

**IMPACT OF BANK SUPERVISION ON LENDING PRACTICES OF NEPALESE
COMMERCIAL BANKS**

A Dissertation submitted to the Office of the Dean, Faculty of Management in partial
fulfilment of the requirements for the Master's Degree

By

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Certification of Authorship

I hereby corroborate that I have researched and submitted the final draft of dissertation entitled “**Impact of Bank Supervision on Lending Practices of Nepalese Commercial Banks**”. The work of this dissertation has not been submitted previously for the purpose of conferral of any degrees nor it has been proposed and presented as part of requirements for any other academic purposes.

The assistance and cooperation that I have received during this research work has been acknowledged. In addition, I declare that all information sources and literature used are cited in the reference section of the dissertation.

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June, 2024

REPORT OF RESEARCH COMMITTEE

Ms. Tilottama Gyawali has defended research proposal entitled '**Impact of Bank Supervision on Lending Practices of Nepalese Commercial Banks**' successfully. The research committee has registered the dissertation for further progress. It is recommended to carry out the work as per suggestions and guidance of supervisor Dr. Pitri Raj Adhikari and submit the dissertation for evaluation and viva voce examination.

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APPROVAL SHEET

We, the undersigned, have examined the dissertation entitled '**Impact of Bank Supervision on Lending Practices of Nepalese Commercial Banks**' presented by Tilottama Gyawali a candidate for the degree of Master of Business Studies (MBS Semester) and conducted the Viva voce examination of the candidate. We hereby certify that the dissertation is worthy of acceptance.

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List of Abbreviations

BFI	Bank and Financial Institutions
CAR	Capital Adequacy Ratio
CD Ratio	Credit Deposit Ratio
CIB	Credit Information Bureau
CIR	Cost Income Ratio
CV	Coefficient of Variation
DI	Deposit Insurance
DMB	Deposit Money Banks
ETA	Equity to total assets
FY	Fiscal Year
GBIME	Global IME Bank Limited
GDP	Gross Domestic Product Growth
INF	Annual Inflation Rate
KYC	Know Your Customer
LC	Letter of Credit
LLP	Loan Loss Provision
MENA	Middle East and North Africa
MIS	Management Information System
Nabil	Nabil Bank Limited
NBL	Nepal Bank Limited
NBU	National Bank of Ukraine
NEPSE	Nepal Security Exchange Ltd.
NIM	Net Interest Margin
NLTA	Net loan to total assets
No. I	Number of Inspection
NPL	Non-Performing Loan
NRB	Nepal Rastra Bank
p	probability
PCSE	Panels Corrected Standard Errors
RBB	Rastriya Banijya Bank Limited
RBI	Reserve Bank of India
ROA	Return on Assets
ROAA	Return on Average Assets
ROE	Return on Equity
SD	Standard Deviation
SEBO	Security Exchange Board
SR Letter	Supervision and Regulation Letters

Abstracts

This study investigates the impact of regulatory supervision on the credit practices of commercial banks in Nepal, focusing specifically on loans, advances and provisions for loan losses. Using a detailed analysis of three important banks: Rastriya Banijya Bank (RBB), Nabil Bank and Global IME Bank (GBIME), the study examines key performance indicators, including total loans and advances, loan loss provision ratios, non performing loan, return on assets (ROA), return on capital (ROE) and inspection frequency of Nepal Rastra Bank (NRB). The research employs a conceptual model to explore the relationship between regulatory oversight and banking performance. The independent variables, ROA, ROE, are analyzed against the dependent variables that include return on loans and advances, credit deposit ratio, loan loss provision, non-performing loan ratio, number of NRB inspection. The findings reveal that the regulatory supervision, in particular the inspections of the NRB, significantly influences the lending practices of the commercial banks. These inspections help manage bad loans and guarantee adequate provisions for credit losses, thus mitigating credit risk and improving profitability. The study concludes that there is a positive correlation between the supervision of the NRB and the financial health of the banks. The directives and regulatory policies issued by the NRB play a crucial role in shaping the credit strategies of commercial banks, ensuring that they comply with their social responsibilities and at the same time maintain profitability and liquidity. The implications of these findings suggest that the bank administration must prioritize the rigorous evaluation of the financial status of borrowers and their capacity to pay to minimize bad loans and safeguard the financial stability of the bank. The study underlines the importance of effective regulatory supervision to maintain the solidity of the banking sector and suggests that continuous monitoring and adaptable policy frameworks are essential to sustain banking performance in the long term.

