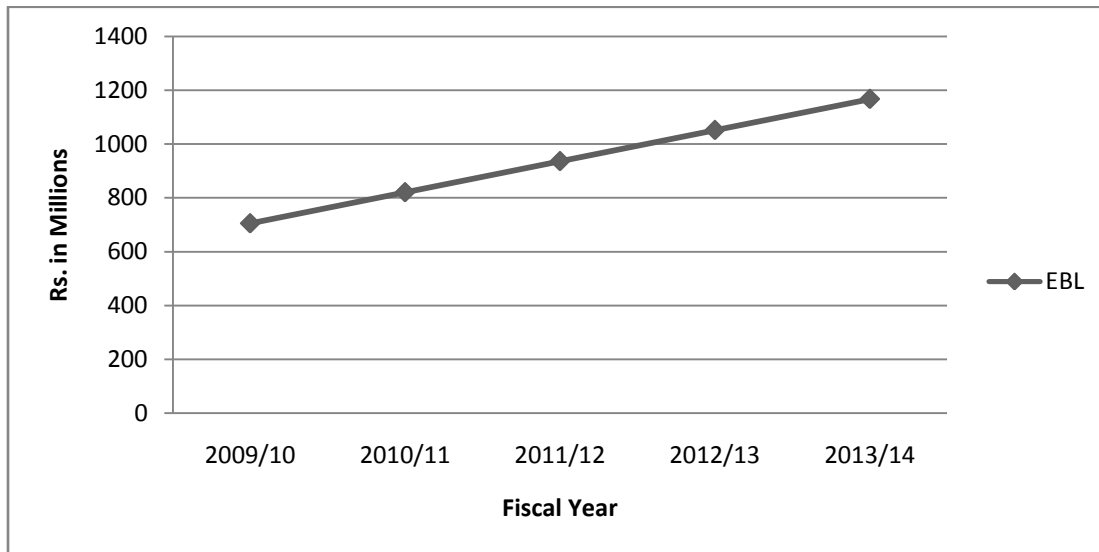
FY	EBL
2009/10	704.86
2010/11	820.36
2011/12	935.86
2012/13	1051.35
2013/14	1166.85
Regression	NPAT = 11.88 + 115.50X

(Source: Appendix - III)

The trend analysis of net profit after tax indicates that the net profit of both the banks will have positive relationship with the time period, and thus the net profit of both the banks increases in the forthcoming fiscal years. The net profit of EBL

will increase by Rs. 115.50 millions in each fiscal year in the forthcoming periods. This indicates that the pace of growth of net profit of EBL will be greater. By the end of the fiscal year 2013/14, the estimated value of net profit of EBL will be Rs. 1166.85 millions.

Figure 4.9
Trend Analysis of NPAT



4.8 Findings of the Study

- The total deposit of the EBL is in increasing trend. In fiscal year 2062/63 the deposit has increase by 20.45% compared to the corresponding period of Last fiscal year, in FY 2063/064 -25.22%, in FY 2064/65 -36.69% and in FY 2065/066 -31.76% amounting to Rs 1818.62 millions.
- The total operating profit and net profit is also in increasing trend. In fiscal year 2062/63 the operating profit has increased by 60.85% compared to the corresponding period of Last fiscal year, in FY 2063/064 -18.55%, in FY 2064/065-20.79% and in FY 2065/066 -31.95%. Likewise the net profit of EBL is also in increasing trend. In fiscal year 2062/063 the net profit has increased by 52.44% compared to the corresponding period of Last fiscal year, in FY 2065/066 -18.94%, in FY 2064/065 -38.88%.

- EBL has become successful to compile the NRB lending and deposit directives laid to the commercial banks.
- Overall EBL is having profits year by year. Now a day it is one of the best commercial bank all over the Nepal. Comparatively there is more strength than weakness.
- Credit activity is the integral part of banking business. Detailed information on various aspects of credit activities and the system implemented by the bank has to be included during the process of loan sanction in order to minimize risk inherent with it.
- It is crucial for a banking institution to lay down clearly defined systems and procedures for conducting its day to day operations. It is still more crucial that the laid down systems and procedures are meticulously compiled with by all concerned.
- Based on the entire study and findings have been made. This study particularly deals with findings about credit management banking system and information flows.

