

CHAPTER 1

INTRODUCTION

1.1 General Background

Bank is an institution established by law, which deals with money and credit. In other words, it is an institution which deals with money, receiving it on deposits from customers, honoring customers' drawings against such deposits and demand, collecting cheques from customers, and lending or investing surplus deposits until they are required for repayment. Likewise it is a financial institution which deals with monetary transaction by accepting various types of deposits, distributing various types of loans and rendering other financial services. There are several definitions of a bank by different authors and scholar's. Some of them are as follows:-

“A bank is an establishment for the custody of money received from or on its customers, its essential duty is to pay their draft on it, its profit arises from its use of money left unemployed by them.” - **Oxford Dictionary**

“Banks are the financial institutions that accept funds in the form of deposit repayable on demand or short notice.” - **World Bank**

“A person or company carrying on the business of receiving money and collecting drafts, for customers subject to the obligation of honoring cheques upon them from time to time by the customers to the extent of the amounts available on their current accounts” - **Dr. Hart**

“Bank is an organization whose principle operation is concerned with accumulation for the temporarily idle with money of the general public for the purpose of advancing to other expenditure.” - **Kent**

“A banker is defined as an individual partnership or corporation, whose sole or pre-dominating business banking”. - **Halsbury laws of England**

“A commercial bank is a bank, which deals in exchanging currency, deposits, giving loans and doing commercial transactions”. So bank is an organization, which deals with deposits, lends money and renders a wide range of financial services." - **Commercial Bank Act 2031 of Nepal**

Origin of Banking

The term “bank” was originated from the Latin word “BANCUS” and the Italian word “BANCO”, the German word “BACK” and French word “BANKE”. Regarding the origin of banking institution in the world, the bank first established was “Bank of Venice” of Italy. The second bank was established in Spain in 1401 A.D. as “The bank of Barcelona”. Then after, Bank of Geneva & Bank of England as a joint venture bank in 1401 & 1694 A.D. respectively. Several national and foreign banks were established in India & other countries subsequently.

Banking in Nepal

In the context of Nepal like as in other country, the goldsmiths and landlords were the ancient bankers. The Nepalese people were highly exploited by Shahu Mahajans who charged higher interest rate and even manipulated the principal amount. If we try to analyze the history of banking transaction in depth, evidence of money lending practices can be found before 8th century. In 780 B.S., Gunakamadev, the ruler of Kathmandu, reconstructed Kathmandu valley by borrowing debt from the people; Tanka dhari system in which government used to provide loans to their employees at 5% interest against gold, silver etc. security was running in the period of Ranodip Singh in 14th century in Kathmandu by an office called Tejarath Adda.

After the liberalization process of 1990s, Nepalese financial system has grown rapidly. There has been huge development in the Nepalese financial market not only in terms of quantity but also in quality. Today, Nepalese banking sector is recognized as a luring sector offering opportunities. Nepal Bank Limited was the first bank in Nepal, established in 1994 B.S. (1937 A.D.). It was established as a semi private commercial bank under Nepal Bank Act. Later Nepal Rastra Bank was established as the central bank in 2013 B.S (1956 A.D), with an objective to provide the policy decision, guidance and control the banking and to monitor this sector. NIDC (Nepal

Industrial Development Corporation) and Agriculture Development Bank Limited (ADBL) was established in 2020 B.S (1959 A.D). Rastriya Banijya Bank, a government owned commercial bank, was established in 2022 B.S. In mid-eighties, financial liberalization policy played a crucial role for the establishment and development of several commercial banks (both foreign joint ventures and private commercial banks) and financial institutions. Nabil Bank was established as the first joint venture bank in 1984.

In the present context, the commercial banks are the only prominent institutions in the Nepalese economy to mobilize the collection of scattered monetary savings among the common people. During the last two and half decades, the Nepalese Financial System has grown significantly. In the beginning of 1980s, there were only two commercial banks and two development banks in the country. After the adoption of economic liberalization policy, particularly the financial sector liberalization that paved the way for establishment of new banks and non-bank financial institutions in the country. Consequently, banks operate in a highly competitive arena where 32 'A' class commercial banks, 88 'B' class development banks and 78 'C' class finance companies and other financial intermediaries compete for a share in the financial market in Nepal. Despite these competitive conditions, the banking sector maintained its profitability levels. However, net interest margins are expected to shrink in coming years, as liquid and low costs funds have become scarcer in the market. Banks will have to increasingly concentrate on enhancing their non-interest income component, to maintain profitability. Mobilizing deposits in a high inflation and tight liquidity environment has been a challenge. In 2066-67 (2009/10), deposit augmentation of commercial banks went up by 10.65% (Rs. 67.28 billion) amounting to Rs. 631.28 billion. Similarly, loans and advances of commercial banks have increased by 15.80% (Rs. 73.06 billion) to Rs. 462.2 billion during the year.

For the last few years, there has been notable expansion in the geographical and numerical presence of the banks and financial institutions with expanded financial transactions as well. Branches of the commercial banks expanded to 1085 in mid-April 2011 from 990 in mid-July 2010. Of the total bank branches, 35.7 percent are located in Kathmandu valley, 25.3 percent in mountain and 39 percent in terai.

Credit Policy of Commercial banks in Nepal

Modern economy is a credit economy, as credit has come to play a major role in setting all kinds of monetary and business transactions. Change in the volume of credit influences the level of business activity and the price level in the economy. Nepal Rastra Bank adopts the credit control policy to control the creation of credit in order to maintain stability in the economic system. The main objectives of NRB for Credit Control are: maintain price stability, bring economic stability, maximize level of employment, achieve economic growth, bring stabilization in Money Market, and to maintain exchange rate stability.

Nepal Rastra Bank has directed commercial banks to advance loans to small entrepreneurs of agriculture, small industries and services in 1974. As per the directive, commercial banks began to finance to needy borrowers without much stress on collateral but on the viability of the project. This was the shift from traditional to modern way of financing.

Improving upon the traditional collateral-oriented policy the commercial banks have now begun extending loans in accordance with the merit of the project or programme. This policy of programme oriented credit extension will be further encouraged. However, it is equally important to make this kind of credit extension risk-free for the commercial banks. Therefore, an efficient monitoring unit will be formed to supervise whether the extended credit is utilized productively and meaningfully in keeping with the purpose or not.

Monetary Policy for Fiscal Year 2010/11 had introduced a credit ceiling on real states and housing loans to reduce credit concentration risk. However, in view of the relatively higher value addition of housing sector, the credit ceiling on the housing sector will be moderately eased while the credit ceiling on land purchase and plotting will be continuously tightened. For this purpose, in 2010/11 the credit ceiling for land purchase and sale has been fixed to 10% of total credit. The institutions that have credit flow on land purchase and sale in excess of the specified limit should bring down such exposures to 10% of the total credit within two years time.

As per the current Monetary Policy for Fiscal Year 2011/12 – “Despite a slowdown in real estate and stock market transactions, the non performing loan (NPL) ratio has increased marginally. This NPL ratio which was 2.5 percent in mid-July 2010 reached 3.4 percent in mid-April 2011. The NPL ratios of Nepal Bank Limited and Rastrya Baniyja Bank Limited, which are of special concern under Financial Sector Reform Program, stood at 4.2 percent and 11.1 percent respectively. The NPL ratios of these two banks were respectively 2.3 and 9.8 percent in mid-July 2010. To avoid further depletion in the quality of loan and advances of banks and financial institutions, NRB has raised the ceiling for individual residential home loan upto Rs. 8 million from Rs. 6 million and allowed renewal of such loan upto mid-July 2012 upon the payment of interest dues by the borrowers. Similarly, banks and financial institutions are allowed to fix margin requirement of their own by minimizing inherent risk in such margin-type loan against the collateral of shares.”

1.2 Credit Management

The term credit is popularly used to denote the granting of an advance in lump sum, usually on the basis of some acceptable securities. The principal business of commercial banks is to make loans to qualified borrowers. The commercial bank earns profit by giving the amounts deposited with it in the form of loans. In commercial banks, loan is regarded as the most income generating assets. It is treated as the heart of the commercial banks in the sense that it occupies large volume of transactions, it covers the main part of investment and most of the investment activities are based on the loan; it is the main factor for creating profitability. Loans and advances is the major component of the bank's lending portfolio. Similarly, earning from loans and advances occupy a major space in income statement of the bank. However, it is very important to reminiscent that most of the banks in the world have failed because of shrinkage in the value of loans and advances. Therefore, loan is regarded as the risky assets. Risk of non-repayment of loan is known as credit risk.

"Making loans lies at the heart of bank's activities." - C. L. Harris

Credit management is a system which helps to manage loan effectively. Loan management is especially focused on the management of loan disbursement and collection of procedures, controlling and monitoring of lending activities. In other words, loan management refers management of loan exposures arising from loans, corporate bonds and loan derivatives. Loan exposures are the main source of investment on commercial banks and the return from such investment is supposed to be the main source of income.

The objective of loan management is to minimize the bank's risk by maintaining credit risk exposure within acceptable parameters. The performing loans have multiple benefits to society, whereas, non-performing loan erodes even existing capital. Sound credit policy is required to ensure that loans are given to the productive sector, which contributes to the society in a number of ways. So, the bank has to strongly analyze the proposals before lending loan in order to minimize the credit risk. Whenever a bank offers credit facility to the borrower, it is always subject to the terms and conditions stipulated in the sanction letter. Bank being the creditors tries to insert the stringent conditions while the borrower requests the bank for lenient ones. If the borrower can shop around, he succeeds in getting loan at lenient conditions. In order to give maximum returns to shareholders, bank requires investing most of its fund in different areas in the form of loan. Some areas may be riskier. Consequently, a clear and sound loan management system must be made for the safeguard of depositor's fund and also for the adequate return to shareholders. Loan management can be defined as the decision made in advance about management of loan/ credit.

Loan management is not only the most important function of a bank; it also determines the future of banking institutions. The quality of loan of borrower and quality of securities determines the health of any bank. The efficiency of bank lies in how it multiplies the deposits of depositors. Hence, lending should be accompanied by some basic principles and practices. No banker would willingly give a loan, unless he has sufficient confidence in the borrower that it will not be necessary to seek help of court for recovery. Safety of funds, liquidity of funds, purpose of loan, security for loan, profitability, spread of loan portfolio and compliance with national interests are some of the principal that a banker should follow while granting a loan. Besides these the character of person receiving credit, the capacity of the borrower to utilize the

fund, the percentage of borrower stake in the business etc. are the basic element which measures the quality of the borrower and ultimately the quality of the loan.

Loan management is a study in determining the importance of the bank's lending policy towards National Economic Development because it ensures efficient allocation of funds to achieve the material and economic well being of the society as a whole. In this regards loan disbursement pattern has been a major catalyst in achieving priority of industries in the context of Nepal's economic development. Since, the prosperous economic condition is represented by the development of industry, trade and business, which are main grounds to the banks to conduct its activities and to fulfill its objective of profit making. The proper loan management policy helps the bank to make profitable investment, which in turn directly helps in development of a country as well as to achieve the goal of profit making.

"Loan and advances" is the most profitable of all the assets of a bank. Banks universally seek after the asset. These assets constitute primary source of income to banks. Here the banker is brought into direct relation with the public. His capacity and judgement and his usefulness to the community is judged by the way he leads the money left with him by the depositors. As a business institution, a bank aims at making a huge profit. Since loans and advances are more profitable than any other assets, he is willing to lend as much as of his funds as possible. But he has to be careful about the safety of such advances. The banker has to temper liberally with caution. If he is too liberal, he may easily impair his profits by bad debts and if he is too timid, he may fail to obtain in adequate return on the funds, which are confided to him for use. It is by his capacity in lending that a bank manager is judged". (Swamy, Radha and Vasudevan, 1997:550)

1.3 Profile of Concerned Banks

For the purpose of this study, two commercial banks are taken as a sample banks among 32 commercial banks, namely Himalayan Bank Ltd. (HBL) and Nepal SBI Bank Ltd. Short glimpses of these two financial institutions are mentioned here.

1.3.1 Himalayan Bank Limited:

Himalayan Bank was established in 1993 in joint venture with Habib Bank Limited , one of the largest commercial bank of Pakistan. It is the first commercial bank of Nepal whose maximum shares are held by the Nepalese private sector. Besides commercial banking services, the bank also offers industrial and merchant banking services.

The bank's head office is located at Karmachari Sanchayakosh Building, Tridevi Marg in Thamel, which is the main business tourist area of the Kathmandu Valley. Besides this, the bank has thirty five branches located at Thamel, New Road, Maharajgunj, Bhaktapur, Patan, Teku, Chabahil, Swoyambhu, New baneshwor, Sorahkhutte, Dillibazar, Kalanki, Satdobato inside the valley as well as it has branches at Birgunj, Bharatpur, Tandi, Hetauda, Bhairawa, Biratnagar, Banepa, Dharan, Pokhara, Butwal, Nepalgunj, Itahari, Palpa, Dang, Trishuli, Jhapa, Parsa, Baglung, Dhangadhi, Gorkha, Barhabise and Nawalparasi. The Bank will be aggressively opening new branches at different parts of the Nepal to serve its customers better.

Products such as Premium Savings Account, HBL Proprietary Card and Millionaire Deposit Scheme besides services such as ATMs and Tele-banking were first introduced by HBL. HBL has always been committed to providing a quality service to its valued customers, with a personal touch. All customers are treated with utmost courtesy as valued clients. The Bank, wherever possible, offers tailor made facilities to its clients, based on the unique needs and requirements of different clients. To further extend the reliable and efficient services to its valued customers, Himalayan bank has adopted the latest banking technology. This has not only helped the Bank to constantly improve its service level but has also prepared the Bank for future adaptation to new technology. The Bank already offers unique services such as SMS Banking and Internet Banking to customers and will be introducing more services like these in the near future.

All Branches of HBL are integrated into Globus (developed by Temenos), the single Banking software where the Bank has made substantial investments. This has helped the Bank provide services like 'Any Branch Banking Facility', Internet Banking and SMS Banking. Living up to the expectations and aspirations of the Customers and other stakeholders of being innovative, HBL very recently introduced several new

products and services. Millionaire Deposit Scheme, Small Business Enterprises Loan, Pre-paid Visa Card, International Travel Quota Credit Card, Consumer Finance through Credit Card and online TOEFL, SAT, IELTS, etc. fee payment facility are some of the products and services. HBL also has a dedicated offsite 'Disaster Recovery Management System'. Looking at the number of Nepalese workers abroad and their need for formal money transfer channel; HBL has developed exclusive and proprietary online money transfer software- HimalRemit TM. By deputing our own staff with technical tie-ups with local exchange houses and banks, in the Middle East and Gulf region, HBL is the biggest inward remittance handling Bank in Nepal. All this only reflects that HBL has an outside-in rather than inside-out approach where Customers' needs and wants stand first. HBL has access to the worldwide correspondent network of Habib Bank for fund transfer, letter of credit or any banking business anywhere in the world. Himalayan Bank Limited has just entered into the eighteenth year of successful operation. During these eighteenth years, they have established themselves as one of the top-recognized bank in the country. They have pioneered several products. For starters, they were the first bank to launch card service. Facilities for the convenience of their customers are:

1. Tele-banking
2. Credit card
3. ABBS (Any Branch Banking System)
4. ATM (Automated Teller Machine)
5. Locker facility
6. Himal Remit
7. SMS banking
8. Auto loan
9. Home loan
10. Subidha loan

Table No.1.1
Share Capital of the HBL

Particular	Amount (Rs. in million)
Authorized capital	3000.00
Issued capital	2000.00
Paid up capital	2000.00

(Source: Annual Report of HBL)

Paid up capital has increased to Rs.2000 million from Rs.1600 million in 2009/10 by capitalization of profit and issuance of bonus shares. Their net worth is valued at Rs.3995.40 million at the end of last fiscal year. Deposit stands at Rs. 40920.63 million at present. Their loan portfolio stands at Rs. 32968.27 million at present. (19th Annual Report)

Himalayan Bank has collected fund from share capital, loans and borrowings, deposits specially. That has been utilized into different sectors. It is into investment and loan and advances. Investment lies in Nepal Government securities, Nepal Rastra Bank debenture and share, debentures and bonds of other companies, while loans in different sectors.

1.3.2 Nepal SBI Bank Limited:

Nepal SBI Bank Ltd. is the first indo Nepal joint venture bank in the financial sector sponsored by three institutional promoters, namely State Bank of India, Employees Provident Fund and Agricultural Development Bank through the memorandum of understanding signed on 17th July 1992, the bank began operation on 8th July 1993 within a period of less than one year. NSBL is a joint venture bank registered on 2050/01/06 by the Department of Industry, NG.

State Bank of India owned 50%, Employee Provident Fund owned 15%, Agricultural Development Bank owned 5% and General Public owned 30% of total share.

NSBL is the fifth joint venture bank established in Nepal and until the date of this study Nepal SBI Bank Ltd. has its forty three full-fledged branches, six extension

counter. NSBL has corporate office at Hattisar. Inside the valley, the bank branches are located at Durbar Marg, Bhaktapur, Bouddha, Lainchaur, Dallu, Gaushala, Gongabu, Gwarko, Kalanki, Kuleshwor, Maharajgunj, New Baneshwor, New Road, Patan and Teku. Besides, outside the valley, the branches are located at Abukhaireni, Baglung, Bhairahawa, Biratnagar, Birgunj, Birtamod, Butwal, Dang, Damak, Damauli, Dhangadhi, Dharan, Gulmi, Hetauda, Itahari, Ilam, Janakpur, Mahendranagar, Narayangarh, Nepalgunj, Pokhara, Palpa, Rampur, Shishuwa, Surkhet and Tikapur .

The bank had set up its corporate and banking office at Durbarmarg with computerized operations. However, the space available at Durbarmarg was not adequate to facilitate its business, latter the corporate office was shifted to Kamalpokhari leaving Durbarmarg office as banking office. Now this bank has its corporate office at Hattisar. Various centers were surveyed for its Branch extension and action plan in this regard was finalized to implement it in future. Regarding the branch expansion since its establishment, most of the boarder cities of Nepal- India have been favored. In course of Branch Expansion in the border city of Nepal-India, the first city branch outside Kathmandu was established at Adarsha Nagar, Birgunj on 2052/08/01 (17.11.1995)

Nepal SBI Bank Limited is being giving all shorts of commercial banking facilities to its customers. Such as: it accepts deposits from customers and such accumulated deposits are used to lend to the borrowers. Not only it provides the lending and deposits collection facilities, it also facilitates to its customers by the means of Letter of Credits, Guarantees, collection of outward as well as inward bills. Customers are taking facility of local clearing with out charge. Nepal SBI Bank Limited has the broad network with all over India as it is the joint venture bank with State Bank of India and the parent bank has about 12 thousand branches in India only. Its network is also linked with rests of the world. In India, the State Bank of India has launched its own credit card (SBI Card).

Issue and payment of Demand Drafts drawn to and from India is its main service. This bank, not only give service of money transfer to and from India by the means of Demand Drafts, it also issue SBI Rupee Traveler's Cheques. SBI Rupee Travelers'

Cheque is as good as cash but better to carry with than cash because of big denominated cheques. The facilities of money transfer which is giving by the bank by the means of:

- a) Demand Drafts
- b) Traveler's Cheques
- c) Fax Transfer
- d) Telex Transfer etc.

Table: 1.2
Share Capital of the NSBL

Particulars	Amount (Rs. in million)
Authorized capital	2000.00
Issued capital	1869.30
Paid up capital	1869.30

(Source: Annual Report of NSBL)

Paid up capital has increased to Rs. 1869.30 million from Rs.1653.62 million in 2009/10 by capitalization of profit and issuance of bonus shares. Their net worth is valued at Rs.2869.60 million at the end of last fiscal year. Deposit stands at Rs. 42415.44 million at present. Their loan portfolio stands at Rs. 21718.79 million at present. (18th Annual Report)

Nepal SBI Bank has collected fund from share capital, loans and borrowings, deposits specially. That has been utilized into different sectors. It is into investment and loan and advances. Investment lies in Nepal Government securities, Nepal Rastra Bank debentures and share, debentures and bonds of other companies, while loans in different sectors.

1.4 Statement of the Problem

Although the Nepalese financial sector is growing at a faster pace, it has not remained out of any challenges. Various opportunities have been emerged in the Banking Industry in Nepal due to the globalization and economic liberalization. Many financial institutions have been established. Likewise there are number of challenges in the Nepalese financial system.

The major challenges of the Nepalese financial system are as under:

- Development of investment friendly environment.
- Development and innovation of new products to attract the potential customer.
- Commercial banks are more prone to commercial loans only and give less priority to provide credit facilities for agricultural activities and cottage and small industries.
- Nepalese banks and financial institutions have to be prepared to face international competition in terms of technology, productivity, efficiency capital and experience.
- Banks have to manage their capital in line with their risk exposure as per the BASEL II, which have added challenge to provide sufficient return as required by their risk exposure.
- Unhealthy competition among the commercial banks.

In the under-developed countries like Nepal, the major problem is that capital formation and proper utilization of the resources of existing in the economic system. Commercial banks are responsible to avoid above problems and to contribute to the national economy in the existing scenario. Various commercial, joint venture banks, development banks have played vital role by accepting deposits and providing various types of loans according to the needs of various types of customers. Despite its regular functions performed by the joint venture banks, there exist a considerable number of problems regarding joint venture banks, services they offer, their relationship with the concerned individuals, groups and organizations.

The majority of the commercial banks originated by government are found to be unsatisfactory. The financial loss and marginal responsibilities for their ailing units have to be done by the government. But the private banks are running successfully. The joint venture banks are not interested in granting loan to the primary sectors of the economy. Banking is not being easy accessibility of public in remote village area. Private Banks has concerned their operation mainly in town and capital of the country. The present study will try to analyze and examine the loan management and investment portfolio of respected banks.

The present status of commercial banks seems to invest funds in the less risky sectors of the economy giving a less priority to other sectors of the economy like small business and agriculture. This is mainly due to the lack of sound investment policy of commercial banks and proper loan management. The main problem that lies behind this poor loan management is that the activities of commercial banks are dependent upon the instructions and guidelines of Nepal Rastra Bank. The commercial banks do not have their independent investment policy, which may help enhance the profitability of the bank as well as work in the general interest of the economy of the nation.

The entire banking sector of Nepal is coping with multiple challenges such as, liquidity crisis, inflated interest rate, declining deposits and danger of real estate collapse. From the overview of the issues, the liquidity problem that started in the second half of the fiscal year 2009-10 is not going to be resolved any time soon and this is reflected in the inter-bank lending rate which stands at around 10 percent. According to Maha Prasad Adhikari, newly appointed deputy governor of Nepal Rastra Bank (NRB), “The banking sector will continue to see tight liquidity for a few more months.” Increased government expenditure in the coming months might give some relief.

The main source of liquidity in the banking sector is deposits. But, commercial banks have failed to attract depositors despite offering high interest rates on deposits. NRB, in its report on the macro-economic situation of the country, has revealed that the diversion of deposits from commercial banks to class B and C financial institutions is the main reason for deposits declining in commercial banks. According to the report, bank deposits declined by Rs 4.5 billion in the first four months of the current fiscal year. Deposits in commercial banks stood at Rs 622 billion as of December 24, 2011 on the contrary development banks’ deposits rose by 63 percent to Rs 77 billion and finance companies saw their deposits grow by 35.08 percent to Rs 77 billion in the last fiscal year.