Keywords: bank supervision, loan and advances, ROA, ROE, Number of Inspection, Return on Loan and Advances, Non-performing loan, Loan loss provision

Chapter I

Introduction

1.1 Background of the study

Bank supervision plays an important role in the banking sector of any country. Tong Zenyin (1991) mentions that supervising and regulating the operation of financial institutions are the important functions of the central bank. He also mentions that only when the supervision and regulation are duly performed can the financial sector play its role fully in macroeconomic regulation and control. A supportive environment is necessary for the financial systems to flourish (Phina et al., 2021). The international and national economic systems both depend on banking; therefore, to ensure the balance and effectiveness of the banking system, bank regulation and supervision are essential tools (Özker, 2020).

There is need of supervision for various reasons. Bank supervision leads to better performance (Boubacar, 2023). Supervision ensures the stability of the financial system by monitoring banks to prevent risks like fraud, mismanagement, and insolvency. It safeguards depositors' funds and maintains public confidence in the banking sector, protecting consumers from potential losses. Supervision promotes compliance with regulatory requirements such as capital adequacy ratios, liquidity standards, and anti-money laundering measures. Supervision fosters a transparent banking environment by ensuring that banks adhere to ethical practices and disclose relevant information to stakeholders. To manage Emerging Risks in a rapidly evolving financial landscape, supervision helps address emerging risks and ensures that banks adapt to changing market dynamics effectively. With globalization, supervision becomes crucial for ensuring that banks comply with international standards and regulations, facilitating participation in global financial markets. The supervision of the central bank mainly concentrates on monetary policy, the quality of regulatory personnel, macro prudential function and credit management (Tingen et. All, 2020). Supervision encourages banks to adopt technological advancements responsibly, enhancing efficiency and customer service while mitigating associated

risks. Overall, bank supervision serves as a cornerstone for promoting financial stability, protecting consumers, and supporting sustainable economic growth in Nepal.

Banks are the largest financial institutions around the world, with branches and subsidiaries throughout the world. The banking sector is a major player in the financial growth through the financial services they offer to public. Through the provision of financial services, bank ensures monetary and societal permanence and maintainable development of economy hence loan and advance is an important role of bank. Loan and advance means any financial assets of a bank arising from a direct or indirect advance or commitment to advance funds by a bank to a person. Loans is that have been made or bought and are being held for repayment. Loan and advances constitute the major assets of banks, thrifts and other lending institutions. Credit portfolio management is a key function for banks (and other financial institutions, including insurers and institutional investors) with large, multifaceted portfolios of credit, often including illiquid loans (Nario et. all, 2016). The value of loan portfolio depends not only on the interest rates earned on the loans but also on the quality or likelihood that interest and principle will be repaid. Loan portfolio managers have need to credit management guidelines in place and only buy loans return to borrowers who made those guidelines. On commercial loans, borrowers usually have to requalify for the loan every year and if reduced revenues mean that a company no longer meets the portfolio credit standards, then the lender or portfolio controller can call in the loan, which means the borrower has to repay the debt. However, the lenders and loan portfolio cannot call in personal loan.

Commercial bank generates profit by lending the amount in periods. Loan or credit and in return it gets interest. Banks loans are classified as; loans and advance, overdrafts, cash credit, discounting of bills and so on. But beside this, the other forms of credit are bills of exchange, bank overdrafts, promissory note, letter of credit (LC), traveler cheque, treasury bills (Pandey,2011).