CHAPTER - V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.4 Summary

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

EBL has started its operation from October 18, 1994 with the objective of extending professionalized banking services to various sections of the society in the kingdom of Nepal and thereby contribute to the economic development of the country.

EBL has been promoted by well established business/industrial house of Nepal as a joint venture with PNB of India, one of the largest commercial banks in India having more than 4400 branches and over 200 foreign correspondents around the globe. At present EBL has been successful to operate 32 branches all over in Nepal, which has recorded to have large number of networks within Nepal among other commercial banks.

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

Rentals and scheme for Professionals as also the Loan against Lease Rentals of the properties.

The central focus of commercial banking concerns the acquisition and servicing of loans. A bank mobilizes deposits and lends to businesses. Banks lend or invest up to 70 – 80% of their deposits. Indeed, commercial banks are the primary, if not only, source of loans for most small and medium-sized business firms and provide vital service to business organizations and to the community as a source of loans. There is a risk involved in lending the money. With the opening up of the economy rapid changes are taking place in the technology and financial sector exposing banks to greater risks. The well managed bank must institute loan policies designed to ensure that adequate control exists in the approval and disbursement of loans and that outstanding loan are monitored so as to ensure compliance with terms of the loan and ultimate repayment of principal and interest.

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

5.5 Conclusion

Bank is a resource mobilizing institution, which accepts deposit from the various sources and invest such accumulated resources in the fields of agriculture, trade, commerce, industry, tourism etc. The commercial bank has its own role and

contribution and it is a source for economic development. It maintains economic confidence of various segments and extends credit to people. Now the role of bank is not only limited to the lending. It has also extended its business to remittance - non fund based business where the bank can generate income without lending to borrowers. However, the income generated from the fund based business cannot be ignored as it covers more than 70% of the total income of the bank.

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

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

EBL has followed the information procedure in controlling the credit policies and practices by its own credit control procedure and norms laid by the NRB. Which are as follows:

Own practice

1. Approval of Credit facilities by branch and HO level
2. Proper Documentation for working capital and term loan facilities
3. Board Parameters for considerations of loan parameters
4. Interest rate rating according to the compliance parameters

5. Reporting to the higher authorities on weekly, monthly quarterly and yearly basis.

NRB Norms

1. EBL has compiled the capital Adequacy norms for commercial banks laid by NRB.
2. The lending on priority sector and deprived sector, EBL has complied on lending on priority sector but on deprived sector it is little behind on compiling the norms.
 - Under the research period of five years, the deposit collection and loan flowed by the bank is in increasing trend. The deposit has been increased by 11491.24 million in five years and lending has been increased by 9033.12 million. Therefore, despite the period of recession in economy, the deposit and lending of EBL shows the positive growth.
 - The NPL of EBL is in decreasing trend and has decreased up to 0.80% of total loan and advance disbursed by the bank in F/Y 2065/066.
 - In total deposit of EBL, almost 50% of deposit is saving and 40% of lending has been disbursed to construction and manufacturing in F/Y 2065/066.
 - The operating profit of EBL is increasing trend. In comparison to the last four years EBL achieved more than 200% increase in net profit.
 - Despite in increase in number of commercial banks, the growth of loan and advances of EBL is in increasing trend besides maintaining the low non performing loans among the other commercial banks. This shows the good result of credit management of the Everest Bank Limited. The bank complies strict rules and regulation considering the NRB directives while processing the loan appraisal of the borrower. All possible steps are taken to strengthen the pre sanction appraisal of the loan – “Prevention is better than Cure”.

- Everest Bank Limited is more focused on fund based income rather than non fund based and others. The major portion of the bank's income is generated through the interest earned from the loan and advances. Any loose measures control found in the appraisal of the loan proposal will directly effect the interest income of the bank.
- The loan proposal processed and the lending criterion of the bank is found as per the rules and regulations prescribed by NRB.