However, bankers don’t agree with the central bank’s claim. “Deposits have not diverted, only the money in the informal sector went to other financial institutions,” said Sashin Joshi, president of Nepal Bankers’ Association (NBA). “Until the

provision related to capital gain tax and anti-money laundering is relaxed, deposits are not going to come to the banks.”

Another challenge for the banking sector in 2011 is recovering loans given to the realty sector. After the central bank capped bank loans for the realty sector in the second half of the last fiscal year, realty transactions have nosedived. The central bank has confined lending to the housing sector to 25 percent and realty to 10 percent through the monetary policy.

“With realty prices starting to come down and possibility of real state collapse not ruled out, those having taken loans in the speculative market may default,” said Joshi. “Defaults may go up in the third and fourth quarter of the current fiscal year.” As of the first quarter of the current fiscal year, bank lending to the realty sector stands at about Rs 100 billion, with Rs 65 billion in land alone.

Another challenge facing banks is to maintain profitability. Banks’ net profit shrank to Rs 3.46 billion in the first three months of the current fiscal year from Rs 3.80 billion in the same period last year, according to banks’ quarterly financial statements. “Profits of banks will come down in the new year due to narrowing margin and intense competition among BFIs,” said Joshi.

Apart from the afore mentioned problems, other problems are arising from lack of smooth functioning of economy, some of them are arising due to confused policy and many of them are arising due to default of the borrower. Liberalization in economy has produced some degree of opportunities and more than it had created confusion and uncertainty. The liberation of the financial sector demands a new technology of lending to cope with the risky pressures on the profitability of banks and financial sector institutions.

In this perspective, the following are the grossly noted problem of the study.

-) Relationship of investment and loan & advances with total deposits and net profit.
-) Over liquidity caused by the lack of good lending opportunities.

-) Lack of proper coordination between government owned banks and joint venture commercial banks.
-) Low priority to the disadvantage sector.
-) Risk arising from the mismanagement of lending and investment portfolio.
-) Is fund mobilization and investment policy of commercial bank effective and efficient?
-) Is the lending position sound to reflect a good status of the bank's performance?

1.5 Significance of the Study

The study mainly fills a research gap on the study of loan management of commercial banks. The study will provide a useful feedback to the policy makers of the bank and becomes a useful reference for other commercial banks of Nepal and central bank for the formulation of appropriate strategies. This study evaluates the loan management of commercial banks and finds loopholes and significantly contributes to make the management sound.

- i. This study would provide clear vision how bank is managing its loan disbursement.
- ii. The analysis would proved a useful feedback for further improve to the policy makers to the bank.
- iii. This study also becomes a useful reference for the other joint venture banks of Nepal and central bank (NRB) for the formulation of appropriate strategies.
- iv. All the stakeholders of this bank will be benefited from this research.

1.6 Objectives of the Study

The main objectives of the present study are to assess the trend of distributing loan to the public and institutions by the bank and its intention beyond that and how efficiently bank is capable in handling all these jobs. The specific objectives of the study are:

- Assess the liquidity position of commercial banks.
- To analyze the lending strength in relative term and in absolute term of commercial banks.

- To measure the efficiency of lending and its contribution in profitability of commercial banks.

1.7 Limitations of the Study:

Each and every study is followed by some limitation. This study too has some limitations which are as follows:

- i. The secondary data of the latest 8 years are only taken into consideration and hence the conclusion drawn confines to the limited period only.
- ii. The accuracy of this report depends on the reliability of secondary data since secondary data such as Annual reports, text books have been analyzed.
- iii. The results drawn for this study may not be generalized to other banks as two commercial banks are considered for the study,.
- iv. Study of the banking activities is the vast one. The chief objective of this study is bounded within the investing of that particular bank's resource. All the other functional section has not been considered in detail.

1.8 Organization of the Study:

This study has been organized into five chapters.

Chapter I: Introduction

The Introduction chapter deals with introduction, loan management which includes general background, definition of the bank, statement of the problem, objective of the study and significance of the study and limitations of the study and loan management of commercial banks.

Chapter II: Review of Literature

The second chapter is concerned with the review of available literature. It includes conceptual/theoretical review of the related studies books, journals and the published and unpublished research works as well as thesis.

Chapter III: Research Methodology

The third chapter deals with the research methodology used in the study, which includes research design, population and sample, source of data, data collection techniques and limitations of the methodology.

Chapter IV: Presentation and Analysis of Data

It deals with the presentation and analysis of all the relevant collected data. Similarly, this chapter also includes the major findings of the study and this is the heart of the study.

Chapter V: Summary, Conclusion and Recommendation

This chapter deals the summary of the study, the main findings, conclusion, recommendations and suggestion on the basis of the study.

CHAPTER 2

REVIEW OF LITERATURE

Review of literature is the process of locating, obtaining, reading, evaluating, learning and understanding the concepts of the related topic. After selecting the topic of the research, researcher should study different materials like books, journals, magazines, articles etc. to collect the necessary information about the research topic through the different sources. The purpose of literature review is, thus, to find out what research studies have been conducted in one's chosen field of study, and what remains to be done.

This chapter is divided into two main sections. The first section deals with the conceptual framework and the second section the review of previous studies.

2.1 Conceptual Framework

This sub-chapter presents conceptual aspect of the study, which includes concept of commercial banks, loan definition, types of loan, classification of loan, Process, objectives of loan / credit policy, components of loan policy, principle of good lending, etc

2.1.1 Concept / Meaning of Bank

A bank is a financial institution which deals with monetary transactions. The main function of bank is accepting money in the form of deposits from public and advancing loan for the development of trade and commerce. Bank collects scattered money from public in the form of deposit by providing them certain percent of interest and distributes the accumulated fund to others, who are in need of money by charging certain percent of interest, which is usually higher than the interest that it gives to the depositors.

Crowther observes that " the present day banker has three ancestors: merchant, money lender and goldsmith. A modern bank is something of each of these. According to

him, a bank collects money from those who have it to spare or who are saving it out of their incomes and it lends this money to those who require it."

2.1.2 Commercial bank

Commercial banks, as the name itself signifies, are designed to accept deposit and advance credit to commercial sector. Their operations are mainly commercial in nature. Commercial bank occupies quite an important place in the framework of every economy. The commercial banks pool together the scattered savings of community and arrange for their productive use and generate profit. They accept deposits from the public on the condition that they are repayable on demand or on short notice. Commercial banks, these days, undertake numerous kinds of financial activities and provide numerous kinds of financial services apart from the statutory functions.. Dudley Lockett has rightly observes commercial bank to be a "departmental store of financial services". Commercial bank mission, goals, objectives and policies are similar to those of other financial institutions so that commercial bank is business firm. Like any other business organization, commercial banks strive for long run profits by lending and investing funds at their disposal at as high a rate of return as is consistent with an appropriate degree of safety of principal. We can conclude that the commercial bank is merely a business firm engaged in financial intermediation as well as performs additional functions under strict supervision and control of central bank intending to earn profit from each transaction as other business firms.

2.1.3 Credit

The term credit is popularly used to denote the granting of an advance in lump sum, usually on the basis of some acceptable securities. A loan is a type of debt. All material can be lent but this article focuses exclusively on monetary loans. Like all debt instruments, a loan entails the redistribution of financial assets over time.

Traditionally loans were provided for working capital funds for business operations but banks have now extended their lending activities to investment in long term bonds and open end securities, both government and private. Further more, loans are advanced not just for financing trade and industry, but also to government units as well as to consumer for a range of personal products like automobiles, home, education etc. Under the loan system, credit is given for a definite purpose and for a

predetermined period. The borrower initially receives an amount of money from the lender, which they pay back, usually but not always in regular installments, to the lender. This service is generally provide a cost, referred to as interest on debt. A borrower may be subject to the certain restrictions known as loan covenants under the terms of the loan. Acting as a provider of loans is one of the principal tasks for financial institutions. For other institutions, issuing of debt contracts such as bonds is a typical source of funding Bank loans and credit are one way to increase the money supply.

Legally, a loan is a contractual promise of a debt to repay a sum of money in exchange for the promise of a creditor to give another sum of money.

When a lender gives money or property to a borrower and the borrowers agrees to return the property or repay the borrowed money, along with interest, at a predetermined date in future.

"Loan can be defined as the temporary provision of money usually at interest."

2.1.4 Types of credit

1. Funded:

Funded loan refers to the loan which is disbursed in the forms of cash or any other payments made on behalf of customers. Whenever a bank disburses a loan and cash goes out of the bank immediately, then it is classified as funded loan. Funded loans are recorded in the books of accounts and appear in the balance sheet under the heading of loans and advances.

Example of funded loans are: Overdraft/ Cash Credit/ Hypothecation loan, Importers' Loan/ Trust Receipt Loans, Exporters' Loan/ Packing Credit Loan, Short Term Loan/ Demand Loan, Long term loan, Home Loan/ Hire Purchase/Consumer/ Mortgage Loan/ Auto Loan, Credit cards and Bills purchase.

2. Non Funded:

Non funded loans are those loans which bank commits for the future payment or any other conditional payment on behalf of its customer. It involves the issuing

bank's commitment to honor certain promises as per the letter of credit or guarantee or similar documents favoring a third party, without requiring any immediate outlay of funds by bank at the time of making commitment. It does not appear in the banks balance sheet. It is recorded as contingent liabilities outside the balance sheet.

Examples of non-funded loans are: letter of credit, Guarantee (Bid Bond, Performance bond, Advance payment, retention etc.), Acceptance and endorsement and commitments etc.

3. Fixed Term:

Fixed Term loans are those loans which are granted for the capital expenditure. These types of loans are generally for more than one year and are repaid on fixed installments over the loan tenure. These loans are secured mortgaging the specific fixed assets financed or the entire block of fixed assets of a particular project.

Example : Project Loan, Home/ Housing Loan, Hire purchase and other term loans

4. Working Capital:

Working Capital loans are granted to finance the working capital requirement of business for its day to day operation. The working capital requirement relate to processing, production, sale of goods and services which are granted for bridging the financial gaps in the production cycle of the business.

Example: Pledge, Hypothecation, Overdraft, Demand Loan, Cash credit etc.

5. Retail/Consumer:

These loans are granted for the consumption purpose. They are based on the security and future cash flow of the borrower.

Example: House/Home loan, Vehicle/ Auto loan, Education loan, Personal loan, Management loan etc.

6. Corporate:

Corporate loans are those loans which are granted for big business houses. These loans are appraised on the basis of detail analysis of the borrowers past performance, projected balance sheet and financial statements to determine financial viability of the project and its debt servicing capacity. The technical, managerial, commercial viabilities of the project are critically examined by the banker before granting these loans.

For Example: all the loans disbursed to the corporate sector.

7. Others:

- i. Bills Purchased: Loan granted to the customer for purchasing Traveler's Cheque, Bank cheques, Export/ Import bills etc. They have the limits for short period of time generally 90 days.
- ii. Credit card: The banks generally avail revolving types of limit for the credit card customers. These limits are assigned and loaded in the borrower's card to make withdrawal or to pay the prices of goods and services. Repayment is needed to be made after fixed period of time. Eg. Master Card, Visa Card etc.
- iii. Loans against Fixed deposit: Banks also lend money to its customer against the fixed deposit receipt of own banks as well as other banks.

2.1.5 Meaning of Investment

Investment is a kind of saving in one form as we invest in shares, bonds and property but these are merely transfer of assets from one person to another. As per some personalities investment is defined as below.

William F. Sharpe and Alexander J. Gorden defines investment as, "Investment, in its broadest sense, means the sacrifice of certain present value (possible uncertain) future value." In the view of Sharpe and Gorden the investment is venture that the return is uncertain. So, they have presented their view in the books that banks should look for the safe and less risky investment. (Sharpe, Alexander and Bailey, 2005:1)

An investment is the current commitment of dollars for a period of time in order to derive future payments that will compensate the investors for (1) the time the funds

are committed, (2) the expected rate of inflation, and (3) the uncertainty of the future benefits. (Reilly, F.K., 1994:1)

It is clear that an investment means to trade current fund for some expected future stream of payments or benefits, which will exceed the current outlay by amount of return or interest that will compensate the investor. The return or interest is expected because of uncertainty involved in expected future cash flows. Bank has to be always careful while investing their funds in various sectors.

2.1.6 Classification of Loans

People need money for different purpose so loan can be classified as following according to the purpose of requirement of loan.

1. Social Loan
2. Commercial Loan
3. Hire Purchase
4. Industrial Loan
5. Land and Building
6. Staff Loan
7. Overdraft
8. Bill Purchase

Bank provide loan for different purpose as well as different sectors. Bank collects as deposit from its customers and distribution in different sectors. The priority sector loan are given below.

1. Agriculture
2. Cottage Industry
3. Service
4. Hire Purchase
5. Deprived

2.1.7 Objectives of Credit Policy

The decision made in advance about the management of loan is known as credit policy. Credit is always a matter of judgement, based on one's own experience and convictions. There cannot be 100% correct approach. The ultimate result may be either good or bad of loan approval and from such experience one has to arrive at a proper credit policy. The bank should make a credit policy for its effective operation and investment. Credit policy is made in such a way that loan advanced by a bank should be repaid with interest in time. The main objective of bank is to secure deposit and it is secured only when loans and advances are secured. There is a well-said statement "a hen should not lay all its eggs in the same basket" which means the bank should not consider the policy of investment only in one or two sectors. Concentration in particular type of loan should be avoided. If it considers such policy, certainly its investment policy will not be successful. Therefore, to be a successful and competent bank, it should mobilize its deposit to the optimal level so that it can earn maximum profit by lending the fund in many profitable sectors. The policy of marketability should also be taken into consideration. In a small market in Nepal, a bank should flow its loan by taking the first class securities for its existence in the market.

Encouraging maximum number of loan of small amounts ensures liquidity and with less incidence of bad loan. Necessary conditions have to be incorporated in the sanction letter of loan for safety and liquidity of loans, performing loans have multiple benefits to the society where as non performing loans erodes even existing scare loan. The objectives of a written loan policy are to assure compliance by lending personnel with the bank's policies and objectives regarding the portfolio of loans, to provide personnel with a framework of standard with which they can operate. (Dahal, B and S., 2002:115)

Without creating credit, commercial banks cannot exist in the competitive environment. Loans and advances is the heart of bank's activities. So, Commercial banks must have strong and flexible credit policies.

The objectives of sound credit policy are as follows:

a) Contribute Economic Development

Sound loan policy says that loans are given to the productive sector which multiple benefit to the society as direct and indirect employment generations, capital creation tax to the government, uplift the living standard of the people and many more.

b) Performing Assets

Performing assets are those loans that repay principal and interest to the bank from the generated cash flow. The basic objectives of sound loan policy is to maintain the financial health of the bank which results in the safety of depositor's money and increase in the returns to the shareholders.

c) Guidance to Lending Officials

There should not be any discrimination whether he deals with one officer or another and one branch or another. There should be a uniform standard procedure throughout the organization, which helps, in consistent judgment by the individual loan officers.

d) Establish a Standard for Control

Periodic follow up is essential for proper implementation of any loan policy. A sound loan policy helps in identifying the deviation between actual and standard performance along with corrective actions to be taken.

2.1.8 Components of Lending Policy:

Sound lending policy shall include the following components (*Analyzing and Managing Banking risk, publisher: World Bank*)

i. Limit on total outstanding loans:

A limit on the total loan portfolio is usually expressed relative to deposits, capital, or total assets. In setting such a limit, factors such as credit demand, the volatility of deposits, and credit risks should be considered.

ii. Credit Concentrations:

A lending policy should stimulate portfolio diversification and strike a balance between maximum yield and minimum risk. Concentration limits usually refer to the maximum permitted exposure to a single client, connected group, and/or sector of economic activity (e.g. agriculture, steel or textiles.) This is especially important for small, regionally oriented or specialized banks. A lending policy should also require that all concentrations be reviewed and reported on a frequent basis.

iii. Distribution by Category:

Limitations based on aggregate percentages of total loans in commercial, real estate, consumer, or other credit categories are common. Policies related to such limitations should allow for deviations that are approved by the board.

iv. Type of Loans:

A lending policy should specify the types of loans and other credit instruments that the bank intends to offer to clients and should provide guidelines for specific loans. Decisions about types of credit instruments should be based on the expertise of lending officers, the deposit structure of a bank and anticipated credit demand. Types of credit that have resulted in an abnormal loss should be controlled by senior management or avoided completely.

v. Maturities:

A lending policy should establish the maximum maturity for each type of credit, and loans should be granted with a realistic repayment schedule.

maturity scheduling should be determined in relation to the anticipated source of repayment, the purpose of the loan and the useful life of the collateral.

vi. Loan pricing:

Rates on various loan types must be sufficient to cover the costs of funds, loan supervision, administration (including general overhead), and probable losses. At the same time they should provide a reasonable margin of profit.

vii. Lending authority

In smaller banks, it is typically centralized. Whereas, in order to avoid delays in the lending process, larger banks tend to decentralize according to geographical area, lending products, and/ or types of customers. Credit policy should establish limits for all lending officers. Lending limits could also be based on group authority, which would allow a committee to approve larger loans. Reporting procedures and the frequency of committee meetings should be specified.

viii. Appraisal process:

A lending policy should outline where the responsibility for appraisals lies and should define formal, standard appraisal procedures, including reference to reappraisals of renewals or extensions. Acceptable types and limits on the amount of appraisals should be outlined for each type of credit facility. The ratio of the amount of the loan to the appraised value of both the project and collateral, as well as the method of valuation and differences among various types of lending instruments, should be detailed. A lending policy should also contain a schedule of down payment requirements, where applicable.

ix. Maximum ratio of loan amount to the market value of pledged securities.

A lending policy should set forth margin requirements for all types of securities that are accepted as collateral. Margin requirements should be related to the marketability of securities. A lending policy should also assign responsibility and establish a time table for periodic pricing of collateral.

x. Financial statement disclosure

A bank should recognize a loan, whether original or purchased, in its balance sheet. This should occur as soon as the bank becomes a party to the contractual provisions that apply to the loan. A bank should initially carry the loan at cost.

xi. Impairment

A bank should identify and recognize the impairment of a loan or a collectively assessed group of loans. This should be done whenever it is neither probable nor assured that a bank will be able to collect the amounts due according to the contractual terms of a loan agreement. Impairment can be recognized by reducing the carrying amount of the loan to its estimated realizable value through an existing allowance or by charging the income statement during the period in which the impairment occurs.

xii. Collections

A lending policy should define delinquent obligations of all types and specify the appropriate reports to be submitted to the board. These reports should include sufficient details to allow for the determination of the risk factor, loss potential, and alternative course of action. The policy should require a follow-up collection procedure that is systematic and becomes progressively stronger. Guidelines should be established to ensure that all major problem loans are presented to and reviewed by the board.

xiii. Financial information:

The safe extension of credit depends on complete and accurate information regarding every detail of the borrower's credit standing. A possible exception to this rule is the case in which a loan was originally approved with readily marketable collateral to be used as a source of repayment. Lending policy should define the financial statement requirements for business and individuals at various borrowing levels and should include appropriate guidelines for audited, non-audited, interim, cash flow and other statements.

- xiv. A lending policy should be supplemented with other written guidelines for specific departments of the bank. Written policies and procedures that are approved and enforced in various departments should be referenced in a bank's general lending policy. The absence of written policies, guidelines and procedures is a major deficiency and a sign that a board of directors is not properly executing its fiduciary responsibilities.

2.1.9 Credit process:

Before granting loan, banks & financial institutions have to pass through a predetermined process. Well-defined process helps to minimize credit risk as well as other potential complexities of future. There are various processes which have to be passed for granting the loan. The processes are explained below.

1. Credit Appraisal

Credit appraisal is the process whereby the risks relating to the repayment of a loan are evaluated. It is the first step in credit process, which involves analysis of borrower's capacity to repay the loan. Good credit appraisal may be a milestone in maintaining good credit portfolio in the banking business. Better credit quality may be regarded as outcome of the better credit appraisal technique. Every lending situation may vary from case to case. Proper credit appraisal involves the assessment of three main aspects: the applicant, the purpose, and the security. The banks should also assess the applicant's character and capital position (or financial capacity to repay). The Banks should also assess the economic and industry conditions and the borrower's need for funds, including the feasibility of any proposed venture, the amount of funds required, and the cash flow expected to liquidate the credit facility. Banks should assess the marketability and price stability of the security offered. Moreover in case of business borrowers financial statements and project progress reports are normally good indicators of the state of their business.

A credit appraisal is a generally standardized presentation demonstrating the detail analysis of a particular lending situation. The conclusions drawn on the analysis helps in decision making for lending. Before making the credit appraisal it is must for the

credit analyst to understand the situation of macro environment and the industry a firm operates in.

2. Credit Approval

The loan is approved by competent authority after completion of the credit appraisal on the basis of the recommendation of credit analyst as well as credit risk officer. Approving authority may enquire and make addition in terms and conditions of the credit agreement during the stage of approval. Principally the approval process needs to be started after completion of the documentation process. But in practice the competitive market has developed the trend of collecting initial document in the first stage for approval of loan. Final and original documentation are obtained only before disbursement of loan. Approval of credit facilities should be done only by the authorized officers of the bank within their respective authorized limits. In practice, “Principally agreed” type of pre-approval is also granted to the borrower subject to the condition of providing necessary documents (securities) before disbursement of loan.

3. Credit Documentation

Credit documentation means obtaining and executing necessary legal documents in order to protect the interest of the Bank. The borrower must present the documents before being availed the loan as specified in the agreement. Documentation means the execution of credit documents in the proper form as required by bank’s internal policies as well prevailing legal provisions. It establishes the contractual relationship between lending bankers and the borrowers. Documents are essential to avoids ambiguities and settlement of future disputes.

The necessity of credit documents depend on the type of loan product. There are several credit documents which are required. Some of the documents may be compulsorily required as per bank’s credit policy guideline while others may be needed to minimize credit risk. Loan and security documentation refers to the possession and possible use of legal documents to validate the claim of the Bank against the borrower. The credit analyst prescribes the document to be obtained while obtaining the approval for various facilities provided to borrower.

4. Disbursement

After ensuring that all the documents have been obtained from the borrower, banks disburse the approved loan limits. The disbursement may be in full or in partial amount as per the approved terms and conditions. In case of revolving credit banks provide limit to the customer and in case of long term financing the disbursement is guided by the terms and conditions specified in the offer letter.

5. Credit Monitoring

Credit monitoring is the process of ensuring the lent fund is utilized for the sanctioned purposes. Whether the borrower is complying with terms and condition specified in the credit agreement, is the main concern of credit monitoring. Regular monitoring process of credit provides important information, which can be the early warning signals for future risk. The credit monitoring may be viewed from two aspects. First, regular credit supervision for good customers which includes stock/receivables/trading assets monitoring in case of project financing, and repayment of interest as well as installment. Second, delinquent borrowers must be monitored with special care which includes follow up, issue of reminder letter, security observation etc.

6. Credit Recovery and Restructuring

All the borrowers may not serve interest as well as principal on time according to the agreed term and conditions. In case of delinquent in payment banks need to take recovery action. When borrower fails to meet obligation, banks take recovery action as per the recovery policy of the bank. The actions regarding recovery are; issue reminder notice, 7/15/35 days notice as per prevailing laws. The bank may go for recovery of its dues through selling of the mortgaged/pledged/lien assets when there is no chance of repayment by the borrower.