A bank's lending behavior generally depends on the type of bank, capital base, deposit base, deposit density, interest rate, exchange rate, inflation, gross domestic product, investment portfolio, liquidity, monetary and fiscal developments, credit regulations issued from time to time by the regulatory authority and internal policies of banks, as

well as other non-economic factors. Supply side and demand side factors determine the lending behavior of the bank. This study focuses on the supply factors. In order for banks to balance their core objectives of liquidity, profitability and solvency, credit must be handled efficiently. As credit constitutes a major part of bank's assets, the study of the determinants of lending behavior becomes necessary as the commercial banks in Nepal need to understand how to manage these huge assets in terms of their loans and advances (Timsina, 2017).

Loan and Advance affects the profitability and liquidity of the company, which means it has a direct impact on the financial performance of the banks. Financial performance is the picture of the organization that shows how the organization is making profits. Profit is one of the basic indicators of good financial performance. Financial performance shows the financial strength and weakness of companies. The balance sheet and profit and loss statement show the financial performance of an organization. Analysis of these financial statements helps measure the overall financial performance of the organization. Financial performance analysis helps to establish a strategic relationship between the two items of the balance sheet and the income statement and other operational data to reveal the meaning and importance of these items. Thus, financial performance analysis is required to take managerial and financial decision (Bist, 2004).

The main focus of the study is to define the supervisory/regulatory guidelines which mainly consists of the directives issued by Nepal Rastra Bank (NRB) and analyze the impact of the such directives on the selected Commercial Banks. NRB issues following categories of directives among many others as regulatory guidelines to commercial banks. Directives relating to loan classification and loan loss provision, directives relating to banking regulations and prudential norms, directive(s) relating to single borrower and limitation of the sectoral credit and facilities, directive(s) relating to credit information and blacklisting and directive(s) relating to the list and format of different forms. The bank supervision is based on the directives issued by NRB. The lending practices of commercial banks are impacted by the directives issued by the central bank. Therefore, this study examines the supervision of lending practices of commercial banks by NRB through its directives.

1.2 Problem statement

Nepal's financial sector is an important component of its economic landscape and contributes significantly to economic growth and development. The role played by the NRB in the supervision and regulation of banks and financial institutions is key to stability and confidence in this sector. As the financial landscape evolves, it becomes imperative to critically assess the impact of NRB supervision on these entities. (NRB, 2023)

The financial performance of bank basically depends on its own activities (internal factors) and the overall performance of the economy (external factors) (Shrestha, 2020). The deposit collection and the net profit earned by Nepalese banks have also increased along with the increment in loan disbursed amount. It is palpable that the interest income on loan disbursed is the main source of income for the bank (NRB, 2022). However, granting loan is not an easy task. Ineffective loan management could jeopardize the existence of the bank and ineffective loan management has been main reason of failure of renowned banks of Europe and America. Lending is the main component of any bank's business. It is a tricky area-subject to losses due to economic downturns, portfolio mismanagement, loan officer judgment errors, and regulatory difficulties due to compliance errors. And, with different people managing different areas in different ways, oversight becomes a real problem. It is easy to lose control and end up with problems where there shouldn't be any problem. It is absolutely necessary to manage loans effectively and efficiently, while minimizing charge-offs. It is very challenging task on the part of bank because the bank has to disburse loan in the appropriate sector and recover it in time as well. It is very difficult to choose right and productive sectors for granting loan. Hence, there is the chance in flowing bank's deposit in unproductive sector. To ensure banks profitability and existence there must be proper management of loans and advances (Swami, 2014). Loan affects overall development of the country. The loans which are obtained from commercial banks are directly related to the development of the country. Hence, for developing country like Nepal, the problem of lending has become very serious. This is due to lack of sound policy of commercial banks (Pandey, 2010).

Commercial banks collect deposits from the public and utilize the largest portion of the deposited money for disbursing loans and advances. The balance sheets of the

commercial banks show that deposits constitute a major portion of the liabilities side and loans and advances constitute a major portion of the assets side. With the increase in competitive environment, it becomes difficult to choose right and productive sector for providing loan and advances. Hence, there is the chance of flowing bank's deposit in unproductive sectors. Unsecured loan and investment to unproductive sectors increases the risk of bank collapse. Providing loan to industries and production sectors are very risky projects. Banks are switching over from project financing to consumer financing such as housing loan, education loan, vehicle loan, professional loan, personal loan. Consumer financing may result in high profit for bank but quantitatively these loans are disbursed in low amount. So, the bank should not largely depend upon the consumer financing (Shankar, 2019).