5.6 Recommendations

In market-oriented economy, customer will not prefer those FIs that have high interest spread. If any CBs try to gain by maintaining higher interest spread rate, they will find difficult to sustain in the competitive money market. In fact, maintaining lower interest spread rate means possessing higher competitive position and higher financial intermediation efficiency. In money market, there are same CB's those are forced to maintain higher spread interest rate because of higher cost of capital and large position of NPA level. In a situation where the level of non- performing asset of the bank is quite large, all the bad debts get translated in to higher interest rate for the borrowers & lower interest rate for the depositors. It is a clear symptom of financial & commercial inefficiency. In sum up, Darwin's principle of "Survival of Fittest" also fits in the banking sector. Our money market is being much more competitive and only those fittest FIs can only sustain or exist in the prevailing situation. It is no doubt to say that CB's having lower interest spread rate can only survive in financial environment otherwise it has to loose its existence.

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

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

- The ratio of non performing loans on total loans of the bank among others highlights the sound credit management of the bank. But there are still outstanding non performing loans of the bank. The bank should take the optimum advantage from Debt Recovery Tribunal (DRT) in order to minimize the non performing loans.
- The bank has made the lending of 39.4% on construction and manufacturing sector. Other sectors are far behind as compared to lending made in construction and manufacturing. The bank should increase its lending in service sector area, the sector where the lending is more secured. Further the bank should also give more emphasis on trading sector of the economy. As the import turnover of the economy is greater than the export turnover of the country.
- The bank should introduce the credit card facility to its customers. It helps to increase the lending portfolio of the bank.
- As the bank is fully computerized system it should take the full advantage of it. The support module of the financial System has not been fully utilized by the bank. The module should be made in operation in order to grasp the business of the changing technological business of the banking system.
- The yield on advances are declining as no fresh investments are coming & due to low cost of deposits in major banks like Himalayan bank, Nepal Investment Bank & Nabil etc, they are attracting/canvassing quality credit customers with lower rate of interest. Hence in order to be competitive in the market it is pertinent to lower the cost of deposit of the bank.
- In order to be competitive in the market and provide better facility to the customer the bank should speedily process the loan application received and notified the concerned customer incase of loan is rejected duly assigning the reasons for such rejection.

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Appendix - I

Calculation of correlation coefficient and regression line between Net Profit & D/E Ratio of EBL

Year	D/E Ratio X	NPAT Y	$x = X - \bar{X}$	$y = Y - \bar{Y}$
2004/05	0.36	168.21	0.09	-190.16
2005/06	0.31	237.29	0.04	-121.08
2006/07	0.25	296.41	-0.02	-61.96
2007/08	0.16	451.22	-0.11	92.85
2008/09	0.28	638.73	0.01	280.36
Total	1.36	1791.86		

i) Calculation of Mean

	For D/E Ratio		For NPAT
Mean	$\bar{X} = \frac{\sum X}{5} =$	0.27	$\bar{Y} = \frac{\sum Y}{5} =$

ii) Calculation of Correlation Coefficient between D/E Ratio and NPAT

$$r_{xy} = \frac{\sum xy}{\sqrt{\sum x^2} \sqrt{\sum y^2}} = \frac{-28.12832}{56.22} = -0.5003$$

iii) Calculation of Standard Deviation (σ)

For D/E Ratio:		For NPAT:
$\sigma_x = \sqrt{\frac{\sum x^2}{N}}$	$= \sqrt{\frac{0.02}{5}}$	$\sigma_y =$
$=$	0.07	$=$

iv) Simple Regression Equation of NPAT on D/E Ratio

$$Y - \bar{Y} = r \times \frac{\sigma_y}{\sigma_x} (X - \bar{X})$$

or, $Y - 358.37 = -0.5003 \times \frac{168.45}{0.07} (X - 0.27)$

$$\text{or, } Y - 285.52 = -1262.49 X + 343.40$$

$$\text{or, } Y = 701.77 - 1262.49 X$$

v) Calculation of Probable Error (P.E.)