Sometimes borrower may request for the continuation of credit agreement by restructuring the terms and conditions. In such case, if the bank is assured that the loan will be repaid once the loan is restructure/rescheduled, new agreement can be established which is known as restructuring of loan.

2.1.10 Principle of good lending

Banks have to follow the basic principle of lending for minimizing risk associated. Credit and investment should be secured and generate good income. Therefore, it is important that bank extends credit facilities based under certain principles, which are as follows:

1. Principle of safety and security

The bank should lend their fund in those areas where there is least probabilities of default. While granting a loan, bank should carefully examine the economic, financial and commercial viability of the business, quality of its management and past track record. The bank should accept that type of securities, which are commercial, durable, marketable and high market prices. In this case 'MAST' should be followed for the investment.

M=Marketability

A= Ascertain Ability

S=Stability

T=Transferability

2. Principle of liquidity

The bank should have best mechanism to manage the assets and liabilities in a sound manner. The bank has to regulate the maturities of its assets (loan) with the maturities of liabilities (deposit). The bank should not delay or default the making payment to its depositors or other liabilities, as this would result in loss of trust and faith of customers. Once the confidence is lost in depositor's eye they may withdraw all their deposits within a short period without giving any chance to the bank to manage. Even the best bank can hardly survive in such situation. Hence, the liquidity position of the bank is such an important factor. Bank must comply the various regulatory requirement regarding liquidity like Cash Reserve Ratio (CRR) and Statutory Liquid Ratio (SLR).

3. Principle of Risk Diversification

The bank should mobilize its resources on various collateral, various places, different business, different individuals and different organization in order to mitigate risk. This would help the bank to minimize the loss if any one sector fails to repay loan. The credit risk can be minimized through diversification of credit portfolio that means

prevention from excessive concentration of loans into few borrowers/ industries/ sectors.

4. Principle of Profitability

Banks are commercial organizations with the motive to derive the maximum profit for the sustainability and growth. A commercial bank wants to maximize the volume of wealth through maximization of return on their investment and lending. The bank needs to pay adequate return to their shareholders. They take risk and invest their fund where they gain reasonable amount of return. The profit of commercial bank mainly depends on the interest rate, volume of loan, its time period and nature of investment in different securities.

5. Principle of loan purpose

Banks should analyze the cause, purpose and objective of the loan. If the disbursed loan from the bank is misutilized, there will be less chances of repayment by the borrower. Lending activities should be guided by banks' own credit policy and remained within the boundaries of legal framework. They need to be careful to prevent lending money laundering terrorist activities, conducting illegal business etc.

6. Principle of National Interest

In addition to its own business profitability, the bank should also consider the national interest. Even though the bank cannot get maximum returns from such investment, it should carry out its obligations towards the society and the country. The bank is required to invest on such sectors as per the government and Nepal Rastra Bank's instruction. Government bonds, priority sector and deprived sector lending are the examples of such interest.

2.2 Theoretical Review

Bank is defined as an institution which deals with money and credit. Generally, the word bank is understood as the place where we can keep our extra money for safety and its proper investment and also the place where we can go for the financial help. Some of the definitions of the banks are given by different personalities are as follows:

As per Kent-"A bank is an organization whose principal operations are concerned with accumulation of the temporarily idle money of the general public for the purpose of advancing to other for expenditure."

As per Sayers - "A bank is and institution whose whole debt are widely accepted in settlement of other people's debt."

"Ordinary banking business consists cash for bank deposits and bank deposits for cash; transferring bank deposits from one person or corporation to another giving bank deposits in exchange for bills of exchange, government bonds, the secured promises of businessmen to repay and so forth."

As per Dr. H.L. Hart -"A banker is one who, in the ordinary course of this business, receives money which he pays by honoring cheque of persons from whom or whose accounts receives." (Khadka, Sergunj and Singh, Hridaybir, 2057:4)

As per C.R. Crowther-"A bank collects money from those who have it to spare or who are saving it out of their incomes, and it lends this money to those who require it." (Singh, Hridaybir, 2007:5)

As per H.D. Crosse -"Lending is the essence of commercial banking, and consequently, the formulation and implementation of sound policies are among the most important responsibilities of bank directors and management. Well conceived lending policies and careful lending practice are essential in a bank to perform its credit creating function effectively and minimize the risk inherent in any extension of credit.

He further states, "The field of investment is more challenging as it offers relatively greater scope to banker for judgement and discretion in selecting their loan portfolio. But this higher degree of freedom in the field of credit management is also accompanied by the greater risk." (Crosse, H.D., 1963)

James B.Bexely

James B.Bexely, expresses his view as, "Investment policy fixes responsibilities for the investment disposition of the bank's assets in terms of allocating funds for

investment and loan, and establishing responsibility for day to management of those assets.” It is assumed the management should be responsible for the investment decision of banks. (Belxely, James, 1987)

2.3 Review of Monetary Policy

Monetary Policy for Fiscal Year 2010/11 has also introduced a credit ceiling on real states and housing loans to reduce credit concentration risk. However, in view of the relatively higher value addition of housing sector, the credit ceiling on the housing sector will be moderately eased while the credit ceiling on land purchase and plotting

will be continuously tightened. For this purpose, in 2010/11 the credit ceiling for land purchase and sale has been fixed to 10% of total credit. The institutions that have credit flow on land purchase and sale in excess of the specified limit should bring down such exposures to 10% of the total credit within two years time.

Cash Reserve Ratio

Cash Reserve Ratio (CRR) is the portion of deposits that the banks have to maintain with the central bank. The higher the ratio, the lower the amount that banks can use for lending and investment. CRR is in the form of fiat currency stored with NRB, the central bank. As per the present provision, 5.5 percent cash reserve ration has to be maintained with NRB by the commercial banks and financial institutions. The reserve ratio is used as a tool in the Monetary Policy, influencing the country's economy, borrowing, and interest rates. It will cause immediate liquidity problems for banks with low excess reserves.

Statutory Liquidity Ratio

Statutory Liquidity Ratio restricts the bank's leverage in pumping more money into the economy. As per the new provision, commercial banks have to maintain 15% SLR. SLR is maintained in liquid form with the banks themselves. SLR refers to the amount that all banks require to maintain in cash or in the form of gold or approved securities. The investment on government security, cash in vault; deposit held with the NRB including cash reserve ratio of bank and financial institutions will be eligible for

the calculation of SLR. The objectives of SLR are to restrict the expansion of bank credit, augment the investment of banks in government securities and ensure solvency of banks.

We can get SLR by adding Cash and Bank balance and Investment on government securities and dividing by total deposits.

2.4 Review of NRB Directives

Nepal Rastra Bank (NRB) is an apex institution in money and capital markets in Nepal. It works as a central bank of Nepal. Being the nation's central bank, it directs, supervises and controls the functions of commercial banks and other financial institutions. NRB has issued various directives in order to develop a healthy, competitive and secured economic systems to ensure overall national development. A unified directives was issued to all commercial banks and financial institutions licensed by NRB on 16th July 2005 in place of different directives issued earlier. The relevant things have been highlighted here.

NRB in the directives has directed all the national level commercial banks operating at present must increase their paid up capital to Rs. Two billion proportionately by Ashad end 2070 B.S. For this, the base year is fixed as at Ashad end 2064 B.S. and these commercial banks are required to increase the paid up capital proportionately from FY 2064/65 B.S. Currently operating commercial banks can increase the minimum capital funds by at least 80 percent paid capital and rest 20 percent can be adjusted by the source that can be counted in the core capital like general reserve, share premium, non-redeemable preference share and retained earnings. If the commercial banks could not maintain a minimum capital fund of Rs. Two Billion, NRB will take following actions:

-) By the end of the fiscal year 2064/65, they were not allowed to declare and distribute dividend.
-) By the end of the fiscal year 2065/66, they were not allowed to accept deposit.

) By the end of the fiscal year 2066/67, they were not allowed to flow loans and advances.

) By the end of the fiscal year 2067/68, they were not allowed to all the transactions except recovery of loan and payment of deposit. After this time frame, the process of cancellation of license will be initiated.

Directive relating to loan classification and provisioning

With an object to minimize the possible risk associated with credits extended in the form of loans and advances, the directives relating to loan classification and provisioning has issued in exercise of authority under section 79 of NRB Act, 2058

Pass

Loan and Advances whose principal amount are not past due and past due for a period up to three months shall be included in this category. There are classified and defined as performing loans.

Sub-Standard

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

Doubtful

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

Loss / Bad

All loans and advances which are past due for a period of more than one year as well as advances which have least possibility of recovery or considered unrecoverable and those having thin possibility of even partial recovery in future shall be included in this category.

Loan and Advances falling in the category of sub-standard, doubtful and loss are classified and defined as non-performing loan. Here, if it is appropriate in the views of the bank management, there is no restriction in classifying the loan and advances from

low risk category to high risk category. For instance, loan falling under sub-standard may be classified into doubtful or loss and loans falling under doubtful may be classified into loss category and the term loan and advances also include bill purchased and discounted.

Loan loss provisioning

The loan loss provisioning on the basis of the outstanding loan and advances and bills purchased classified as above should be provided as follows:

Classification of loan	Loan Loss Provision
Pass	1%
Sub-Standard	25%
Doubtful	50%
Loss	100%

Loan Loss Provision set aside for performing loan is defined as general loan loss provision and loan loss provision set aside for non-performing loan is defined as specific loan loss provision. (NRB directive no.8)

Directive relating to Limit on Credit Exposure and Facilities to a Single Borrower, Group of Related Borrowers and Single Sector of the Economy

According to the directive, commercial banks may extend credit to single borrower or group of related borrower in such a way that the amount of fund based loans and advances is up to 25% of the core capital and non-fund based off-balance sheet facilities like letters of credit, guarantees, acceptances, commitments is up to 50% of its core capital fund (NRB, Directive No.7). The banks are required to adjust as per new regulations in a phase wise manner as follows;

Time Table	Fund based credit limit	Non fund based facilities limit
By the end of Ashad 2059	40% of core capital	75% of core capital
By the end of Ashad 2060	25% of core capital	50% of core capital

Where a customer has once utilized the off-balance sheet facilities and such facilities have turned into Fund-based credit, directives relating to Fund-based credit limit should be applied for fixation of limit to such customer. In the following cases, the exemption in limit of credit and facilities is not applicable.

Credits and facilities, extended against fixed deposit receipts, deposits placed with the bank. NG securities, NRB bonds as well as against unconditional guarantees, issued by the world bank, Asian development bank and international finance corporation including multilateral institutions and loan and advances and facilities extended against unconditional guarantees issued by internationally rated agency or banks specified as first class banks by NRB from time to time.

Advances and facilities to be used for the purpose of importing specified merchandise by the following public corporation.

Name of the Corporation	Merchandise
Nepal oil corporation	Petrol diesel, kerosene and LP Gas
Nepal food corporation	Cereals

For the purpose of the above prescribed exposure limits, group of related borrower should be treated as a single group the following circumstances.

1. Where a company holds 25% or more shares in another company than both of such companies.
2. Director of a company, shareholders of a private company and husband, wife, son. Daughter in law, brother's wife sisters of such director or shareholder residing jointly in the same house or separately as well as all other persons who are supported by such related persons. In the addition, another company in which such persons individually or by their relatives as above. Separately or jointly hold 25% shares, then such companies, or
3. Firm, company stated to be associated as a group, or members of such group or
4. Even if the director, shareholder or other relatives as specified in sub-clause (b) holds jointly or individually, less than 25% shares of another company is controlled by the following ways than such companies:

-) By being chair person of the board of directors
 -) By being the chief executive of the company
 -) By appointing more than 25% of the directors
5. Where one borrower of company gives a cross guarantee to another borrower or company, than such companies
 6. The bank should prepare the record of the single borrower and related customers on half-yearly basis and submit to NRB, banking operation department and inspection and supervision department.

Directive relating to investment in shares and securities by commercial banks.

Arrangement for implementation of investment policy under approval of the board of directors. Banks shall prepare written policy relating to investments in the shares and securities of other organized institutions. Such policies shall be implemented only under the approval of the board of directors. There should be no restriction as to investment by the banks in the securities of organized NG and securities issued by NRB.

Arrangement relating to investment in shares and debenture of organized institutions. Banks must invest in shares and debentures of any on organized institutions no exceeding 10% of the paid-up-capital of such organized institution, the cumulative amount of such investment in all the companies in which the banks has financial interest shall be limited to 20% of the paid-up-capital of the bank and the total amount of investment should be restricted to 30% of the paid up capital of the bank. Any amount of investment made in excess of this limit, for the purpose of calculation of the capital fund, shall be deducted from the core capital fund. For the purpose of calculation of capital fund, the amount of such investment in shares and securities shall be deducted from the core capital fund. Bank should invest in the shares and debentures of organized institutions, which are already listed in the stock exchange or where arrangement exists for listing within one year.

Where, the shares and debentures are not listed within the period prescribed, provisioning equivalent to the whole amount of such investment be provided and credit to investment adjustment reserve. The outstanding amount in such reserve should not be utilized for any other purpose till the paid shares and debentures of the

organized institution are listed. The outstanding amount of investment adjustment reserve should be included under supplementary capital.

Directives relating to cash reserve ratio requirements

To ensure adequate liquidity in the commercial bank, to meet the depositor's demand for cash at any time to inject the confidence in depositor's regarding the safety of their deposited funds, commercial banks are required to have maximum CRR. In this regard, NRB has directed commercial banks to deposit 5% of total deposit in the NRB.

Directives relating to capital adequacy norms for commercial banks.

Maintenance of the minimum capital fund.

The total capital fund is the sum of core capital and supplementary capital. On the basis of the risk-weighted assets, the banks should maintain the described proportion of minimum capital funds as per the following time table:

Time Table	Required Capital	Fund on the basis of weighted risk assets (%)
	Core capital	Capital Fund
For FY 2058/59	4.5%	9.0%
For FY 2059/60	5.0%	10.0%
For FY 2060/61	5.5%	11.0%
For FY 2061/62	6.0%	12%

For the purpose of calculation of the capital fund, the capital of the bank is divided into the following two components:

1. Core capital:

The amounts under the following heads shall be included in the core capital:

- a) Paid up capital
- b) Share premium
- c) Non-Redeemable preferences shares
- d) Accumulated profit and loss account

However, where the amount of goodwill exists, the same shall be deducted for the purpose of calculation of the core capital

2. Supplementary capital

For a purpose of calculation of capital funds, the amount under the following heads, subset up to one hundred percent of the core capital, shall be included under the supplementary capital:

- a) General loan loss provision
- b) Exchange equalization reserve
- c) Assets revaluation reserve
- d) Hybrid capital instruments
- e) Unsecured subordinated debt
- f) Other free reserve not allocated for a specific purpose

(Source: NRB Directive no.1)

2.5 Review of Thesis

During research for this study, various dissertations and thesis submitted by various students have been consulted and been thoroughly analyzed.

i. A study done by Mr. Poudel Purushottam (2004) entitled “A study on Lending Practices of Joint Venture Commercial Bank with Reference to Nepal Bangladesh Bank Ltd. (NBBL) and Himalayan Bank Ltd. (HBL) has following facts and findings.

Major Objectives: impact of deposit collection and its effect on lending practices, to obtain the degree of contribution made by both banks in lending, to evaluate loan disbursement and its recovery and to explore the performance of credit and its contribution in total profitability.

Conclusion: The researcher found that the liquidity position of NBBL is comparative better than HBL because the mean current ratio of NBBL is higher than of HBL. The mean ratio of loan and advances to total assets of NBBL is higher than HBL. But the mean ratio of investment to total loan and advances of HBL is higher than of NBBL. He has concluded that NBBL is able to manage its assets to compete in this competitive banking business than HBL.

Recommendation: The researcher recommends both banks to strictly follow the NRB directives which will help them to reduce credit risk arising from borrower's defaulter, lack of proper credit appraisal, defaulter by black listed borrowers and professional defaulter, Loan loss provision of both banks is in fluctuating trend. So both banks are suggested to adopt sound credit collection policy, which will, helps to decrease loan loss provision.

ii. A study done by Mr. Upendra Shrestha (2005) entitled "Investment practices of joint venture banks in Nepal with special reference to Nabil Bank Ltd. and SCBNL and Nepal SBI Bank Ltd." has following facts and findings.

Major Objectives: Commercial banks intend to invest their funds in inadequate areas to get higher level of profit taking high risk. This may lead to loss in profit as well as principle. Commercial banks extend limited credit to agriculture and industrial sector which is not satisfactory.

Commercial banks tend to make loan on short term basis against movable merchandise. There is huge gap between deposits and investment due to lack of proper investing opportunities. They are even discouraging people by offering very low interest rate and minimum threshold balances.

Conclusion: The study found that the liquidity position of Nabil and SCBNL are not satisfactory, it, is therefore, suggested to them to improve cash and bank balance to meet current obligations. Loans and advances to total deposits ratio of SCBNL is low, and it is recommended to follow liberal lending policy for enhancement of fund mobilization. It is recommended to NSBL that it have to invest its fund on shares and debentures of other companies. It is suggested to enhance off balance sheet transactions, diversifying their investments, open new branches, pay merchant banking role and invest their risky assets and shareholder's fund to gain higher profit margin.

Recommendation: Nabil and SCBNL are recommended to increase their cash and bank balance to meet current obligations and loan demand.

iii. A study done by Ms. Kanchan Sharma (2006) entitled “Investment Policy and Repayment of Loan Investment of Joint Venture Banks in Nepal” studied about the Loan Investment of four banks NSBL, NBBL, SCBL and HBL has following facts and findings.

Major Findings: The researcher found that current ratio of NIBL is fluctuating and have very poorest ratio at the F/Y 01/02. SCBL has also fluctuating current ratio and it has poorest ratio at the F/Y 00/01. On government securities, SCBL has higher and NBBL has lower ratio of investment to current assets ratio than the other banks. From the analysis we can say that SCBL has invested huge amount of its current assets in government securities. As a result shows that all the bank has maintain satisfactory liquidity positions, but NBBL has maintain sound liquidity positions than other banks and SCBL has huge proportion of govt. securities in current assets. The banks are successful to mobilize its deposit on loan and advance and among all banks NBBL has quite successful to maintain high ratio of loan and advance to total deposit ratio and SCBL has mobilize least amount of its deposit to loan and advance. From the analysis of credit risk ratio NBBL has a high credit risk ratio and also NBBL has highest growth ratio of total deposit and NIBL has least growth ratio. SCBL and HBL has satisfactory growth ratios. NIBL has fluctuating trend of total deposit but its growth ratio on net profit is strong as HBL and SCBL seems good on net profit.

iv. A study done by Mr. Ramesh Maharjan (2007) entitled “A Study on Loan Management of Nepal Bank Ltd.” has following facts and findings.

Main objective: To find out effect of new credit policy on loans and advances of NBL and to analyze the trend of loan disbursement, loan recovery as well as to find out the strength and weakness in loan disbursement.

Conclusion: The researcher concludes that “Loan Management of Nepal Bank Ltd.”, concerned with the management of loan disbursement and loan recovery of the concerned institution is been analyzed herein. Efficient and effective flow of loan and advances generate income to banks very appropriately and this finally helps for both long run survival and profiteer. Management of loan disbursement includes lending

management and impact study of lending practices. Similarly lending management encompasses trend analysis of loan disbursement, sector wise loan disbursement with statistical tools of correlation analysis. Lending practices and procedures of NBL includes activities of which is guided by its own loan policy.

v. A study done by Willen N. Joshi (2008) entitled “A study on Credit Management Practices and Analysis of Lumbini Bank Ltd.” has following facts and findings.

Main Objective: To examine and study the lending efficiency or inefficiency of selected commercial bank and also to analyze the relationship of deposits, loans and advances and net profit of the bank.

Conclusion: The researcher has concluded that LBL has maintained its vault to deposit ratio in satisfactory level, therefore, the liquidity position in terms of Vault to total deposit ratio is good as during study period the liquid funds to total deposit ratio has been always above industrial average. This implies the liquidity position of LBL is up to industrial average. Although the liquidity position of LBL is good in terms of Cash in vault, however the status is not satisfactory as the Liquid funds to Total deposit and NRB balance to total deposit curves are below the industrial average in most of the cases. LBL is seen poor in maintaining its balance with NRB. Therefore, it can be concluded that LBL has not maintained adequate liquidity.

Recommendation: The bank was recommended to maintain required liquidity position as per the directives of NRB. Further, it is also recommended to look for portfolio and non-risky area to invest which will help to increase profit of the Bank. If the bank follows strictly the NRB directives it will help to reduce credit risk arising from defaulters. Bank's deposit are fine to meet loan and advances, however proper monitoring of loan and advances should be done to decrease non- performing assets. Bank's provision for loan loss is increasing drastically which affects overall banking performance. So it is recommended to adopt sound lending policy, which will help to decrease loan loss provision and non- performing loan. It is rightly said that “Prevention is better than Cure.”

vi. A study done by Ms. Rabina Maharjan (2010) entitled “A Study on the lending policy and strength of Nepal Investment Bank Ltd.” has following facts and findings.

Main Objective: To observe the loan disbursement of NIBL and to analysis the amount of loan invested in industrial areas.

Conclusion: The researcher concludes that the lending strengths of NIBL in term of exposure of loans and advances is good i.e. ratio of loans and advances to total assets, loan and advances to shareholder’s equity which indicate a good performance of NIBL in its lending activities. Viewing the productivity of loans and advances and its contribution in the national economy, the performance of NIBL has been satisfactory. The contribution made by this bank in agricultural purpose, however, is lower, it has increased contribution to the manufacturing sector continuously. A considerable percentage of NIBL’s credit has been granted to unproductive sector of general use and social purpose; however such loans are also required in order to improve individual’s social status and fulfillment of basic needs. Since, this bank has better activity ratio, it has been a major contribution in managing the lending activity of NIBL which put this bank in the top position in absolute term.

2.6 Review of Articles / Journals

The effort has been made in this present section to examine and review some related articles published in different economic journals, world encyclopedia, bulletins, magazines and newspapers.

i. As per world encyclopedia on the subject loans basically is “Banks and thrifts made three types of loans: commercial and industrial loans, consumer loans, and mortgage loans. Commercial and industrial loans are loans to businesses or industrial firms. These are primarily short-term working capital loans (loans to finance the purchase of material or labor) or transaction or longer-term loans (loans to purchase machines and equipment). Most commercial banks offer a variable rate on these loans, which means that the interest rate can change over the course of the loan.

Whether a bank will make a loan or not depends on the credit and loan history of the borrower, the borrower's ability to make scheduled loan payments, the amount of capital the borrower has invested in the business, the condition of the economy, and the value of the collateral the borrower pledges to give the bank if the loan payments are not made.

Consumer loans are loans for consumers to purchase goods or services. There are two types of consumer loans: closed-end credit and open-end credit.

Closed-end credit loans are loans for a fixed amount of money, for a fixed period of time (usually not more than five years), and for a fixed purpose (for example, to buy a car). Most closed-end loans are called installment loans because they must be repaid in equal monthly installments. The item purchased by the consumer serves as collateral for the loan. For example, if the consumer fails to make payments on an automobile, the bank can recoup the cost of its loan by taking ownership of the car.