No doubt, the commercial banks of Nepal are committed for economic and industrial development of the country. But these banks do not have successful results and operations. Due to tough competition, favoritism in loan disbursement and lack of peace and political instability, these banks are facing problems on loan investment and recovery patterns due to lack of supervision the loan granted by these banks for one purpose is used for another. Similarly, the lending procedures are cumbersome and lengthy. The terms, conditions and languages are unfamiliar to the general people. Hence, most of the major banking problems have been caused by weakness in loan management. Some studies believe that banking regulations improve banking efficiency, whereas others disagree (Boubacar, 2023). To ensure effective management of loan in commercial banks NRB need to play its role as a supervisor from time to time.

To make study more specific as well proper guide line, the study tries to answer the following research questions as below;

- i. Is there any relationship between lending practices (return on loan and advances, credit deposit ratio, non-performing ratio, loan loss provision ratio) and profitability (return on assets, return on equity) of commercial bank?
- ii. What is the effect of supervision on lending practices and profitability of the commercial bank?

1.3 Objectives of the study

The general objective of the study is to understand and analyze the impact of NRB supervision on the lending practices of commercial banks of Nepal. The specific objectives are:

- i. To examine the relationship between bank profitability (ROA, ROE) and lending practices (return on loan and advance, non-performing loan ratio, credit deposit ratio, loan loss provision).
- ii. To assess the effect of supervision on lending practices and profitability of commercial bank.

1.4 Rationale of the study

This research is driven by the need to comprehend the intricate relationship between NRB supervision and the performance of banks and financial institutions in Nepal. The study is focused to uncover critical insights into the effectiveness of regulatory measures, the adaptability of financial institutions, and the overall impact on the stability and growth of Nepal's financial sector. By understanding these dynamics, the study seeks to contribute to informed policymaking and the continual improvement of regulatory practices.

The stability and efficiency of the banking sector is critical to the overall health of the economy. As financial intermediaries, commercial banks play a vital role in channeling funds from savers to borrowers, facilitating economic growth and development. However, this central role also makes them susceptible to risks that can have widespread economic consequences. Therefore, banking supervision is essential to ensure the soundness and reliability of commercial banks. This study aims to explore the relationship between banking supervision and the lending practices of commercial banks, highlighting how regulatory supervision influences lending behavior, risk management, and overall financial stability.

1.5 Limitations of the study

The central bank of Nepal, Nepal Rastra Bank (NRB) issues directives as the major tool to supervise and monitor the financial institutions. The directives are revised considering the need of time as well as considering other factors which will affect the

economy of the country. The regular supervision of NRB based on these directives also helps to understand whether any changes in policy level are required or not. These directives which have the potential to change the financial scenario of the country are even more important in that they should be strictly monitored.

Due to the impact of NRB supervision on commercial banks being vague and vast, this study focuses only on the impact of supervision on lending practices of commercial banks. The limitations of this study are as follows:

- i. The study is limited to only three commercial banks of Nepal, namely; Rastriya Banijya Bank Limited, Nabil Bank Limited and Global IME Bank Limited.
- ii. The study deals with certain financial tools such as ratio analysis and statistical tools only.
- iii. Only secondary data is used for analysis which are taken from annual report of respective banks, journals and articles, NRB directives etc.
- iv. The whole study is limited to the past ten years (From FY 2070/71 to 2079/80) period.
- v. Since the selected directive more or less give a good picture of the lending practices of commercial bank, this study does not consider other relevant directives and areas. So, the actual outcome of the research may be biased to some degree.

Chapter II

Literature Review

This chapter mainly reviews the available literature with regards to supervision of central banks, their impact of policies and impact of such policies in commercial banks. In this chapter review the various logical terms pertinent to the area are reviewed and presented, similarly a brief presentation of the related studies and findings as well as review of the various articles programs which are relevant to this research studies, has been made in this chapter.