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

r^2	$1-r^2$	$0.6745 (1-r^2)$	$\frac{\quad}{\sqrt{N}}$	P.E.	6
0.2503	0.75	0.51	2.2361	0.2261	1

c) Calculation of trend value of D/E ratio of EBL

	Year	D/E Ratio		
--	------	-----------	--	--

Year	X	Y	x = X-X	y = Y-Y	x ²
2004/05	1	0.36	-2.00	0.09	4.00
2005/06	2	0.31	-1.00	0.04	1.00
2006/07	3	0.25	0.00	-0.02	0.00
2007/08	4	0.16	1.00	-0.11	1.00
2008/09	5	0.28	2.00	0.01	4.00
Total	15	1.36			10.00

i) Calculation of Mean

	For Year		For D/E Ratio
Mean	$X = \frac{\sum X}{5} =$	3.00	$Y = \frac{\sum Y}{5} =$

ii) Calculation of Correlation Coefficient between D/E Ratio and Year

$$r_{xy} = \frac{\sum xy}{\sqrt{\sum x^2} \sqrt{\sum y^2}} = \frac{-0.31}{0.47} = -0.6568$$

iii) Calculation of Standard Deviation ($\bar{\sigma}$)

For Year	$\bar{\sigma}_x = \sqrt{\frac{\sum x^2}{N}}$	=	$\sqrt{\frac{10.00}{5}}$	=	1.41	For D/E Ratio	$\bar{\sigma}_y =$	=
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iv) Simple Regression Equation of D/E Ratio on Time

$$\bar{y} = \frac{\sum y}{N} + \frac{\sum xy}{\sum x^2} (x - \bar{x})$$

$$Y - \bar{Y} = r \times \frac{\sigma_y}{\sigma_x} (X - \bar{X})$$

$$\text{or, } Y - 0.84 = \frac{0.1008 \times 0.25 (X - 3.00)}{1.41}$$

$$\text{or, } Y - 285.52 = 0.02 X - 0.05$$

$$\text{or, } Y = 0.79 + 0.02 X$$

v) Calculation of Trend Value

Year	a	b	X	Y = a+bX
2009/10	0.37	-0.03	6	0.18
2010/11	0.37	-0.03	7	0.15
2011/12	0.37	-0.03	8	0.12
2012/13	0.37	-0.03	9	0.09
2013/14	0.37	-0.03	10	0.06

Appendix -

d) Calculation of trend value of NPAT of EBL

	Year	NPAT				

Year	X	Y	x = X-X	y = Y-Y	x ²	y ²
2004/05	1	168.21	-2.00	-190.16	4.00	36161.59
2005/06	2	237.29	-1.00	-121.08	1.00	14660.85
2006/07	3	296.41	0.00	-61.96	0.00	3839.29
2007/08	4	451.22	1.00	92.85	1.00	8620.75
2008/09	5	638.73	2.00	280.36	4.00	78600.61
Total	15	1791.86			10.00	141883.09

i) Calculation of Mean

$$\begin{array}{l} \text{For Year} \\ \text{Mean } \bar{X} = \frac{\sum X}{5} = 3.00 \end{array} \qquad \begin{array}{l} \text{For NPAT} \\ \bar{Y} = \frac{\sum Y}{5} = 358.37 \end{array}$$

ii) Calculation of Correlation Coefficient between NPAT and Year

$$r_{xy} = \frac{\sum xy}{\sqrt{\sum x^2} \sqrt{\sum y^2}} = \frac{1154.97}{1191.15} = 0.9696$$

iii) Calculation of Standard Deviation (σ)

$$\begin{array}{l} \text{For Year} \\ \sigma_x = \sqrt{\frac{\sum x^2}{N}} = \sqrt{\frac{10.00}{5}} = 1.41 \end{array} \qquad \begin{array}{l} \text{For NPAT} \\ \sigma_y = \sqrt{\frac{\sum y^2}{N}} = \sqrt{\frac{141883.09}{15}} = 168.45 \end{array}$$

iv) Simple Regression Equation of NPAT on Time

$$\begin{aligned} Y - \bar{Y} &= r \times \frac{\sigma_y}{\sigma_x} (X - \bar{X}) \\ \text{or, } Y - 358.37 &= \frac{0.9559 \times 168.45}{1.41} (X - 3.00) \\ \text{or, } Y - 358.37 &= 113.87 X - 341.62 \\ \text{or, } Y &= 113.87 X + 17.25 \end{aligned}$$

v) Calculation of Trend Value

Year	a	b	X	$Y = a+bX$
2009/10	11.88	115.50	6	704.86
2010/11	11.88	115.50	7	820.36
2011/12	11.88	115.50	8	935.86
2012/13	11.88	115.50	9	1051.35
2013/14	11.88	115.50	10	1166.85