Open-end credit loans are loans for variable amounts of money up to a set limit. Unlike closed-end loans, open-end credit does not require a borrower to specify the purpose of the loan and the lender cannot foreclose on the loan. Credit cards are an example of open-end credit. Most open-end loans carry fixed interest rates—that is, the rate does not vary over the term of the loan. Open-end loans require no collateral, but interest rates or other penalties or fees may be charged – for example, if credit card charges are not paid in full, interest is charged, or if payment is late, a fee is charged to the borrower. Open-end credit interest rates usually exceed closed-end rates because open-end loans are not backed by collateral.

Mortgage loans or real estate loans are loans used to purchase land or buildings such as houses or factories. These are typically long-term loans and the interest rate charged can be either a variable or a fixed rate for the term of the loan, which often ranges from 15 to 30 years. The land and buildings purchased serve as the collateral for the loan. (www.encyclopedia.com/loan)

ii. In the article, “Challenges of a non performing loan management in Nepal” Uma Karki has mentioned the course of increasing trend of non-performing loan. She

identifies the major courses such as poor loan analysis guarantee oriented loan system, desire platoon of valued assets, misuse of loan, lack of regular supervision of loan. (Uma Karki, 2059, NRB Samachar Patra vol.47:87)

iii. In the article published in New Business age, Mr. Kamal Subedi, "Growth in Major Commercial Banks" has compared between the first six month of the fiscal year 2002-03 and 2003-04, which shows that there has been noticeable increase in credit outflow by the commercial banks except of Nepal Bank Ltd. (NBL) and Rastriya Banijya Bank (RBB). There has been increase in credit-deposit (CD) ratios of all commercial banks except of NBL and RBB in which case it has gone down by 10.41% and 5.99% respectively. It may be because their concentration was only on recovery of the huge Non Performing Assets. However, Mr. Subedi pointed out that no matter what the size of NPA is and the circumstances are, each bank has to collect the deposit in order to create a lending and to invest in the new venture. Except RBB all banks have increment in deposit collection. A decrease in CD ratio (the percentage of the deposit mobilization over the credit) signifies the presence of high liquidity and comparatively lower fund mobilization and vice versa. High liquidity and idle funds will result in lower profits. HBL has the highest growth of 18.47% in CD ratio over the last year. Similarly, NABIL, Everest Bank Ltd. (EBL) and Nepal SBI Bank Ltd. (SBI) have recorded growth rates of 6.28%, 11.83% and 7.45% respectively in their CD ratio. However, this ratio of other commercial banks had declined, largely due to factors external to the banks. As per the NRB directives, all commercial banks have to maintain loan loss provision according to the size of overdue loans. Nepal Credit and Commerce Bank (NCCB) were able to decrease to its loan provision by 22.63% as compared to the previous year indicating a good recovery of interest as well as principal.

In case of Nepal Investment Bank (NIBL), growth in loan loss provision (which in face decreased by 6.7%) was much less than the growth of the total credit (which is increased by 53%). Similarly, NBL and HBL were able to maintain a healthy composition of loan loss provision (decreased by 9.49% and 0%) and credit (increased by 3.07% and 26.78%), again signifying good results from their loan recovery efforts. In case of remaining banks, the situation is not satisfactory as the

growth of loan loss provision is higher than the growth of credit. (Kamal Subedi, 2004, New Business Age: 47-48, 2004)

iv. Mr. Bhaskar Sharma has said that “Due to the lack of investment avenues, banks are tempted to invest without proper credit appraisal and on personal guarantee, whose negative side effects would show colors only after four or five years.” Again he said, private commercial banks have mushroomed only in the urban areas where banking transaction in large volumes is possible. The rural and sub – urban areas mostly remain unattended to. This is likely to prevail till competition takes its full rein in the areas.” In his article “Banking the future on competition.” (Bhaskar Sharma, October 2000, Business age, page 13)

v. The Article Published in New Business Age entitled (2004), “The world Bank’s Advice on Financial Sector Reform” written by Nubiz reporter states that a team from the world bank has advised the Nepali authorities for a holistic amendment in the recently promulgated “Banking and Financial Ordinance” latest by February 2005, according to highly placed sources.

The article further stated that about the Debt Recovery Tribunal (DRT), the team has raised concern at the problems of enforcing the judgement and lengthy procedures of summons and judgment that follow the practices of the country’s normal legal system. In this regard, the team has advised the Nepali DRT to learn from the practices in India, Pakistan and Bangladesh.

The World Bank team has raised concern also on the way the Credit Information Bureau (CIB) is being developed and perceived in Nepal, stressing that the objectives of the CIB should be to improve the credit culture in the country and to insure that the financial institutions provide more credit to smaller businesses with the help of CIB.

The World Bank feels that it is equally importance to increase access by smaller business to finance from the banking system. In this regard, the world bank team has advised NRB to reduced the threshold to Rs.1 million immediately as a step to reduce if further to Rs. 5,00,000.00 and ultimately to 0. The team has also blacklisting

directives of NRB. Rather it should be developed as an agency that helps the small borrowers to access bank credit. (New Business Age, July 2004)

vi. In the article published in the 'The Himalayan Times, Kuber Chalise, "NRB makes a move against speculative investment" has presented that, the Nepal Rastra Bank (NRB) suspended margin lending on shares and loan renewal, apparently to curb speculative investment. The directive, to be enforced from Dec. 29, 2007, directs category A, B and C financial institutions-commercial banks, development banks and finance companies respectively – to stop margin lending and renewal of loans against shares. "The actual impact will be on the capital market but it will also hit those financial institutions whose portfolio of lending against shares is big," said Radhesh Pant, managing director of the Bank of Kathmandu and president of the Nepal Banker's Association.

"The directive is aimed at stopping manipulation and insulating the stock market," said National Planning Commission member Dr. Posh Raj Pandey. "If the market is not corrected, more stringent measures will be used. Chiranjivi Nepal, chairman of the Securities Board of Nepal, also agreed: " The directive is for market correction. The capital market is said to be fuelled by margin lending on shares that the banks provide subscribers against their shares." Since the financial institutions are more vulnerable due to margin lending, this directive could save them from crisis and stabilize the capital market, Nepal said," NEPSE needs to be cut down to size. If the share market crashes after reaching a sky high, not only will the investors find themselves on the streets but it will also hit the financial institutions and the national economy." (Kuber Chalise, 2007, The Himalayan Times, Vol.VII No. 37 P-1)

vii. Dr. Sunity Shrestha, in her study, "Investment planning of Commercial Banks in Nepal", she has made a remarkable efforts to examine the investment planning of commercial banks in Nepal. On the basis of her study, she has concluded that the bank portfolio (loans and investment) of commercial banks have been influenced by variable security rates. Investment planning of commercial banks in Nepal is directly traced to fiscal policy of government and heavy regulatory procedure of central bank (NRB). So, the investments are not made in professional manners. Investment planning and operation of commercial banks in Nepal has not been satisfactory in

terms of profitability. To overcome this problem she has suggested, “commercial banks should take their investment functions with proper business attitude and should perform lending and investment operation efficiently with the proper analyze of the project.” (Dr. Sunity Shrestha, 1993)

2.6 Research Gap

As going through all the articles, publication and unpublished research works regarding 'loan management' in this field, I have found that previous research is done in one particular banks like loan management in Agriculture Development Bank, Nepal Bank Limited, Lumbini Bank Limited, etc. So, in my research work I have study on commercial banks with especial reference to Himalayan Bank and Nepal SBI Bank for comparing the management of loan system in more broad way. All the above-mentioned researchers did not present the required and precise financial tools that are most relevant and banks frequently use to assess the feasibility of project/businesses. Here, in this study transparency on lending is measured and analyzed by using various statistical tools, methodology, questionnaire and trend analysis as including primary analysis is used in terms of lending may be the stronger factor for commercial banks in Nepalese market. Present study tries to define lending policy by applying those various facts and this can be useful in this area.

CHAPTER 3

RESEARCH METHODOLOGY

3.1 Introduction

Research Methodology can be understood as a science of studying how research has been done. Research methodology refers to the various sequential steps to be adopted by a researcher in studying a problem with certain objectives in view. It describes the method and process applied in the entire subject of the study. It is a systematic way to define the research problem. (Kothari C.R., 1984)

This chapter looks into the research design, nature and sources of data, data collection procedure and tools & technique of analysis. For the purpose of achieving the objectives of the study, the applied methodologies are used. The research methodology used in the present study is briefly mentioned below.

3.2 Research Design

“A research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure.” (Kothari C.R., 1990)

Research Design is a plan, structure and strategy of the investigation conceived so as to obtain answers to research questions and to control variances. It is the arrangement of conditions for collection and analysis of data. To achieve the objective of this study, descriptive and analytical research design and survey research design has been used. Some financial and statistical tools have been applied to examine facts and descriptive techniques have been adopted to evaluate the loan management of commercial banks in Nepal, with especial reference to the HBL and NSBL.

Research design is the definite procedure and techniques, which guides the study and the ways to do the study. This in fact the specific presentation of the various steps in research process. These steps include the selection of a research problem, presentation

of the problem, methodology, survey of literature, data collection, interpretation and presentation, report writing and bibliography.

3.2.1 Population and Sample

There are a total of 32 commercial banks operating in Nepal at present. Data collection of these entire commercial banks operating is not possible. Therefore, among the population the two banks namely Himalayan Bank Limited (HBL) and Nepal SBI Bank Limited (NSBL) have been selected for the sample of the study. Therefore, the population comprises of all the 31 commercial banks and the samples are HBL and NSBL.

3.2.2 Data Collection Procedure

The data and information are collected from both the primary and secondary sources. For the primary information, research interview and questionnaires are used. However, this study is conducted mainly on the basis of secondary data. The secondary data are collected through directives of Nepal Rastra Bank, Annual Reports of HBL, Annual Reports of NSBL, various publications of Nepal Rastra Bank, magazines, other published and unpublished reports and documents from various sources and websites. And also various books and periodicals have been referred for other related information. All the data are compiled, processed and tabulated in the time as per need and objectives.

a) Primary data

The data collected for the first time for the statistical investigation is known as primary data. Those data were collected through questionnaire to the staffs related to the subject of the study, field visit and interviewing several concerned authorities. Related departments were also observed to get practical knowledge.

b) Secondary data

If the data are compiled from any other source it is known as secondary data. These data could be obtained from NRB directives, Journals and other published and unpublished related document, Annual report.

3.3 Analysis of Data

Before analyzing the data, the data and information have been presented systematically in the Tables, Graphs and Charts. Various financial, accounting and statistical tools have been used to obtain the objectives of study. The analysis of data is done according to the pattern of available and because of limited time and resources simple analytical tools such as percentage, mean, standard deviation, coefficient of variation etc. are used for financial analysis.

3.3.1 Financial Tools

Ratio analysis is the best tool for financial analysis which is used to measure the financial position of a firm. Ratios can be taken as expression of relationships between two items or group of items and therefore may be calculated in any number and ways so far meaningful co-relationship is obtainable.

Different types of ratios such as liquidity ratio, asset / liability management ratio, and profitability ratio are used whenever necessary in this study. Some of these financial tools are as follows.

3.3.1.1 Liquidity Ratio

Liquidity means "cash and nearness to cash". Liquidity ratios measure the firm's ability to meet the current obligations. Banking industry has its survival in its ability to create credit and its creation ability depends upon its liquidity ratio. The conventional measure of liquidity ratio in Nepalese banking industry doesn't have significant relevancy. Lack of investment opportunity and excess liquidity in economy has been demanding low liquidity position in our commercial banks. Since, the private commercial banks have been concentrating on major liquid population. The present scenario of banking demands the low rate of liquidity. Some of the best-known measures of a company's liquidity as follow.

a. Current ratio

The current ratio is the simplest and most traditional method for measuring liquidity. It measures the ability of an entity to pay its near term obligations. 'Current' usually defined as within one year. Though the ideal current ratio depends to some extent on the type of business, a general rule of thumb is that it should be at least 2:1. A ratio of

less than one indicates that the company would be unable to meet its current obligations out of its current assets.

The ratio is calculated by dividing current assets by current liabilities.

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

b. Cash Reserve Ratio

Cash Reserve Ratio (CRR) is the portion of deposits that the banks have to maintain with the central bank. The higher the ratio, the lower the amount that banks can use for lending and investment. CRR is in the form of fiat currency stored with NRB, the central bank. As per the present provision, 5.5 percent cash reserve ratio has to be maintained with NRB by the commercial banks and financial institutions. The reserve ratio is used as a tool in the Monetary Policy, influencing the country's economy, borrowing, and interest rates. It will cause immediate liquidity problems for banks with low excess reserves.

Hence, cash and bank balance includes cash on hand, foreign cash on hand, cheques and other cash balance held in foreign banks. The deposit represents current deposits, saving deposits, fixed deposits, money at call and short notice and other deposits. Dividing cash and bank balance calculated the ratio by total deposits.

It can be stated as,

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

c. Statutory Liquidity Ratio

Statutory Liquidity Ratio restricts the bank's leverage in pumping more money into the economy. As per the new provision, commercial banks have to maintain 15% SLR. SLR is maintained in liquid form with the banks themselves. SLR refers to the amount that all banks require to maintain in cash or in the form of gold or approved securities. The investment on government security, cash in vault; deposit held with the NRB including cash reserve ratio of bank and financial institutions will be eligible for

the calculation of SLR. The objectives of SLR are to restrict the expansion of bank credit, augment the investment of banks in government securities and ensure solvency of banks.

We can get SLR by adding Cash and Bank balance and Investment on government securities and dividing by total deposits. It can be stated as,

$$\text{Statutory Liquidity ratio} = \frac{\text{Cash and bank balance} + \text{Investment on Govt. Securities}}{\text{Total deposit}}$$

d. Cash and bank balance to current asset ratio

Cash and bank balance is composed of total reserve and funds. Current assets consist of cash and bank balance, money at call or short-term notice, loan and advances, investment in government securities, other interest receivable and other miscellaneous current asset.

It is stated as,

$$\text{Cash and bank balance to current asset ratio} = \frac{\text{Cash and bank balance}}{\text{Current asset}}$$

e. Investment on government securities to current assets

Investment on government securities includes treasury bills and development bonds etc. This ratio can be computed by dividing investment on government securities by current assets.

It can be stated as,

$$\text{Investment on govt. securities to current asset ratio} = \frac{\text{Investment on govt. securities}}{\text{Current assets}}$$

3.3.1.2 Profitability Ratio

Any organization should earn profit to survive and grow over a long period of time. Profit is the ultimate output of any organization and it will have no future if it fails to make sufficient profits. Thus, the financial manager should continuously evaluate the efficiency of its organization in terms of profit. Profitability ratios are the best

indicator to measure overall efficiency of operation any organization but only profit earning is not the ultimate aim of the organization and it should never earned at the cost of employees, customers and society.

However profitability is the measure of efficiency and the search for it provides an incentive to achieve efficiency. The profitability ratios are these ratios which indicate the degree of success in achieving desired profit levels.

These ratios have also been used to determine the efficiency of the lending, its quality and contribution in total profitability. The following ratios are taken into under the following headings.

a. Earning per share

The income of per common share is known as earning per share. The amount of EPS measures the efficiency of a firm in relative terms. An organization is able to use its resource to generate profit is due to EPS determines that market of a share.

It is stated as,

$$\text{Earning Per Share} = \frac{\text{Net Profit}}{\text{No. of share outstanding}}$$

b. Net profit to shareholders equity

The ratio between net profits after tax to sales is known as net profit ratio. This ratio measures the amount of profit that a rupee of shareholder's fund has received. A higher ratio is the sign of efficient management.

It is stated as,

$$\text{Net Profit to Shareholder's Equity Ratio} = \frac{\text{Net Profit}}{\text{Shareholder's Equity}}$$

c. Total profit to total asset ratio

Profit is the difference between revenue and expenses over a period of time. A company should earn profit to service and grow over a long period of time. This ratio can be computed by dividing total profit to total asset.

It is calculated as,

$$\text{Total profit to total asset ratio} = \frac{\text{Total Profit}}{\text{Total asset}}$$

3.3.1.3 Activity Ratio

Activity ratio measures the efficiency of an organization from various aspects of its operations. These ratios indicate the efficiency of activity on enterprises to utilize available funds particularly short-term funds. Activity ratios are used to determine the efficiency, quality and the contribution of loans and advances in total profitability. The activity ratio measures the performance efficiency of an organization to utilize its short-term funds.

a. Interest income to total income ratio

This ratio measures the volume of interest income in total income. This ratio also helps to measure the bank performance on other fee-based activities.

It is stated as,

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

c. Interest expenses to total deposit ratio

This ratio measures the cost of total deposits in a relative term. The performance of a commercial bank is dependent upon its ability to generate cheaper fund. Cheaper the fund, more the probability of generating loans and advances and vice versa.

It is stated as,

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

d. Interest from investment to total interest income ratio

This ratio measures the contribution made by interest investment in total interest income. The major portion of interest income is generated by the lending function and investment regarded as the cushion against liquidity risk.

It is stated as,

$$\text{Interest from investment to total interest income ratio} = \frac{\text{Interest from investment}}{\text{Total interest income}}$$

e. Interest income to total interest expenses ratio

The ratio of income to interest expenses ratio measures the gap between interest rates offered and interest rates charged. Since NRB has restricted the gap between the interest rate offered and interest charged, in average, should not be more than 5%.

It is stated as,

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

3.3.1.4 Asset / Liability Management Ratio

Asset / Liability Management ratio measures the proportion of various assets and liabilities in balance sheet. The proper management of assets and liabilities ensure its effective utilization. The banking business converts the liability into assets by the way of its lending and investing functions. Assets and liability management ratio measures its efficiency in multiplying various liabilities in performing assets. The following ratios relating to asset liability management are used to determine the lending strength of subjected banks.

a. Total assets to total liability ratio

The ratio of total asset to total liabilities measures the volume of total liability in total assets of the firm. The banks create credit by the way of lending activities and multiply their assets many times than their liability permits so this ratio measures the bank's ability to multiply its liability into assets.

It can be stated as,

$$\text{Total Asset to Total Liabilities} = \frac{\text{Total Assets}}{\text{Total Liabilities}}$$

b. Loans and advances to total deposit ratio

Loans and advances of any commercial bank represent the major portion in the volume of total assets as it also included in the current assets of commercial banks because generally it provides short term loan, advances, overdraft, cash credit, local and foreign bill purchased and discounted.

It is stated as,

$$\text{Loans and Advances to Total Assets Ratio} = \frac{\text{Loans and Advances}}{\text{Total Assets}}$$

c. Investment to loans and advances ratio

This ratio measure the contribution made by investment in total amount of loans and advances. An investment is a commitment of money that is expected to generate additional money. Every investment entails some degree of risk, it requires a present certain sacrifice for a future uncertain benefit.

It is stated as,

$$\text{Investment to Loans and Advances Ratio} = \frac{\text{Investment}}{\text{Loans and Advances}}$$

d. Loans and advances to total deposit ratio

This ratio measures the extent to which the bank is successful to mobilize their total deposit on loans and advances. This ratio indicates the firm's fund mobilization power in gross.

It is stated as,

$$\text{Loans and Advances to Total Deposit Ratio} = \frac{\text{Loans and Advances}}{\text{Total Deposit}}$$

e. Loans and advances to shareholders equity ratio

Shareholders equity consists of share capital, share premium, reserve fund and retained earnings. The ratio between loan and advances to shareholders equity provides the measures regarding how far shareholders equity has been able to generate assets to multiply its wealth.

It is stated as,

$$\text{Loans and Advances to Shareholders Equity Ratio} = \frac{\text{Loans and Advances}}{\text{Shareholders Equity}}$$

3.3.2 Statistical Tools

Some important statistical tools are used to achieve the objective of this study. In this study, statistical tools such as mean, standard deviation (S.D.), coefficient of variation (C.V.), correlation coefficient (r) and linear trend have been used.

3.3.2.1 Standard Deviation (S.D.)

It is a statistical measure of the variability of a distribution of return around its mean. It is the square root of the variance and measures the unsystematic risk in investment. It is denoted by \exists .

Symbolically,

$$\exists = \sqrt{\frac{\sum (X - \bar{X})^2}{N}}$$

Where,

\exists = Standard Deviation

\bar{X} = Values

\bar{X} = Arithmetic Mean Return

N = Time period (No. of Observation)

3.3.2.2 Coefficient of Variation (C.V.)

Standard deviation is the absolute measure of dispersion. The relative measure of dispersion based on standard deviation is known as coefficient of standard deviation.

Symbolically,

$$\text{Coefficient of S.D.} = \frac{\text{S.D.}}{\text{Mean}} = \frac{\exists}{\bar{X}}$$

The coefficient of dispersion based on standard deviation multiplied by 100 is known as the coefficient of variation.

Symbolically,

$$\text{C.V.} = \frac{\exists}{\bar{X}}$$

Where,

\exists = Standard Deviation

\bar{X} = Arithmetic Mean Return

C.V. = Coefficient of Variation

It is independent of unit. So, two distributions can be compared with the help of C.V. It is the measure of relative risk. The higher the coefficient of variation the higher the relative risk of investment.

3.3.2.3 Correlation Coefficient (r)

Another statistical tool, correlation can be used to analyze the relation between two variables. Two variables are said to have correlation when they are so related that the change in the value of one variable is accompanied by the change in the value of other measure of correlation is called correlation coefficient summarizes in one figure, the degree out direction of movement.

Symbolically,

$$\text{Correlation of coefficient (r)} = \frac{n \sum XY - (\sum X)(\sum Y)}{\sqrt{n \sum X^2 - (\sum X)^2} \sqrt{n \sum Y^2 - (\sum Y)^2}}$$

3.3.2.4 Trend Analysis

This topic analyzes the trend of deposits; loan and advances, investment and net profit of all the concerned banks from 2003/2004 to 2010/2011 and forecast for next 5 years till 2015/2016 are made. Under this topic following sub topics have been presented.

-) Trend analysis of total deposit
-) Trend analysis of loan and advances
-) Trend analysis of total investment
-) Trend analysis of net profit

CHAPTER 4

PRESENTATION AND ANALYSIS OF DATA

This chapter deals on the presentation, interpretation and analysis of the study through definite course of research methodology. Various techniques and methods are used for the analysis of loan management of commercial banks of HBL and NSBL in order to fulfill the objectives of the study.

Data presentation is the organization and classification of the data of loan investment and collection for analysis. The main purpose of analyzing the data of loan investment and collection is to change from an unprocessed to an understandable presentation. The analysis of data consist of organizing, presenting in a tabular form for easy reference to the data and also statistical analysis and drawing inferences is used.

Data is analyzed by using proper statistical tools and financial tools such as correlation coefficient, trend analysis and liquidity measurement to find an answer of research question or fulfill the objective of research.

4.1 Analysis of Secondary Data

In this section the relevant ratios are calculated and appropriate interpretations are done.

4.1.1 Analysis of Financial Ratio

In this chapter, the evaluation and analysis of the performance of HBL in comparison to Nepal SBI Bank are done. The ratios which are relevant and useful in study are calculated and presented. The significant ratios that are studied are given below.

4.1.1.1 Liquidity Ratio

Liquidity ratio measures the firm's ability to meet current obligations. It reflects the short-term financial strength of the business. A commercial bank must maintain its

satisfactory liquidity position to meet the credit need of the community. There is following ratios under liquidity ratio, which are as follows.

I. Current ratio

A ratio between current assets and current liabilities is known as current ratio. Current assets are those, which can be converted into cash within short period of time, normally not exceeding one year.(e.g. Cash in hand, cash at bank, B/R–bills receivable, inventory, debtors, loan and advances, investment etc.) Current liabilities are those obligation which are payable within short period normally not exceeding one year. (e.g. Creditors, bank overdraft, B/P-bills payable, provision for tax, deposits etc.)

We have,

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

Current ratios of HBL and NSBL from fiscal years 2003/2004 to 2010/2011 are given below in table no.4.1

Table: 4.1
Current Ratio of HBL and NSBL

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	1.01	1.04	1.10	1.19	1.11	1.30	1.47	1.53	1.22
NSBL	1.94	1.95	2.27	1.91	1.96	2.73	2.81	3.01	2.32
Combined Mean									1.77

Source: Appendix 1

The table shows that the current ratio of both the banks is more than 1. This indicates that the banks are capable of discharging their current obligation. The mean ratios of HBL and NSBL are 1.22 and 2.32 respectively. We can observe that from the fiscal year 2008/09, current ratios of both HBL and NSBL are higher than their mean ratio. The combined mean is 1.77. The current ratio of NSBL is higher than the combined mean whereas that of HBL is less.

II. Cash Reserve Ratio

Cash and Bank Balance is said to be the first defense of the every cash transaction. Now a day, cash position is being judged separately to highlight this crucial business aspect. Cash Reserve Ratio (CRR) is the portion of deposits that the banks have to maintain with the central bank. The higher the ratio, the lower the amount that banks can use for lending and investment. CRR is in the form of fiat currency stored with NRB, the central bank. The ratio between the cash and bank balance and total deposit measures the ability of the bank to meet the unanticipated cash and all types of deposits. Higher the ratio is better to meet the ability of sudden demand of deposit but high ratio is not desirable since bank has to pay the interest on deposits. This will also maximize the cost of fund to the bank.

We have,

$$\text{Cash Reserve ratio} = \frac{\text{Cash and bank balance}}{\text{Total deposit}}$$

Cash Reserve Ratio of HBL and NSBL from the fiscal years 2003/2004 to 2010/2011 are given below in table no. 4.2

Table: 4.2
Cash Reserve Ratio of HBL and NSBL

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	9.09	8.11	6.48	5.85	4.55	8.79	10.28	7.24	7.55
NSBL	12	8.36	10.16	9.81	9.79	4.21	9.86	11.5	9.46
Combined Mean									8.51

Source: Appendix 1

The table shows the cash reserve ratio of HBL and NSBL. The mean ratios of HBL and NSBL are 7.55 and 9.46 respectively. The ratios of HBL was in declining trend till 2007/08 however the ratios increased up in 2008/09 and 2009/10 but again it dropped to 7.24 in 2010/2011. Whereas, the cash reserve ratio of NSBL is fluctuating during the period, lowest ratio of 4.21 was recorded in 2008/09 then it rose up from 2009/10 with the highest of 11.5 in last fiscal year 2010/11. The mean ratio of HBL is lower than the mean ratios of NSBL which shows that the ratios of NSBL is the more consistent than HBL.

III. Statutory Liquid Ratio

Statutory Liquidity Ratio restricts the bank's leverage in pumping more money into the economy. As per the new provision, commercial banks have to maintain 15% SLR. SLR is maintained in liquid form with the banks themselves. SLR refers to the amount that all banks require to maintain in cash or in the form of gold or approved securities. The investment on government security, cash in vault; deposit held with the NRB including cash reserve ratio of bank and financial institutions will be eligible for the calculation of SLR. The objectives of SLR are to restrict the expansion of bank credit, augment the investment of banks in government securities and ensure solvency of banks.

We can get SLR by adding Cash and Bank balance and Investment on government securities and dividing by total deposits. It can be stated as,

We have,

$$\text{Statutory Liquidity ratio} = \frac{\text{Cash and bank balance} + \text{Investment on Govt. Securities}}{\text{Total deposit}}$$

Statutory Liquid Ratio of HBL and NSBL from the fiscal years 2003/2004 to 2010/2011 are given below in table no. 4.3

Table: 4.3

Statutory Liquid Ratio of HBL and NSBL

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	24.68	30.16	25.90	27.33	28.01	20.93	22.15	22.90	25.26
NSBL	38.01	38.26	42.81	29.27	29.93	16.03	22.22	24.64	30.15
Combined Mean									27.70

Source: Appendix 1

The table shows the statutory liquid ratio of HBL and NSBL. The SLR of NSBL is higher than that of HBL during the period of 2003/04 to 2010/11 except in the fiscal year 2008/09 with the lowest SLR of 16.03. The mean SLR ratios of HBL and NSBL are 25.26 and 30.15 respectively, and the combined mean is 27.70. Both the banks have SLR above 15% which shows that both the banks have better liquidity position.

IV. Cash and Bank Balance to Current Asset Ratio

This ratio shows the bank liquidity capacity on the basis of cash and bank balance i.e. the most liquid asset. Higher ratio indicates the bank ability to meet the daily cash requirement of their customer deposit but the higher ratio is not preferred as the bank has to pay more interest on deposit and will increase cost of fund. Lower ratio is also not preferred as the bank may not be able to make the payment against the cheques presented by the customers. Therefore, bank has to balance the cash and bank balance to current asset ratio in such a manner that it should have the adequate cash for the customers demand against deposit when required and less interest is required to be paid against deposit when required and less interest is required to be paid against deposit when required and less interest is required to be paid against the cash deposit. Cash and bank balance is composed to total reserve and funds. Current assets consist of cash and bank balance, money at call or short-term notice, loan and advances, investment in government securities, other interest receivables and other miscellaneous current asset.

We have,

$$\text{Cash and Bank Balance to Current Asset Ratio} = \frac{\text{Cash and bank balance}}{\text{Current asset}}$$

Cash and bank balance to current asset ratio of HBL and NSBL from the fiscal years 2003/2004 to 2009/2010 are given below in table no. 4.4

Table: 4.4
Cash and Bank Balance to Current Asset Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.1107	0.0958	0.0745	0.0647	0.0493	0.0803	0.0952	0.0673	0.0797
NSBL	0.0995	0.0717	0.0857	0.0835	0.0787	0.0399	0.0924	0.108	0.0824
Combined Mean									0.08105

Source: Appendix 1

The table shows the cash and bank balance to current asset ratio of two banks are better as they show the ability to manage the deposit withdrawal from the customers. The mean ratio of HBL and NSBL is 0.0797 and 0.0824 respectively. NSBL shows

the higher average ratio of 0.0824 which indicates that liquidity position of NSBL is better than that of HBL. The combined mean is 0.08105. Comparatively, NSBL seems to have better position maintaining the cash and bank balance to current ratio. It indicates NSBL's capacity of making quick payment of its deposit. The better position of the bank does not mean that the bank has mobilized its fund in the profitable sector. HBL may have mobilized their more funds in productive sectors.

V. Investment of government securities to current asset ratio

The commercial banks are interested to invest funds collected in various government securities issued by government. The government securities are the safest place to make investment. But the government securities are not so much liquid as cash and bank balance. They can be easily sold in the market or they can be converted into cash in other ways. The main purpose of this ratio is to examine that portion of commercial banks current assets that is invested on different government securities.

We have,

$$\text{Investment on govt. securities to current asset ratio} = \frac{\text{Investment on govt. securities}}{\text{Current assets}}$$

Investment on government securities to current asset ratio of HBL and NSBL from the fiscal years 2003/2004 to 2009/2010 are given below in table no. 4.5

Table: 4.5
Investment on govt. securities to current asset ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.1898	0.2601	0.2231	0.2377	0.2542	0.1109	0.1100	0.1455	0.1914
NSBL	0.2155	0.2564	0.2754	0.1657	0.1619	0.1121	0.1159	0.1235	0.1783
Combined Mean									0.18485

Source: Appendix 1

The table shows the investment on government securities to current assets ratio of HBL and NSBL. The mean ratios of HBL and NSBL are 0.1914 and 0.1783 respectively. The ratios of HBL and NSBL have its ups and downs throughout the period but gradually increased in 2010/11.

The combined mean is 0.18485. The mean ratio of NSBL is less than the combined mean, on the contrary, the mean ratio of HBL is higher than the combined mean.

In conclusion we can say that HBL has invested more percent of its current assets on government securities than NSBL. So, we can say that HBL liquidity position is good and HBL takes investment policy less risky than HBL.

4.1.2 Analyzing the Lending Strength in Relative Term

The lending strength of these banks is measured in relative measures in this section. The relationship between various assets and liabilities of the balance sheet has been established to show the relative strength of lending of each bank comparatively.

4.1.2.1 Total Asset to Total Liability Ratio

The ratio of total asset to total liabilities measures the volume of total liability in total assets of the firm. The banks create credit by the way of lending activities and multiply their assets many times than their liability permits so this ratio measures the bank's ability to multiply its liability into assets.

It is always recommended to have higher ratio of total liabilities ratio since it signifies overall increase of credit and overall development of banks performance.

We have,

$$\text{Total Asset to Total Liabilities} = \frac{\text{Total Assets}}{\text{Total Liabilities}}$$

Table: 4.6

Total Asset to Total Liability Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	1.0565	1.0586	1.0638	1.0684	1.0746	1.0862	1.0876	1.0935	1.0736
NSBL	1.0802	1.0713	1.0815	1.0913	1.0897	1.0602	1.0688	1.0666	1.0762
Combined Mean									1.0749

Source: Appendix 2

The above table shows the total asset to total liabilities ratio of two banks. The mean ratios of HBL and NSBL are 1.0736 and 1.0762 respectively. NSBL has the higher

ratios from 2003/2004 to 2007/2008 than HBL. From past three fiscal years i.e. 2008/2009 to 2010/2011, the ratio of HBL is higher than that of NSBL. Since, the highest ratio of total assets to total liability is considered best, HBL has highest ratio in the last fiscal year of 1.0935. The ratio of HBL is in increasing trend throughout the period. In the other hand the ratio of NSBL is more or less consistent from 2008/2009. The combined mean of these two banks is 1.0749.

4.1.2.2 Loans and Advances to Total Asset Ratio

Loans and advances of any commercial bank represent the major portion in the volume of total assets as it also included in the current assets of commercial banks because generally it provides short term loan, advances, overdraft, cash credit, local and foreign bill purchased and discounted. To make a high profit mobilizing of its fund in the best way, a commercial bank should not keep all its collected funds as cash and bank balance but to invested as loan and advances to the customers. Granting the loan and advances always carries the certain amount of risk. If sufficient loan and advances cannot be granted it should be pay interest on those utilized. Deposits funds and high loan and advances may also be harmful to keep the bank in most liquid position because they can only be collected at the time of certain maturity.

We have,

$$\text{Loans and Advances to Total Assets Ratio} = \frac{\text{Loans and Advances}}{\text{Total Assets}}$$

Table: 4.7

Loans and Advances to Total Assets Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.5218	0.4831	0.535	0.5309	0.5578	0.6490	0.6818	0.7054	0.5831
NSBL	0.6554	0.6514	0.6322	0.7240	0.7416	0.5175	0.4721	0.4712	0.6082
Combined Mean									0.5956

Source: Appendix 2

The loans and advances to total assets ratio of HBL and NSBL is presented it the given table. The mean ratio of HBL and NSBL are 0.5831 and 0.6082 respectively. Although the mean ratio of HBL is not satisfactory in comparison to NSBL as HBL has less mean ratio i.e. 0.5831 but the ratio of HBL is in upward trend whereas that of

NSBL is in downward trend from 2008/2009. The mean ratio of NSBL is higher comparing with HBL. The overall combined mean ratio of these banks is 0.5956.

4.1.2.3 Investment to Loans and Advances Ratio

This ratio measure the contribution made by investment in total amount of loans and advances. The proportion between investment and loans and advances measures the management attitudes towards risky assets and safety assets. An investment is a commitment of money that is expected to generate additional money. Every investment entails some degree of risk, it requires a present certain sacrifice for a future uncertain benefit. Here, investment and loan and advances in whole do not provide the quality of assets that bank has created so it measures the risk of banking business too. The high ratio shows the investment in safe side however safety does not provide with satisfactory return so a compromising ratio between risk and profit should be maintained.

We have,

$$\text{Investment to Loans and Advances Ratio} = \frac{\text{Investment}}{\text{Loans and Advances}}$$

Table: 4.8

Investment to Loans and Advances Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.7192	0.8692	0.6908	0.6644	0.6611	0.3413	0.29	0.266	0.5628
NSBL	0.3448	0.3869	0.4561	0.2642	0.2423	0.8510	0.9077	0.8707	0.5407
Combined Mean									0.5516

Source: Appendix 2

The above table shows the investment to loans & advances ratio of HBL and NSBL. Since, this ratio measures the contribution made by investment. The mean ratio of HBL and NSBL are 0.5628 and 0.5407 respectively where mean ratio of HBL is highest one but the investment to loans and advances ratio of last six fiscal years of HBL is in decreasing trend which is not good; on the other hand, investment to loans and advances ratio of NSBL had been significantly increasing in the year 2008/09 and 2009/10 with a slight fall in 2010/11. The combined mean of this ratio is 0.5516.

4.1.2.4 Loans and Advances to Total Deposit

This ratio measures the extent to which the bank is successful to mobilize their total deposit on loans and advances. This ratio indicates the firm's fund mobilization power in gross. The main source of bank's lending and investment is its deposits. This ratio measures how well the deposits have been mobilized.

We have,

$$\text{Loans and Advances to Total Deposit Ratio} = \frac{\text{Loans and Advances}}{\text{Total Deposit}}$$

Table: 4.9

Loans and Advances to Total Deposit Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.5870	0.5421	0.5950	0.5922	0.6337	0.7358	0.7743	0.8057	0.6582
NSBL	0.7685	0.7787	0.7490	0.8794	0.9293	0.5584	0.5148	0.512	0.713
Combined Mean									0.6848

Source: Appendix 2

The above table explains loans and advances to total deposit ratio of HBL and NSBL. The mean ratio of HBL and NSBL are 0.6582 and 0.713 respectively. From the fiscal year 2008/2009, the ratio of HBL has been increasing whereas just the opposite, i.e. declining trend had started in the ratio of NSBL. It shows that from the recently, HBL has been utilizing more of its deposit in loans and advances in comparison to NSBL. The overall combined mean ratio of these banks is 0.6848.

4.1.2.5 Loans and Advances to Shareholders Equity Ratio

Shareholder's equity consists of share capital, share premium, reserve fund and retained earning. The ratio between loan and advances to shareholders equity provides the measures regarding how far shareholders equity has been able to generate assets to multiply its wealth. The shareholders equity refers to the net shareholders intake in the business. Thus, this ratio measures the size of business and their success in converting liabilities into assets.

We have,

$$\text{Loans and Advances to Shareholders Equity Ratio} = \frac{\text{Loans and Advances}}{\text{Shareholders Equity}}$$

Table: 4.10

Loans and Advances to Shareholders Equity Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	9.7568	8.7246	8.9243	8.2864	8.0301	8.1796	8.4682	8.2514	8.5781
NSBL	8.8277	9.7811	8.3893	8.6522	9.0102	9.1159	7.3305	7.5431	8.5812
Combined Mean									8.5796

Source: Appendix 2

The above table explains the loans and advances to shareholders equity ratio of HBL and NSBL. The mean ratio of HBL and NSBL are 8.5781 and 8.5812 respectively. The mean ratio of NSBL is slightly higher than HBL but in the last two fiscal years the ratio of HBL is higher than that of NSBL which shows that HBL is improving its performance. The overall combined mean of these banks is 8.5796.

4.1.3 Analyzing the Lending Strength in Absolute Term

In this topic, the various variables in their absolute value are measured. Unlike ratio analysis, different variables are measured individually. The volume of variables and its variability are measured. The value of individual variables enables to measure the gross contribution of respective banks in those aspects.

A ratio is an expression of the quantitative relation between two numbers as it describes about only two variables but does not tell about absolute value of those variables. So, in this chapter, some of the important individual variables on their absolute value of mean, standard deviation and also coefficient of variation is measured. The absolute value of individual bank is compared to judge the contribution of respective banks and their practices.

4.1.3.1 Total Deposit

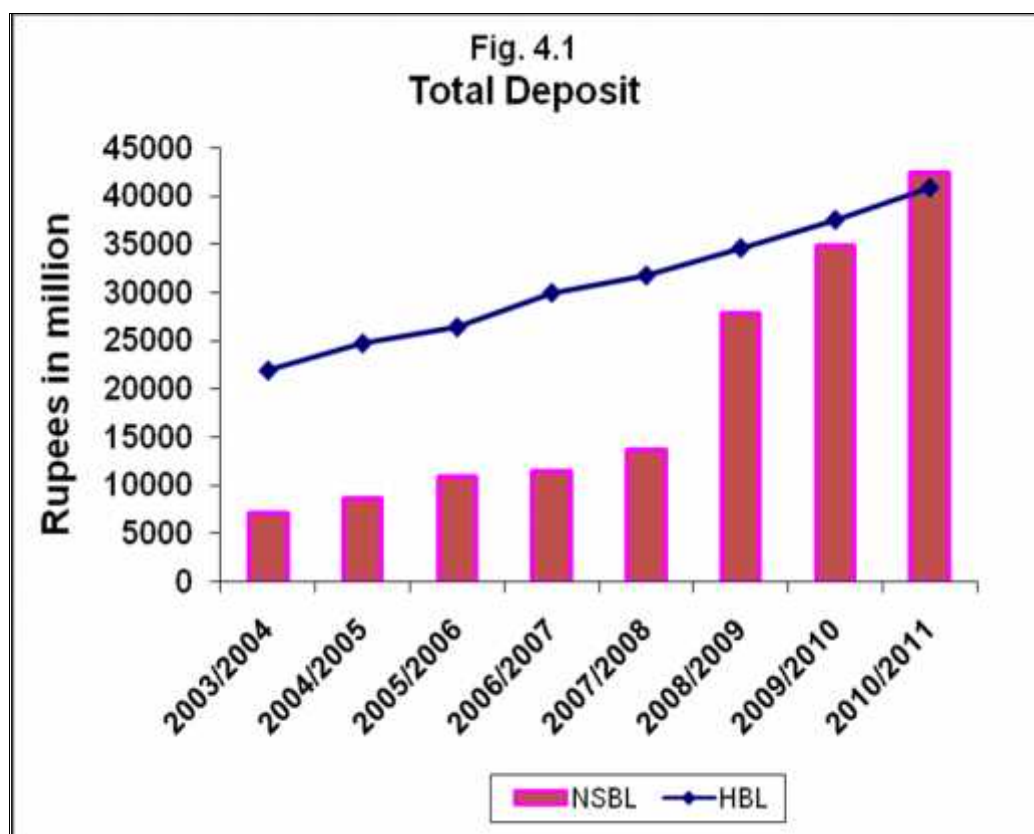
Total deposit consists of all types of deposit like fixed, saving and current deposits. It includes margin deposits and deposits in foreign currency. As deposit is the main source of bank's fund, its volume in total liability plays a vital role in administering the lending and investing function of a bank.

Table: 4.11

Total Deposit of HBL and NSBL (Rs. in million)

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	22010.33	24814.01	26490.85	30048.42	31842.79	34682.31	37611.20	40920.63
NSBL	7198.32	8654.77	11002.04	11445.28	13715.40	27957.22	34896.42	42415.44

Source: Appendix 6



The above figure: 4.1 indicates that the total deposit of these two banks are in increasing trend. HBL has total deposit of Rs. 22010.33 million in the year 2003/2004 and then after it is subsequently increasing throughout the period with as Rs. 40920.60 in the year 2010/2011. Similarly, NSBL had total deposit of Rs.7198.32 in

the year 2003/2004 which has soared up at 2010/11 by 5.89 times and reached to the highest amount of Rs. 42,415.40 in the year 2010/2011. NSBL performance is higher than that of HBL in 2010/11, by 3.65%, which shows that NSBL has been successful in managing its deposits.

Table: 4.12
Mean, S.D. and C.V. of Total Deposits of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	31052.57	6510.3548	20.97%
NSBL	19660.61	13485.3949	68.59%

Source: Appendix 3

The above table shows that the mean of total deposit of HBL is higher than NSBL whereas the standard deviation and C.V of NSBL is higher than that of HBL. The high degree of variation of these two banks is caused by the increasing trend of deposit.

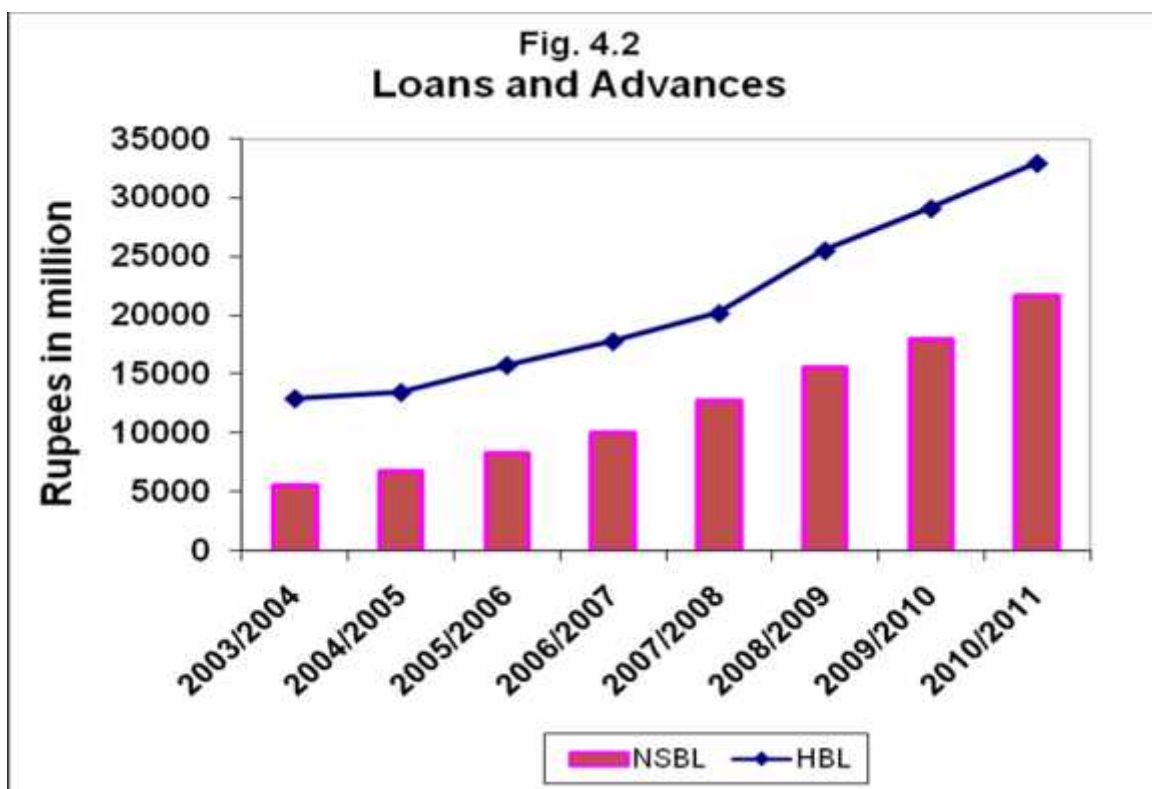
4.1.3.2 Loans and Advances

Commercial bank's function is to create from its borrowed fund. The banks doing so convert its liability into active assets. Loans and advances are the assets coming from such activities. The high volume of loans and advances is the indication of good performance in credit sector. Since the survival of banking business is dependent on good performance of its lending function. The high volume of well performing loans and advances in economy is symbol of healthy business.

Table: 4.13
Loans and Advances of HBL and NSBL (Rs. in million)

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	12919.63	13451.17	15761.98	17793.72	20179.61	25519.52	29123.75	32968.27
NSBL	5531.83	6739.35	8241.46	10065.10	12746.22	15612.05	17963.64	21718.79

Source: Appendix 6



The figure: 4.2 presented above explains that the volume of loans and advances of both HBL and NSBL are in increasing trend. HBL has higher amount of loans and advances than that of NSBL. In 2003/2004, loans and advances of HBL was Rs. 12919.63 million and that of NSBL was Rs. 5531.83 million. Growing all the years, the loans and advances of HBL and NSBL reached to Rs. 32,968.27 million and Rs. 21,718.79 million in the year 2010/2011. As the loans and advances of HBL is more than that of NSBL throughout the period, we can say that the performance of HBL in credit sector is better than that of NSBL.

Table: 4.14

Mean, S.D. and C.V. of Loans and Advances of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	20964.71	7467.24	35.62 %
NSBL	12327.31	5733.97	46.51 %

Source: Appendix 3

The above table shows that the mean and standard deviation of loans and advances of HBL is higher with 20964.71 and 7467.24 respectively. But C.V. of HBL is lower with 35.62% than NSBL with 46.51%.

4.1.3.3 Investment

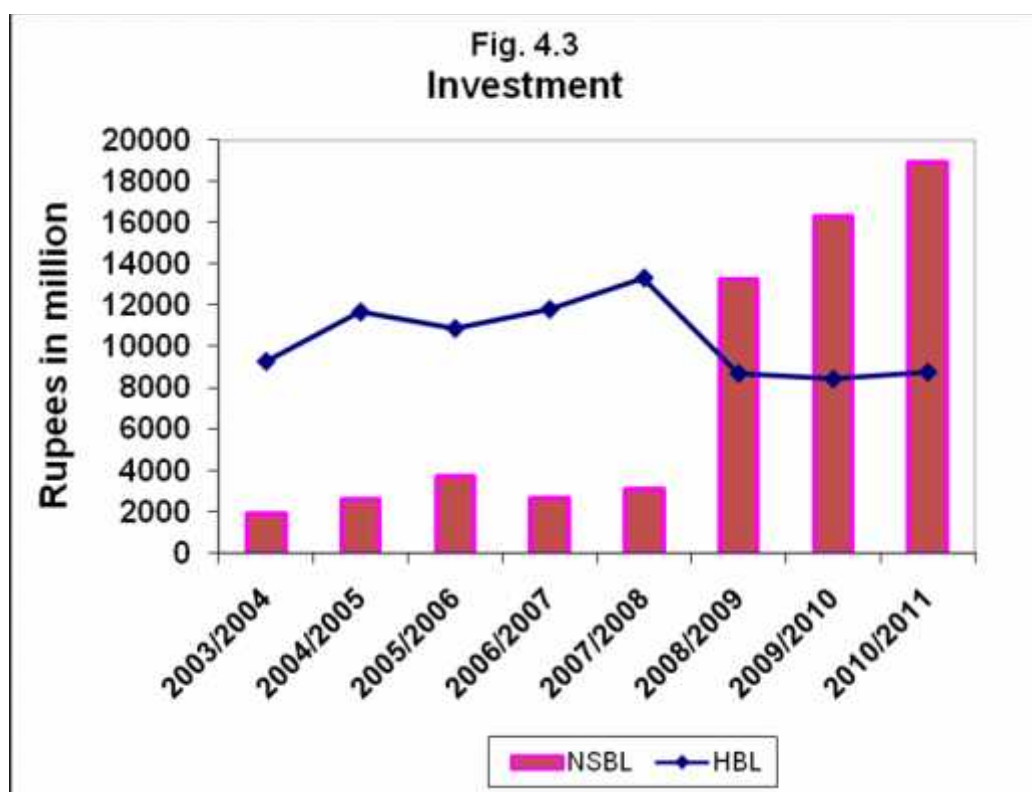
An investment is a commitment of money that is expected to generate additional money. The nature of investment is more liquid than loan and advances. Investment thus provides a caution against liquidity risk.

Table: 4.15

Investment of HBL and NSBL (Rs. in million)

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	9292.10	11692.34	10889.03	11822.99	13340.18	8710.69	8444.91	8769.94
NSBL	1907.52	2607.68	3758.98	2659.45	3088.89	13286.18	16305.63	18911.02

Source: Appendix 6



The above table shows that, the trend value of investment does not have fixed direction. We can notice from the above table that the investment of HBL has been decreasing since 2008/2009 whereas in contrary the investment of NSBL is had increased significantly and is more than that of HBL. HBL had highest investment of Rs. 13,340.18 in the year 2007/2008 but the figure has been constantly decreasing and

reached Rs. 8769.94 in 2010/2011. The investment of NSBL has rose up from Rs. 1907.52 million in the year 2003/2004 to Rs. 18,911.02 million in the year 2010/2011 which is an increment by 9.91 times.

Table: 4.16

Mean, S.D. and C.V. of Investment of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	10370.27	1817.87	17.53%
NSBL	7815.67	7096.5573	90.80%

Source: Appendix 3

The above table shows that the mean value of investment of HBL is higher than NSBL. HBL is better than NSBL in mean investment. The S.D. and C.V of NSBL is higher in comparison with that of HBL.

4.1.3.4 Total Interest Income

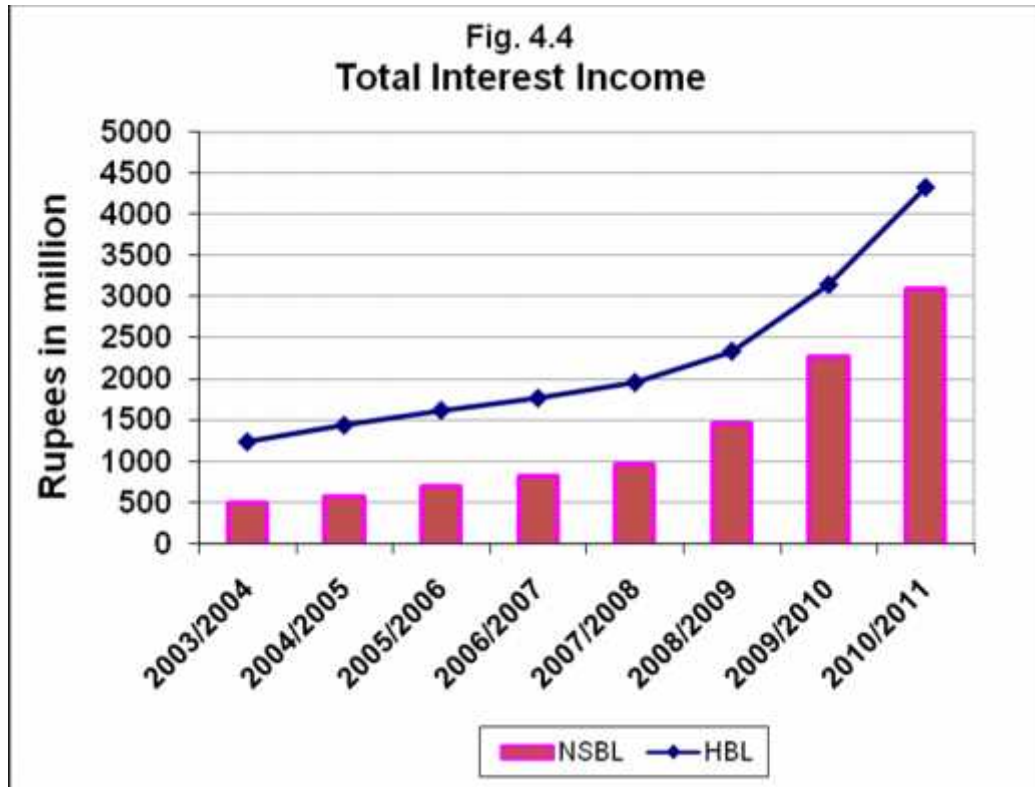
The volume of interest income measures the bank's ability to generate income from lending and investing activities. The high volume is indication of favorable contribution of lending and investing activities in income generation.

Table: 4.17

Total Interest Income of HBL and NSBL (Rs. in million)

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	1245.9	1446.47	1626.47	1775.58	1963.65	2342.20	3148.61	4326.14
NSBL	493.60	578.37	708.72	831.12	970.51	1460.45	2269.70	3104.23

Source: Appendix 6



The above figure shows that the total interest income of all these two banks have a fixed direction and mounting in every subsequent fiscal year. The total income of HBL is higher than NSBL throughout the period. Total Interest Income of HBL was Rs. 1245.9 million in the year 2003/2004 and it reached to Rs. 4,326.14 in 2010/2011. Similarly, total interest income of NSBL in the year 2003/2004 was Rs. 493.60 million and in 2010/2011, it was Rs. 3104.23.

Table: 4.18

Mean, S.D. and C.V. of Total Interest Income of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	2234.3775	1033.3125	46.25%
NSBL	1302.0875	931.23	71.52%

Source: Appendix 3

The above table shows that the mean and standard deviation of HBL is higher but C.V. is lower than NSBL. HBL has successful in maintain its interest income ratio than NSBL.

4.1.3.5 Total Expenses

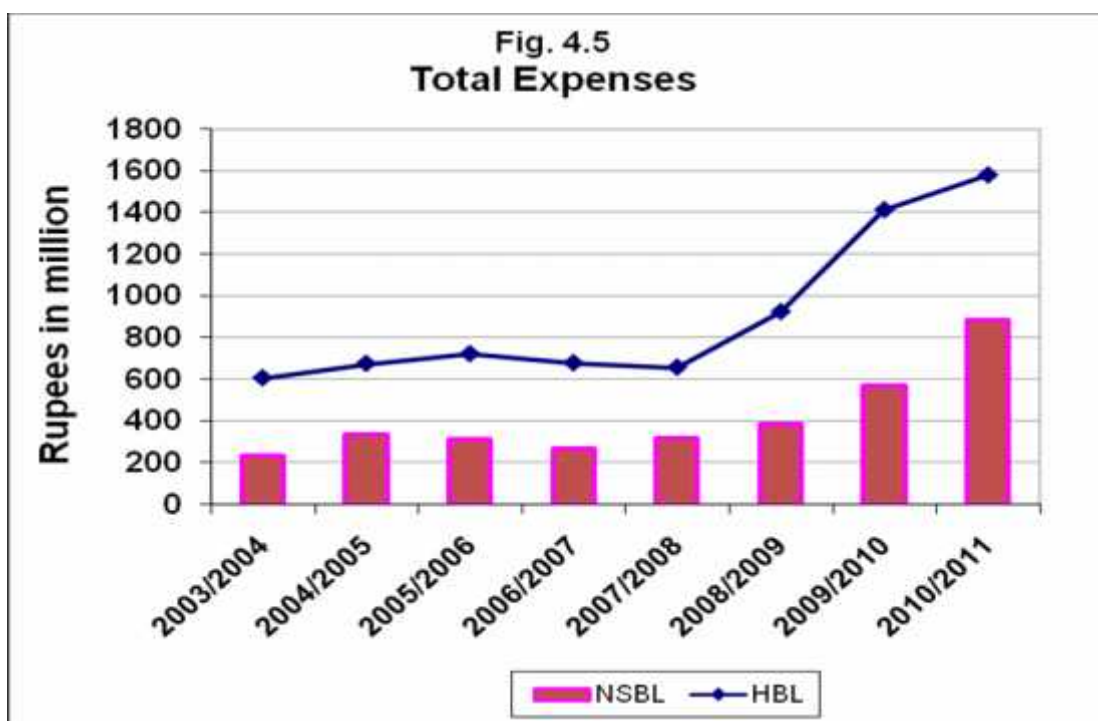
The total expenses include all types of expenses those are charged against profit and loss account.

Table: 4.19

Total Expenses of HBL and NSBL (Rs. in million)

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	607.501	676.175	723.023	679.452	658.357	925.26	1414.61	1581.82
NSBL	255.92	258.43	334.77	412.26	454.92	388.16	571.02	884.48

Source: Appendix 6



The above figure represents the total expenses of HBL and NSBL. We can observe from that the total expenses of HBL had decreased in the year 2006/2007 and 2007/2008 and raised from gradually from 2008/2009. Likewise, similar trend can be observed with the amount of total expenses of NSBL. NSBL, total expenses are ranged from Rs. 255.92 million to Rs. 884.48 in the year 2010/2011. Similarly, total expenses of HBL, in the year 2003/2004 was Rs. 607.501 million and in the last fiscal year, it was Rs. 1,581.82 million.

Table: 4.20

Mean, S.D. and C.V. of Total Expenses of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	908.27	378.6817	36.48%
NSBL	414.89	215.2043	51.87%

Source: Appendix 3

The above table shows that the mean total expenses of HBL is higher with high S.D. and low C.V. comparing with NSBL. NSBL has lowest mean with low degree of S.D.

4.1.3.6 Loan Loss Provision

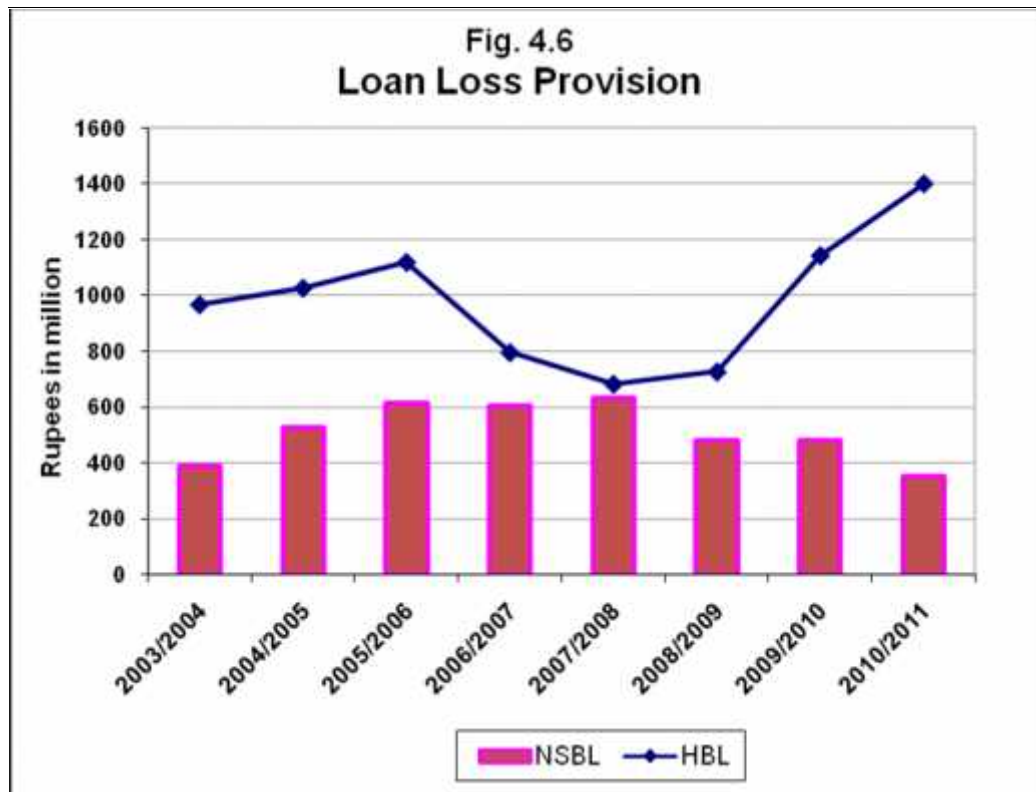
Provision for doubtful debts in balance sheet shows the figure that is the summation of provision made against pass and substandard loans as per NRB directives.

Table: 4.21

Loan Loss Provision of HBL and NSBL (Rs. in million)

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	967.76	1026.65	1119.42	795.726	682.474	726.364	1143.126	1401.29
NSBL	388.17	525.47	614.72	604.60	632.52	480.30	483.09	353.02

Source: Appendix 6



The above figure shows that the loan loss provision of HBL is in increasing order in the first three years and then after the trend is decreased till 2007/2008 and again rose up in the year 2008/2009 to 2010/2011. However, the loan loss provision of NSBL is also increasing for the first three years then it decreased in the year 2006/2007 , increased in the year 2007/2008 and is decreasing till last fiscal year 2010/2011.

Table: 4.22

Mean, S.D. and C.V. of Loan Loss Provision of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	982.85	242.78	24.70%
NSBL	510.24	104.37	20.46%

Source: Appendix 3

The above table shows that the mean, S.D. and C.V. of loan loss provision of HBL with 982.85, 242.78 and 24.70% respectively is higher than mean, S.D. and C.V. of NSBL with 510.24, 104.37 and 20.46% respectively.

4.1.3.7 Net Profit

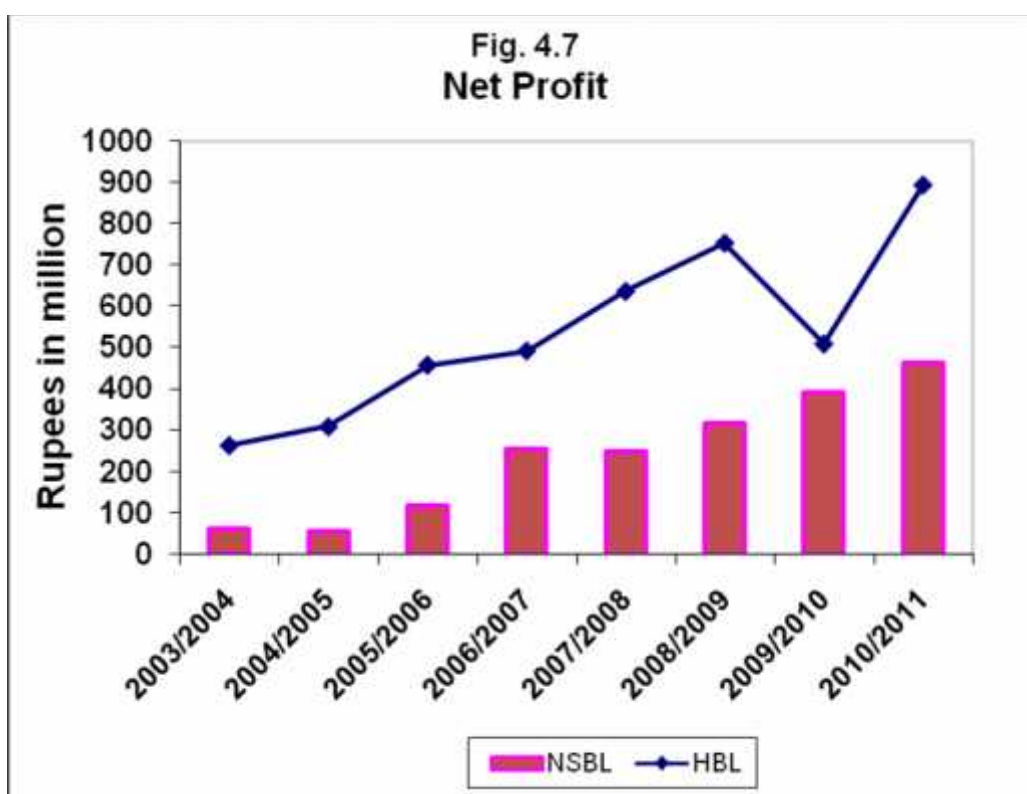
The volume of net profit measures the success of a firm in every aspect of its operation and strategy. A higher net profit is the sign of efficient management.

Table: 4.23

Net Profit of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
HBL	263.05	308.28	457.46	491.82	635.87	752.83	508.80	891.11
NSBL	60.85	57.39	117	254.91	247.77	316.37	391.74	464.56

Source: Appendix 6



The above figure shows the net profit of HBL is higher than NSBL bank. The net profit of HBL is in increasing till 2008/2009 however it decreased to 508.80 million in 2009/2010 but it increased by nearly 75% and reached Rs. 893.11 million in the fiscal year 2010/11. Furthermore, the net profit of NSBL is fluctuating till 2008/2009 however it is in increasing trend since 2008/2009 and reached Rs. 464.56 million in 2010/2011.

Table: 4.24

Mean, S.D. and C.V. of Net Profit of HBL and NSBL

Banks	Mean	S.D.	C.V.
HBL	538.9025	213.6979	39.65%
NSBL	238.82	151.24	63.33%

Source: Appendix 3

The above table shows that the mean net profit of HBL is higher with high S.D. and low degree of coefficient of variation which shows HBL is successful in making profit whereas the mean and S.D. of NSBL is lower but its C.V. is high.

4.1.4 Analyzing Lending efficiency and its Contribution towards Profitability

4.1.4.1 Total Interest Income to Total Income Ratio

This ratio measures the volume of interest income in total income. This ratio also helps to measure the bank performance on other fee-based activities. The high ratio indicates the high contribution made by lending and investing activities.

We have,

$$\text{Total Interest Income to Total Income Ratio} = \frac{\text{Total Interest Income}}{\text{Total Income}}$$

Table: 4.25

Total Interest Income to Total Income Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	1.2119	1.2067	1.1656	1.2711	1.2218	1.1759	1.4507	1.6622	1.2957
NSBL	1.3715	1.4190	1.5341	1.5586	1.5217	1.7571	2.0459	2.1797	1.6735
Combined Mean									1.4846

Source: Appendix 4

The above table explains that the total interest income to total income ratio of NSBL is higher than HBL from the period of 2003/04 to 2010/11. The overall mean ratio of these banks is 1.4846. NSBL had maintained its interest income position as HBL ratio had its up and down trend. The highest ratio of NSBL indicates its greater degree of

dependency on fund based lending and investing activities. However, HBL also have greater degree of dependency on fund basis activities.

4.1.4.2 Interest Expenses to Total Deposit Ratio

This ratio measures the cost of total deposits in a relative term. The performance of a commercial bank is dependent upon its ability to generate cheaper fund. Cheaper the fund, more the probability of generating loans and advances and vice versa. The high ratio is indication of costly fund and this adversely affects the lending activities of a bank.

We have,

$$\text{Interest Expenses to Total Deposit Ratio} = \frac{\text{Interest Expenses}}{\text{Total Deposit}}$$

Table: 4.26

Interest Expenses to Total Deposit Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.0223	0.0227	0.0245	0.0255	0.0259	0.0270	0.0413	0.0590	0.03102
NSBL	0.0355	0.0298	0.0304	0.0360	0.0332	0.0295	0.0414	0.0494	0.0356
Combined Mean									0.0333

Source: Appendix 4

The above table shows that both HBL and NSBL are successful in collecting cheaper fund by its modern and personalized services to the customer. The ratio of NSBL is higher than that of HBL from 2003/04 to 2009/10 but the ratio of HBL had increased in the last fiscal year. The ratios of HBL as well as NSBL are both fluctuating. The combined mean ratio of interest expenses to total deposit ratio is 0.0333.

4.1.4.3 Interest from Investment to Total Interest Ratio

This ratio measure the contribution made by interest investment in total interest income. The major portion of interest income is generated by the lending function and investment regarded as the cushion against liquidity risk. Hence, this ratio measures how efficiently the banks have employed their trend in investment.

We have,

$$\text{Interest from Investment to Total Interest Ratio} = \frac{\text{Interest from Investment}}{\text{Total Interest Income}}$$

Where,

Interest from Investment is the difference between total interest income and interest from loan and advances.

Table: 4.27

Interest from Investment to Total Interest Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.1367	0.1031	0.1059	0.1079	0.1025	0.1515	0.0686	0.8994	0.1083
NSBL	0.0784	0.0865	0.1290	0.1314	0.0960	0.0915	0.0925	0.1279	0.1042
Combined Mean									0.1062

Source: Appendix 4

The above table shows the interest from investment to total interest ratio of HBL and NSBL. The mean ratio of HBL and NSBL are 0.1083 and 0.1042 respectively. The mean ratio of HBL is higher than NSBL. The combined mean of these two banks is 0.1062.

4.1.4.4 Total Interest Income to Interest Expenses Ratio

The ratio of income to interest expenses ratio measures the gap between interest rates offered and interest rates charged, in average, should not be more than 5%. The difference in this ratio is mainly caused by the ratio of fund mobilized and fund collected. The credit creation power of commercial banks has highly impact on this ratio.

We have,

$$\text{Total Interest Income to Interest Expenses Ratio} = \frac{\text{Total Interest Income}}{\text{Interest Expense}}$$

Table: 4.28

Total Interest Income to Interest Expenses Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	2.5347	2.5740	2.5067	2.3137	2.3838	2.5056	2.0267	1.7915	2.3296
NSBL	1.9287	2.2380	2.1170	2.0160	2.1333	1.7709	1.5722	1.4809	1.9071
Combined Mean									2.1184

Source: Appendix 4

The above table shows the total interest income to interest expenses ratio HBL and NSBL. The mean ratio of HBL and NSBL are 2.3296 and 1.9071 respectively. The ratio of HBL has decreased to 1.7915 and NSBL to 1.4809 in 2010/2011. The combined mean ratio of these two banks is 2.1184. We can see that HBL has most consistent ratio than NSBL.

4.1.4.5 Total Income to Total Expenses Ratio

The assessment between the total income and total expenses measures the productivity of expenses in generating income. The amount of income that a unit of expenses generates is measured by the ratio of total income to total expenses. The high ratio is indication of higher productivity of expenses.

We have,

$$\text{Total Income to Total Expenses Ratio} = \frac{\text{Total Income}}{\text{Total Expenses}}$$

Table: 4.29

Total Income to Total Expenses Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	1.6923	1.7728	1.9299	2.0558	2.4412	2.1528	1.5342	1.6453	1.9031
NSBL	1.5186	1.2154	1.4601	1.9958	1.9959	2.1413	1.9428	1.6102	1.7350
Combined Mean									1.8190

Source: Appendix 4

The above table shows that total income to total expenses ratio of HBL and NSBL. The mean ratio of HBL and NSBL are 1.9031 and 1.7350 respectively. The ratio of

HBL was consistent and reached its peak in 2009/10 with the ratio of 2.1528 however it decreased in 2009/10 to 1.5342 and again slightly increased in the last fiscal year 2010/11 and reached 1.6453. Likewise, the ratio of NSBL was in increasing trend and had its peak in 2008/09 but it has been decreasing in last two fiscal years and reached to 1.6102. The combined mean of these two banks is 1.8190. However, the performance of these two banks is good and indicates higher productivity of expenses.

4.1.4.6 Total Income to Total Assets Ratio

This ratio measures how efficiently the asset of business is utilized to generate income. It also measures the quality of assets in income generation.

We have,

$$\text{Total Income to Total Assets Ratio} = \frac{\text{Total Income}}{\text{Total Assets}}$$

Table: 4.30

Total Income to Total Assets Ratio of HBL and NSBL

Bank	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.0415	0.0431	0.0474	0.0446	0.0444	0.0507	0.0508	0.0557	0.0469
NSBL	0.0426	0.0394	0.0354	0.0384	0.0371	0.0276	0.0292	0.0309	0.0351
Combined Mean									0.0410

Source: Appendix 4

The above table shows the total income to total assets ratio of HBL and NSBL. The mean ratio of HBL and NSBL are 0.0469 and 0.0351 respectively. The ratio of HBL has been more or less consistent till 2007/08, however, the ratio has been increasing from 2008/09 till the last fiscal year with the highest of 0.0557. More fluctuations can be observed in the ratio of NSBL with the highest of 0.0426 in 2003/04 and in 2010/11 it has reached to 0.0309. The combined mean ratio of these two banks is 0.0410. But, by analyzing the ratios of both the banks, we cannot find much role of assets in income generation.

4.1.4.7 Net Profit to Shareholder's Equity Ratio

The ratio between net profits to shareholder's equity is known as net profit to shareholder's equity ratio. This ratio measures the amount of profit that a rupee of shareholder's fund has received. A higher ratio is the sign of efficient management. Hence, higher percentage is preferable of the company and vice versa.

We have,

$$\text{Net Profit to Shareholder's Equity Ratio} = \frac{\text{Net Profit}}{\text{Shareholder's Equity}}$$

Where,

Shareholder's Equity = Share capital & share premium + Retained Earning + Reserves

Table: 4.31

Net Profit to Shareholder's Equity Ratio of HBL and NSBL

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	0.1987	0.2000	0.2590	0.2291	0.2530	0.2413	0.1479	0.2235	0.2191
NSBL	0.0971	0.0833	0.1191	0.2191	0.1751	0.1847	0.1599	0.1613	0.1500
Combined Mean									0.1845

Source: Appendix 4

The above table shows the net profit to shareholders equity ratio of HBL and NSBL. The mean ratio of HBL and NSBL are 0.2191 and 0.1500 respectively. The ratio of HBL dropped to 0.1479 in 2009/10 but it regained to 0.2235 in 2010/11. The ratio of NSBL is fluctuating throughout the period. The combined mean of these two banks is 0.1845. The mean ratio of HBL is higher than that of NSBL.

4.1.4.8 Earning per share (EPS)

The income of per common share is known as earning per share. The amount of EPS measures the efficiency of a firm in relative terms. An organization is able to use its resource to generate profit is due to EPS determines that market of a share. However, higher earning per share is preferable and vice versa.

We have,

$$\text{Earning Per Share} = \frac{\text{Net Profit}}{\text{No. of share outstanding}}$$

Table: 4.32

Earning Per Share (EPS) of HBL and NSBL

Banks	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	Mean
HBL	49.05	47.91	59.24	60.66	62.74	61.90	31.80	44.65	52.24
NSBL	14.26	13.29	18.27	39.35	28.33	36.18	23.69	24.85	24.77
Combined Mean									38.51

Source: Appendix 4

The above table shows the earning per share of HBL and NSBL. The mean EPS of HBL and NSBL are 52.24 and 24.77 respectively. The EPS of HBL was higher from 2006/07 to 2008/09, it fell to 31.80 in 2009/10 but increased to 44.65 in 2010/11. The EPS of NSBL is fluctuating throughout the period with minimum of 13.29 in 2004/05 and highest of 39.35 in 2006/07, in the last fiscal year it was 24.85. The mean EPS of HBL is nearly double than that of NSBL. The combined mean EPS is 38.51.

4.2 Analyzing Correlation between Different Variable

4.2.1 Correlation between Total Deposit and Loans and Advances

The correlation between total deposits and loans and advances describes the degree of relationship between two variables. How a unit increases in deposit impact the volume of loans and advances is measured by the correlation coefficient. Hence the deposit is the independent variables and loans and advances is the dependent variables.

Table: 4.33

Correlation Coefficient (r), between Total Deposit and Loans and Advances

Banks	Correlation (r)
HBL	0.98
NSBL	0.97

Source: Appendix 3

The above table describes the relationship between total deposit and loans and advances of two banks. There is a high degree of positive correlation between total deposit and loans and advances in HBL and NSBL with correlation of 0.98 and 0.97 respectively which indicates that both banks are successful to mobilize their deposits in proper way as loans and advances.

4.2.2 Correlation between Loans and Advances and Shareholder’s Equity

Correlation between loans and advances and shareholders equity describes the degree of impact of the increase in loan and advances to shareholders equity. The loans and advances are the independent variable and the shareholders equity is dependent variables.

Table: 4.34

Correlation Coefficient (r), between Loans and Advances and Shareholder’s Equity

Banks	Correlation (r)
HBL	0.99
NSBL	0.99

Source: Appendix 3

The above table explains that there is very high degree of positive correlation between shareholders equity and loans and advances in two banks. Both the banks have same degree of high degree of positive correlation.

4.2.3 Correlation between Investment and Loans and Advances

This correlation measures the degree of relationship between investment and loans & advances. This measure of correlation explains whether the banks have a rigid policy to maintain a consistent relationship between assets and factors such as seasonal opportunity, economic demand, NRB directives etc. has impact volume of these variables. Theoretically, increase or decrease in the volume of loans and advances directly reduces or increase the level of idle fund and this idleness of fund increase the investment.

Table: 4.35

Correlation Coefficient (r), between Investment and Loans and Advances

Banks	Correlation (r)
HBL	-0.56
NSBL	0.93

Source: Appendix 3

The above table explains that there is a correlation between investment and loans and advances of the both banks. We can observe moderate degree of negative correlation between Investment and Loans and Advances of HBL whereas there is high degree positive correlation between investment and loans and advances of NSBL. Though there is positive relationship between investment and loans and advances, this is not only a fact that increases in loans and advances in these banks necessarily increase the volume of investments.

4.2.4 Correlation between Provision for Loan Loss and Loans and Advances

This correlation between provision for loan loss and loans and advances measures the degree of relationship between these two variables. Loans and advances is an independent variable and provision for loan loss is a dependent variable.

Table: 4.36

Correlation Coefficient (r), between Provision for Loan Loss and Loans and Advances

Banks	Correlation (r)
HBL	0.40
NSBL	-0.38

Source: Appendix 3

The above table explains that there is moderate degree of positive correlation between Loan Loss Provision and Loans and advances of HBL, on the contrary, just the opposite correlation can be observed in case of NSBL.

4.3 Statistical Analysis on basis of Trend

Trend analysis and projection of next 5 years.

Under this topic, analysis of deposit, loans and advances, investment and net profit of HBL and NSBL is made. The forecast is made for next 5 years.

The forecast is based on the following assumptions.

1. The main assumption is that other things will remain unchanged.
2. The forecast will be true only when the limitation of least square method is carried out.
3. The bank will run in present position.
4. The economy will remain in the present stage.
5. Nepal Rastra Bank will not change its guidelines to commercial banks.

4.3.1 Trend Analysis of Total Deposit

Under this topic, the trend values of total deposit for seven years from the fiscal year 2003/2004 to 2010/2011 have been calculated and forecast for next 5 years from 2011/2012 to 2015/2016 is done.

The following table shows the trend values of total deposit for 13 years from 2003/2004 to 2015/2016 of HBL and NSBL.

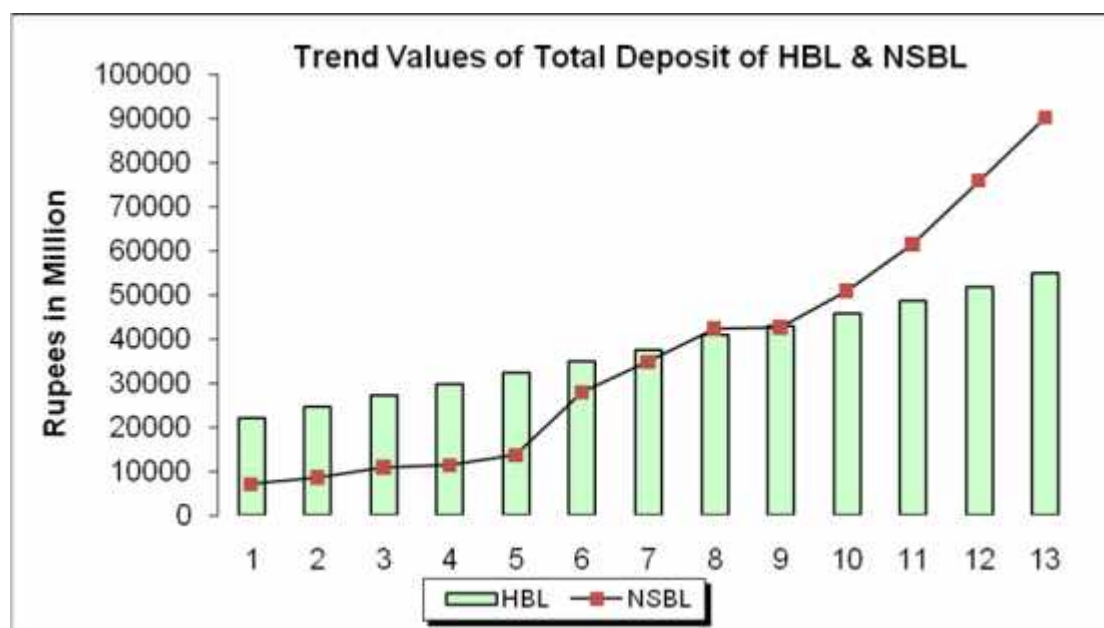
Table: 4.37

Trend values of total deposits of HBL and NSBL

Year	Trend values of HBL	Trend values of NSBL
2003/2004	21940.50	7198.32
2004/2005	24508.00	8654.77
2005/2006	27075.50	11002.04
2006/2007	29643.00	11445.28
2007/2008	32210.50	13715.40
2008/2009	34778.00	27957.22
2009/2010	37345.50	34896.42
2010/2011	40920.63	42415.44
2011/2012	42984.32	42742.60
2012/2013	45731.75	51009.28
2013/2014	48575.15	61547.46
2014/2015	51593.68	75958.76
2015/2016	54967.29	90221.68

Source: Appendix 6

Figure 4.8



We can observe from the above table that the deposits of HBL and NSBL of two banks have the increasing trend. There is no any decreasing trend in these deposits. From the above trend analysis, it is found that the deposit collection position of NSBL is the better in compare to HBL.

4.3.2 Trend value of total loans and advances of HBL and NSBL

Under this topic, the trend values of total loans and advances for eight years from the fiscal year 2003/2004 to 2010/2011 have been calculated and forecast for next 5 years from 2011/2012 to 2015/2016 is done.

The following table shows the trend values of total loans and advances for 13 years from 2003/2004 to 2015/2016 of HBL and NSBL.

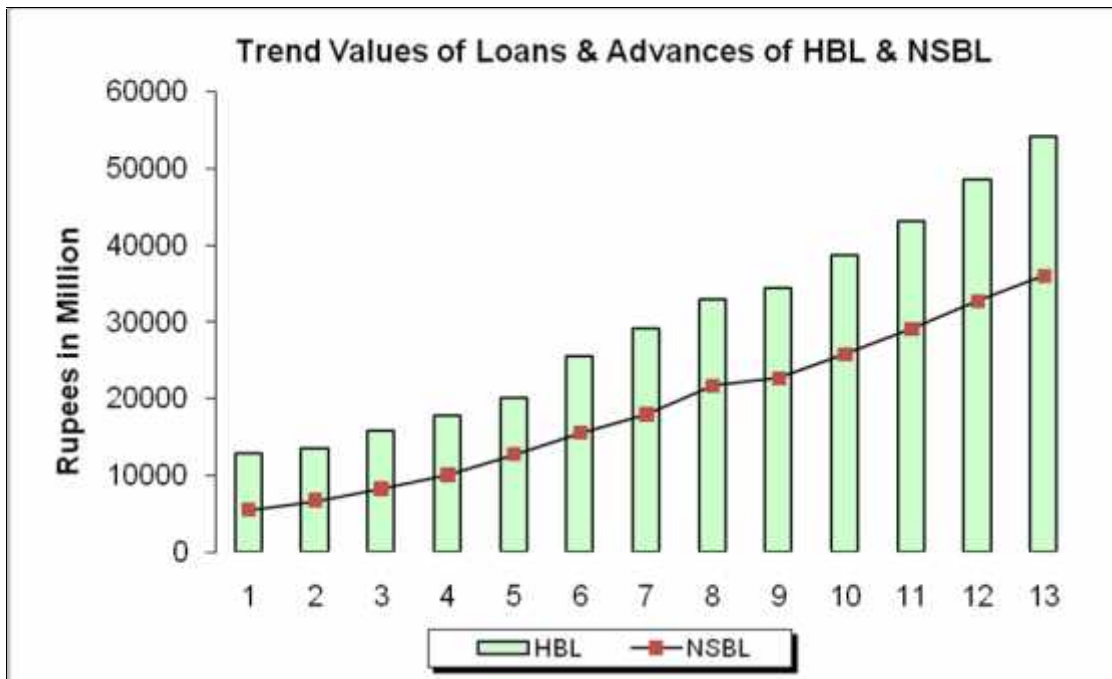
Table: 4.38

Trend values of total loans and advances of HBL and NSBL

Year	Trend values of HBL	Trend values of NSBL
2003/2004	12919.63	5531.83
2004/2005	13451.17	6739.35
2005/2006	15761.98	8241.46
2006/2007	17793.72	10065.10
2007/2008	20179.61	12746.22
2008/2009	25519.52	15612.05
2009/2010	29123.75	17963.64
2010/2011	32968.27	21718.79
2011/2012	34376.95	22732.11
2012/2013	38721.26	25785.52
2013/2014	43257.46	29154.48
2014/2015	48692.92	32736.04
2015/2016	54228.424	36035.22

Source: Appendix 6

Figure 4.9



The above table shows that the total loans and advances of HBL and NSBL have the increasing trend. There is no any decreasing trend in these total loans and advances. From the above trend analysis, it is found that the lending position of HBL is better in compare to NSBL.

4.3.3 Trend value of total investment of HBL and NSBL.

Under this topic, the trend values of total investment for eight years from the fiscal year 2003/2004 to 2010/2011 have been calculated and forecast for next 5 years from 2011/2012 to 2015/2016 is done.

The following table shows the trend values of total investment for 13 years from 2003/2004 to 2015/2016 of HBL and NSBL.

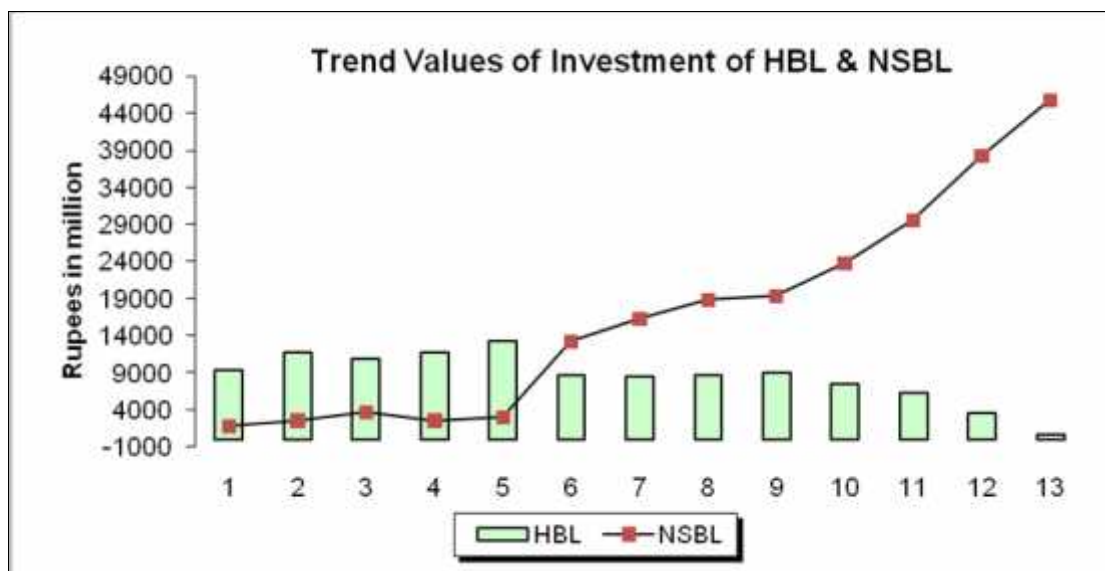
Table: 4.39

Trend values of total investment of HBL and NSBL

Year	Trend values of HBL	Trend values of NSBL
2003/2004	9292.10	1907.52
2004/2005	11692.34	2607.68
2005/2006	10889.03	3758.98
2006/2007	11822.99	2659.45
2007/2008	13340.18	3088.89
2008/2009	8710.69	13286.18
2009/2010	8444.91	16305.63
2010/2011	8769.94	18911.02
2011/2012	9035.80	19415.24
2012/2013	7530.06	23772.20
2013/2014	6344.61	29609.16
2014/2015	3616.92	38282.16
2015/2016	731.71	45713.73

Source: Appendix 6

Figure 4.10



The above table shows that the total investments of HBL is in decreasing trend whereas that of NSBL is in increasing trend. From the above analysis, it is found that the total investment of NSBL is better in compare to HBL.

4.3.4 Trend value of net profit of HBL and NSBL.

Under this topic, the trend values of net profit for seven years from the fiscal year 2003/2004 to 2009/2010 have been calculated and forecast for next 5 years from 2010/2011 to 2014/2015 is done.

The following table shows the trend values of total net profit for 13 years from 2003/2004 to 2015/2016 of HBL and NSBL.

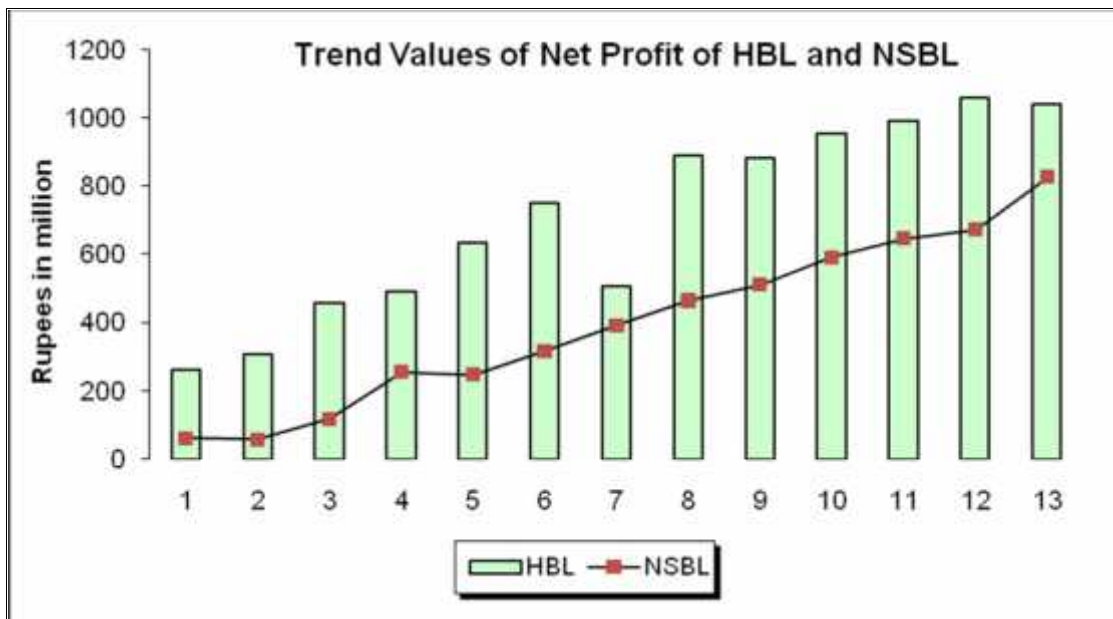
Table: 4.40

Trend values of net profit of HBL and NSBL

Year	Trend values of HBL	Trend values of NSBL
2003/2004	263.05	60.85
2004/2005	308.28	57.39
2005/2006	457.46	117.00
2006/2007	491.82	254.91
2007/2008	635.87	247.77
2008/2009	752.83	316.37
2009/2010	508.80	391.74
2010/2011	893.11	464.56
2011/2012	884.07	511.43
2012/2013	956.56	591.47
2013/2014	992.00	647.09
2014/2015	1061.79	673.03
2015/2016	1040.651	826.841

Source: Appendix 6

Figure 4.11



The above table shows that the net profits of HBL and NSBL all two banks have increasing trend. From the above analysis, it is found that the net profit of HBL is better in compare to NSBL.

4.4 Analysis of Primary data

In this section, the result of questionnaire which were distributed to six commercial banks are presented in broad way.

4.4.1 Respondent Profile

In the first part of questionnaire, respondent profile like Name, Sex, Age, Education level, Position and Experience was asked.

The results are shown in following Table.

Table: 4.41

		Age	
		Frequency	Percent
Valid	20-25	13	26.0
	25-30	28	56.0
	30-35	5	10.0
	35-40	2	4.0
	40-45	2	4.0
	Total	50	100.0

Table: 4.42
Education Level

		Frequency	Percent
Valid	Bachelor	10	20.0
	Masters(enrolling)	7	14.0
	Masters	31	62.0
	Others	2	4.0
	Total	50	100.0

Table: 4.43
Position

		Frequency	Percent
Valid	Assistant	23	46.0
	Officer	20	40.0
	Supervisor	3	6.0
	Manager	3	6.0
	Others	1	2.0
	Total	50	100.0

Altogether 70 questionnaires were distributed to six commercial banks out of which 50 responses were received. Among 50 respondents, the numbers of female and male are 27 and 23 respectively. Out of the total respondent, about 56% responses were received from the age group under 25-30. Low responses i.e. 4% were received from the age group under 35-40 and 40-45. In the case of education level, 62% of respondents were post graduate, 20% were graduate, and 4% were from CA background. The responses were received from assistant, officer, supervisor, manager and others i.e. auditors, out of which 46% responses were received from assistant and officer level, 6% responses were received from both supervisor & manager and only 2% were received from others.

4.4.2 Basic Information

In the next part of the questionnaire, basic information about the bank was asked to the respondents. The first question asked was,

1. Which are the factors that the bank considers for providing loans and advances? (Ranking from highest 1 to lowest 5.)

The result is shown in below table.

Table: 4.44

Average Score of the factor for providing loans and advance

	Average Score
a) Collateral	1.78
b) Business Status	2.48
c) Income Source	2.4
d) Sales / Profit	3.34

The average table shows that out of total respondent, majority of them considered collateral as a main factor for providing loans and advances since the average score of collateral is lowest than other factors whereas average score of sales/profit is highest so, it is considered as least factor for providing loans and advances.

The next questions was asked as,

2. Does the bank provide loan to small and medium enterprises?

100% responses have received that bank will provide loan to small and medium enterprise.

The next questions was asked as,

3. In which sector does the bank give more priority in order to provide loan? (Ranking from highest 1 to lowest 5.)

The result is shown in below table.

Table: 4.45

Average Score for providing loan in different sector

	Average Score
a) Agriculture	3.68
b) Industry	2.14
c) Commercial	1.3
d) Overdraft	2.88

The average table shows that out of total respondent, majority of them give priority to commercial sector in order to provide loan and they give least priority to agriculture

sector in order to provide loan as average score of agriculture sector is less than other sector.

The another questions was asked as,

4. Do you think that there is a relationship between,

- A. Total deposit and loan & advances?
- B. Loan and Advances and Shareholders' Equity?
- C. Investment and loan and advances?
- D. Provision for loan loss and loan and advance?

The result is shown in below table.

Table: 4.46

Relationship between TD and LA, LA and SE, Inv. and LA, Prov. for Loan Loss and LA

Ans.	TD and LA	LA and SE	Inv. and LA	Prov. for Loan Loss and LA
Yes (%)	98	82	72	92
No (%)	2	10	28	4
No idea (%)	-	8	-	4
Total (%)	100	100	100	100

Out of total respondents, 98%, 82%, 72% and 92% thought that there is relationship between TA and LA, LA & SE, Inv. and LA and Prov. for Loan Loss & LA respectively. 2%, 10%, 28% and 4% of the respondents thought that there is no relationship between TA and LA, LA and SE, Inv. and LA and Prov. for Loan Loss and LA respectively. Similarly, 8% of respondent have no idea that there is relationship between LA and SE.

The another questions was asked as,

5. Does the bank follows any rules/criteria to maintain liquidity position?

The result is shown in below table.

Table: 4.47
Responses of Question No. 5

	Frequency	Percent
Valid Yes	49	98.0
No idea	1	2.0
Total	50	100.0

Out of total respondents, 98% of the responses received that the bank follow rule / criteria to maintain liquidity position and only 2% of the respondent have no idea about whether the bank follows any rule to maintain liquidity position.

The other questions was asked as,

6. Which criteria / ratio do your bank considers most for maintaining / checking liquidity? (Ranking from highest 1 to lowest 5.)

The result is shown in below table.

Table: 4.48
Average Score of Liquidity Position

	Average Score
a) CRRatio	1.6
b) CR	2.98
c) QuickRatio	3.16
d) CBBtoTDRatio	2.34

The above table shows most of the respondent considers CRR for maintaining liquidity since average score of CRR is lower than other ratios and only few respondent considers Quick Ratio as a least ratio for maintaining liquidity.

The other questions was asked as,

7. Does the bank use any specific tool to forecast total deposit and other variables?

The result is shown in below table.

Table: 4.49
Responses of Question No. 7

		Frequency	Percent
Valid	Yes	42	84.0
	No idea	8	16.0
	Total	50	100.0

Out of the total respondents, 84% responses received that the bank use specific tool to forecast total deposit and other variables. Only 16% of respondent does not have idea about specific tool to forecast total deposit and other variables by the banks.

The another questions was asked as,

8. Which tool does your bank prefer?

The result is shown in below table.

Table: 4.50
Tools used to forecast Total Deposit and other variables

		Frequency	Percent
Valid	Trend Analysis	21	42.0
	Survey	7	14.0
	Constant Growth	4	8.0
	Management Policy	12	24.0
	Any other	6	12.0
	Total	50	100.0

The above table shows that about 42% of respondent have choose Trend Analysis in order to forecast total deposit and other variables. 24% have choose management policy and 14%, 8% and 12% have choose survey, constant growth and others to forecast total deposit and other variables.

The next questions was asked as,

9. Do the bank measures the efficiency of lending and its contribution in total profitability?

The result is shown in below table

Table: 4.51
Responses of Question No. 9

	Frequency	Percent
Valid Yes	50	100.0

100% responses received that the bank measures the efficiency of lending and its contribution in total profitability.

The another questions was asked as,

10. How does the bank measure the efficiency of lending? (Ranking from highest 1 to lowest 5.)

The result is shown in below table.

Table: 4.52
Average Score of measuring the efficiency of lending

	Average Score
a) By Comparing Ratio	1.62
b) By Comparing Profit	1.6
c) By Comparing Area	3.1
d) No. of customer	3.68

The above table shows that most of the respondent measure the efficiency of lending by comparing profit and least of them measure the efficiency of lending by considering number of customer.

The other questions was asked as,

11. Which ratio does your bank consider / emphasized?

The result is shown in below table.

Table: 4.53

Ratios of measuring the efficiency of lending

	Frequency	Percent
Valid ROA	13	26.0
ROE	9	18.0
EPS	17	34.0
Int. from Inv. to Tot. Int. Ratio	7	14.0
Any other	4	8.0
Total	50	100.0

Out of the total respondent, 34% of the respondents select EPS to measure the efficiency of lending. 26%, 18%,14% and 8% select ROA, ROE, Int. from Inv. to Tot. Int. Ratio and others respectively to measure the efficiency of lending.

And the last questions was asked as,

12. “The bank has specific set of rule / procedure for providing loan.”

The result is shown in below table.

Table: 4.54

Responses of Question No. 12

	Frequency	Percent
Valid Strongly Agree	42	84.0
Agree	8	16.0
Total	50	100.0

The above table shows that 82% of the respondents strongly agree and only 18% of them agree with above statement. No responses for undecided, disagree and strongly disagree were received of above statement.

4.5 Major findings of the study

The major findings of the study are as under

4.5.1 Liquidity Ratio

-) The mean current ratio of NSBL is higher than that of HBL. However, the combined mean 1.77 shows that NSBL has least consistent ratio.
-) The mean ratio of cash ratio of NSBL is higher than that of NSBL which indicates that the performance of NSBL is the better in this regard.
-) The SLR of NSBL is higher than that of HBL. Both of the banks have SLR above 15%.
-) NSBL seems to have better position maintaining the cash and bank balance to current ratio. It indicates NSBL's capacity of making quick payment of its deposit.
-) The mean ratio of investment on government securities to current asset ratio of HBL is higher than NSBL and combined mean. HBL has to invest its excess fund into other sectors, which generates more profit than the risk free securities. NSBL can invest more on government securities that should be up to the combined mean.

4.5.2 Findings from measurement of Lending Strength

-) The measurement of lending strength in relative term has revealed that the total asset to liabilities ratio of NSBL is bit lower. However, the performance of HBL has not deviated far from the combined mean. The high ratio is the result of high volume of shareholders equity in the liability mix.
-) The ratio of investment to loan and advances had measured the total portion of measurement in loan and advances. The ratio of HBL is higher than NSBL. The ratio of NSBL has indicated the low level of depending in investment activities.
-) The ratio of loan and advances to total deposits ratio has measured the portion of total deposit that is used to increase the income of banks irrespective of the portfolio of its application. NSBL has deployed the higher portion of its earning activities and this ratio of HBL. This is the indication that the fund mobilizing activities of NSBL significantly better than HBL. Performance in

loan and advances has not increase proportionately as compare to the deposit increment and it has further failed to utilized the excess fund in investing activities rather it has kept the high volume of fund at money at call and short notice.

-) The ratio of loan and advances to shareholders equity has gains the significant importance in measuring the capital fund and corresponding contribution in loan and advances. The mean ratio of NSBL is 8.5812, which is higher than HBL i.e. 8.5781. The low number of equity shares, retained earnings and the reserve of NSBL as compared to other bank and at the same time, contributing high volume of loan and advance resulted the ratio of NSBL so high as compared to other bank. HBL has generated low volume of loan and advances as compared to the volume of shareholders equity. This ratio concludes that HBL and NSBL have not been succeeding to advances high volume of credit as much as their capital funds grants to them.
-) The mean volume of total deposit, investment and loan and advances of HBL is higher than that of NSBL. HBL has the highest mean loan loss provision and that of NSBL has the lowest. The volume of net profit of HBL has the highest.

4.5.3 Findings from Lending Efficiency and its contribution towards Profitability

-) The Total Interest Income to Total Income of NSBL is higher than the mean ratio. Since there is high degree of deviation between the contributions of interest income to total income ratio, is resulted by high ratio of loan and advances to total assets.
-) The interest expenses to total deposit ratio indicate the cost of fund in NSBL is higher than HBL. NSBL has succeeded in collecting the fund in cheapest possible price.
-) The ratio of interest from investment to interest income measures the dependency in investing activities. HBL has higher interest from investment to interest income ratio than NSBL. This shows the direct impact of investment to total investment and loan & advances ratio.

-) Among the various measures of profitability ratios, the EPS reflects the relative measure of profitability. The EPS of HBL is significantly higher than that of NSBL which shows that the performance of HBL is better.
-) The ratio of net profit to shareholders equity ratio of HBL is higher. Low profit and highest amount of shareholder's equity in HBL have resulted low net profit to shareholder's equity ratio.
-) The total income to total asset ratio measures the earning power of each rupee invested by an organization irrespective of volume expenditure incurred. Here, the ratio of total income to total asset of HBL is higher than NSBL. The exclusion of high volume of expenditure in generating high volume of profit has caused this ratio to give the different result as measured by other profitability ratio.
-) The ratio of total income to total expenses reflects the earning capacity of rupee expenses. The ratio indicates that a rupee of expenses would result in value of ratio minus one (Ratio-1) in net profit. Thus, the higher the ratio, better the productivity of expenditure. The productivity expenses in HBL is better as its rupee expenses is able to contribute Rs. 1.9031 in net profit. The ratio of NSBL is least so the bank should reduce its expenditure for generating profit, otherwise the performance of this bank would adversely affect.

4.5.4 Findings from analyzing correlation between different variables.

-) There is high degree of positive correlation between the total deposit and loans and advances. The correlation of HBL and NSBL is 0.98 and 0.97 respectively. HBL is slightly better in generating loans and advances. This also shows that a unit of increment in deposit is more likely in HBL since the degree of correlation is higher.
-) There is moderate degree negative correlation between investment and loans and advances of HBL whereas positive correlation can be observed in that of NSBL. There is positive correlation between provision for loan loss and loan & advances of HBL; on the contrary, negative correlation in NSBL.

4.5.5 Findings from Trend Analysis

The trend analysis of HBL and NSBL reveals that,

-) The deposits of HBL and NSBL of two banks have the increasing trend. There is no any decreasing trend in these deposits.
-) The total loans and advances of HBL and NSBL have the increasing trend.. From the above trend analysis, it is found that the lending position of HBL is better in compare to NSBL.
-) The total investment of HBL is in decreasing trend whereas that of NSBL is in increasing trend. From the above analysis, it is found that the total investment of NSBL is better in compare to HBL.
-) The net profits of HBL and NSBL all two banks has the increasing trend. From the above analysis, it is found that the net profit of HBL is better in compare to NSBL.

4.5.6 Findings from Primary Data

-) Most of the respondents consider that the collateral is a main factor in order to provide loan and advances. Other prior factors being income source and business status. Whereas the respondents consider sales/ profit as a least factor.
-) On the view of respondents, the bank mostly provides loans to commercial sector, small and medium enterprises and gives least priority to agriculture sector.
-) There is also relationship between total deposit and loan & advance, loan & advances and shareholders equity, investment and loan & advance and provision for loan loss and loan & advances.
-) In order to maintain liquidity most of the responses received that the bank considers CRR as a main ratio and quick ratio as a least ratio.
-) Out of total respondents, about 42% of the respondent chooses trend analysis to forecast total deposit and other variables.
-) Most of the respondent measure the efficiency of lending by comparing profit and least of them measure the efficiency to lending by considering number of customer. And for this, EPS is considers to measure the efficiency of lending.

CHAPTER 5

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

A well developed banking system is a necessary precondition for the economic development of a country. Bank is a resource for the economic development, which maintains the self-confidence of various segments of society and extends credit to the people. So if there is an insufficiency and banking and finance facility, the growth of the economic development becomes slow. The main objectives of commercial banks are to mobilize idle resources in the particular productive uses after collecting them from scattered sources. They also provide capital for the development of industry, trade and business by investing the saving collected as deposits from public. In return they render various services to customers facilitating their economic and social life. The performance of a bank depends on the management of funds by investing in the most productive sectors with minimum loss of loan as far as possible. This very business yields sufficient gross income to bear necessary cost as well as to earn substantial profit.

Commercial banks are playing vital role in the economic development of Nepal. During the last two and half decades, the Nepalese Financial System has grown significantly. This study has been undertaken to analyze as well as to compare the credit management and portfolio behavior of two commercial banks i.e. HBL and NSBL in terms of various financial ratios such as liquidity position, lending strength portfolio behavior and other various indicative ratios along with their mean, standard deviation and coefficient of variation. The basic objective of this study is to analyze the critical status of credit management of the banks and to give some remedial measures thereto.

For the analysis of credit management of the commercial banks, the financial statement of the last seven years i.e. from 2003/2004 to 2009/2010 had been reviewed. Financial statements are sorted tabulated and interpreted by using

appropriate ratios. To achieve the objective of this study, descriptive and analytical research design and survey research design has been used.

The study has been organized into five chapters consisting of Introduction, Review of Literature, Research Methodology, Presentation and Analysis of Data and Summary, Conclusion and Recommendation.

5.2 Conclusions

The measurement of the liquidity has revealed that the liquidity positions of the banks are in satisfactory level. The current ratio of NSBL is higher and HBL is lower than the combined mean which shows that NSBL has least consistent ratio. Cash reserve ratio of NSBL is higher and HBL is lower and higher cash ratio is better for the cash position of a bank. The mean ratio of cash and bank balance to current ratio of NSBL is higher than combined mean. Statutory Liquid ratio of NSBL is higher than HBL but both have SLR above 15% which is required by NRB.

The mean ratio of investment on government securities to current asset ratio of HBL is higher than NSBL and combined mean. HBL has to invest its excess fund into other sectors, which generates more profit than the risk free securities. NSBL can invest more on government securities that should be up to the combined mean.

The measurement of lending strength in relative term has revealed that the total asset to liabilities of NSBL is the higher than HBL. However, the performance of HBL has not deviated far from the combined mean. The high ratio is the result of high volume of shareholders equity in the liability mix. This signifies overall increase of credit and overall development of banks performance. It is concluded that performance NSBL is better in this regard.

Loan and advances to total asset ratio of NSBL is higher. The investment to loan and advances ratio shows that HBL has higher ratio. This shows that HBL has utilized investment more in loan and advances than NSBL. The loan and advances to total deposit ratio of NSBL is higher which shows that NSBL has used total deposit to increase the income of banks irrespective of the portfolio of its application. It has deployed the highest portion its total deposits in its earning activities. This indicates

that the fund mobilizing activities of NSBL significantly better than HBL. The loan and advances to shareholders equity ratio of NSBL is higher than HBL. This ratio gains the significant importance in measuring the capital fund.

The mean volume of total deposit, investment and loan and advances of HBL is higher than that of NSBL. HBL has the highest mean loan loss provision and that of NSBL has the lowest. The volume of net profit of HBL has the highest.

The C.V. of NSBL is the higher than HBL in almost all of the cases except slight lower in Loan Loss provision. The mean volume of loan and advances of HBL is higher as high volume of well performing loan and advances in economy is symbol of healthy business. The mean volume of net profit of HBL is highest. It is concluded that HBL has the superior performance in its lending activities compare to NSBL. If HBL succeeded in collecting the less cheap sources of fund in future the lending strength of HBL would be better in coming future. The measurement of efficiency in lending has revealed that the mean ratio of interest income to total income ratio has concluded that the contribution of interest income in total income mix of NSBL is the greatest. The ratio of interest income and interest expenses of HBL is higher than NSBL. Among the various measures of profitability ratios, the EPS reflects the relative measures of profitability, performance of HBL are significantly better than NSBL. The total income to total asset ratio measures the earning power of each rupee employed of total income to total asset of HBL is higher. From the study, it is found out that HBL is able to borrow loan with lower interest rate and invest in high earning sector with the highest earned ratio.

There is higher degree of positive correlation between total deposit and loan and advances, loan and advances and shareholder's equity.

On the basis of primary data, most of the respondents consider that the collateral is a main factor in order to provide loan and advances. Other prior factors being income source and business status. Whereas the respondents consider sales/ profit as a least factor. On the view of respondents, the bank mostly provides loans to commercial sector, small and medium enterprises and gives least priority to agriculture sector. There is also relationship between total deposit and loan & advance, loan & advances and shareholders equity, investment and loan & advance and provision for loan loss

and loan & advances. In order to maintain liquidity most of the responses received that the bank considers CRR as a main ratio and quick ratio as a least ratio. Out of total respondents, about 42% of the respondent chooses trend analysis to forecast total deposit and other variables. Most of the respondent measure the efficiency of lending by comparing profit and least of them measure the efficiency to lending by considering number of customer. And for this, EPS is considers to measure the efficiency of lending.

5.3 Recommendations

On the basis of the study following suggestions can be made:

1. To maintain the sound liquidity position

The sound liquid position is a must for any financial institute for prevention of going through financial distress. The higher liquidity is not preferable as there would be more idle money so it is recommended to look upon new area of lending and investment.

2. To give extra priority on productivity and priority sector loan

NSBL's contribution in loan and advances is the lowest and this has low growth rate compare to HBL. Since the entire economy is largely dependent on the proper execution of lending functions by commercial banks. The low tendency toward lending affects the performance of all the banks in long run due to its paradox. Low level of lending constitutes the low level of investment resulting in low level of productive and employment generation and this cause slack of economy. This slackness in economy adversely effects the funding as well as non-funding activities of banking business. Thus NSBL is recommended to give extra priority on productivity and priority sector loan.

3. To improve their operational efficiency and increase the productivity of expenses

The productivity of the expenses in HBL is significantly higher than NSBL, thus these banks are highly recommended to improve their operational efficiency and increase the productivity of expenses made. Introducing sophisticated banking system, developing high motivational strength in management, increasing interest turnover are

some technique that improve the productivity of expenses and increased the gap of income and expenses.

4. To follow the directives of NRB

Following the normal guidance of NRB and acting upon this also reduce many of credit risk arising from borrower's defaulter, lack of proper credit, appraisal, defaulter by blacklisted borrowers and professional defaulter. The banks are recommended to follow the directive of NRB strictly and be more cautions and realistic while granting loans and advances. The major solution of reducing the risk is to avoid lending in more risky area until banks does not fully satisfy itself regarding the failure viability of the project.

5. To reduce the amount of non-performing loan and loan loss provision

The loan loss provision suggests that the banks have been maintaining a large amount as loan loss provisions. Such huge amount of loan loss provision is a burden for the bank, which increases the liability and reduces the operating profit of the banks. Thus, the bank should prioritize to reduce its non-performing loans into performing loans thereby reducing the amount of loan loss provision. HBL has highest loan loss provision comparing to NSBL so it is recommended that HBL have to improve the category of its loan and try to minimize the bad debts, which fall under non-performing loan.

6. To invest funds in more profitable sector:

NSBL should focus more on reducing the amount of non-performing loans and loan loss provision so that depositors and other stakeholders of the bank are safeguarded. Similarly, the bank must invest its fund in more profitable sectors but its investment and investment in government securities is higher comparing to HBL so the bank must live up to its liquidity and invest its funds in more profitable sectors.

7. To fulfill national and social objectives

The high volume of liquidity shows that the high degree of lending strength has been prevailing in all of these banks. The lack of reliable lending opportunities and fear of losing the principal in rural sector has been keeping these banks to less orient towards the lending function. Hence, the government should take appropriate action to initiate

these banks to attract to flow credit in this sector. But in view of risk element in lending the bankers still prefer to give a negative outlook in handling lending proposals. This attitude requires to be changed among the bankers and any proposal coming to them should be processed to banking norms to that it can be sanctioned for availment for production or approved social objectives.

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