2.1 Theoretical review

Various theories relating to loan management of commercial banks:

Commercial loan theory

The oldest banking theory is the commercial lending theory, also called The doctrine of real bills. Commercial lending theory holds that banks should only lend on short-term, self-liquidating commercial paper. According to Hosna and Manzura (2009), the commercial loan theory is aimed at persuasively influencing both bank loans and the general economic activities. Strict adoption of this theory will reveal that it is expected to serve as a money supply for changes in the aggregate economic activity. The popularity of this doctrine among deposit money banks (DMB) in Nigeria is evident. Nigerian bankers believed that since their resources were repayable within a short period, the money of said depositors must be used accordingly in short-term loans.

The shiftability theory

This theory believes that assets need not be tied on only self-liquidating bills, but also held in other shiftable open-market assets, such as government securities (Moti, Masinde and Mugenda, 2012). The shiftability theory did not replace the commercial loan theory or made it to be invalid which is a point to be noted. Instead, the shiftability theory focused on a more general view of the banking business by broadening the list of assets considered legitimate for bank ownership. The shiftability theory does not deem commercial loan as inappropriate bank assets, rather it does say that commercial loans are not the only appropriate asset. The essence of the shift theory is that a bank's liquidity depends on its ability to transfer its assets to someone

else at a predictable price. Hence, for example, it would be perfectly acceptable for a bank to hold short-term open market investments in its asset portfolio.

The credit risk theory

Credit risk according to Salas and Saurina (2002) refers to the risk that a borrower will default on any type of debt without making required payments. The risk primarily relates to the lender and includes the loss of principal and interest. Disruptive losses can be total or partial and can occur in a number of circumstances, such as when an insolvent bank is unable to return funds to a depositor. To reduce the lenders risk, the lender may conduct a credit check on the potential borrower, also may require the borrower to take appropriate insurance, such as mortgage insurance or request collateral or third-party guarantees. In general, higher the risk gets higher will be the interest rate that the debtors will be required to pay on the debt (Owojori, Akintoye, & Adidu, 2011).

The liability management

Theory This theory assesses that it is unnecessary to observe conservative standards since reserve money can be borrowed or obtained in the money market using short term debt instruments whenever a bank experiences reserve deficiency. According to Shafiq and Nasr (2010) it does not refer that the bank manages only its liabilities and passive income with respect to its assets. Rather, the theory continues to believe that the asset structure of the bank has a important role to play in providing the bank with enough liquidity. But the theory takes a one dimensional approach to liquidity and states that the bank can also use its liabilities for the purpose of liquidity. The bank needs liquidity for the purpose of withdrawing deposits as well as to meet the reasonable credit requests of its customers. Not only are bank loans profitable but a bank that would not or cannot make loans to its depositors when they require funds is not likely to keep those depositors for very long period.

Principles of lending loan and advances

The precautions to be taken by a banker, and the principles to be taken care of, while granting advances. By way of introduction, an attempt is being made in the following paragraphs to discuss the general principle to be in mind by a banker while granting loans and advances (K.C., 2010).

i. Liquidity

The term 'liquidity' refers to the ability to generate cash on demand. A bank generally utilizes its deposits with the aim of granting loan and advances. These deposits are refundable on demand or on the expiry of a specified period. In either case, the banker should be ready to meet these obligations whenever required. The advances granted by the banker are as liquid as possible.

ii. Profitability

Banks are essentially commercial ventures. It is true that excessive and unjustifiable profits can only be at the cost of the customers, in so far higher lending rates push up production costs, and in the ultimate analysis, adversely affects society in general. At the same time, the facts remain that while strong operation profits allow for full prudential provisioning high net profits allow for allocation to capital and reserves, which is essential for any bank to maintain its competitive viability and expand its lending operations. Also, the shareholders of banks are entitled to reasonable dividend. All this indicates that it is that their lending operations are sufficiently profitable.

iii. Safety and security

The banker should ensure that the borrower has the ability and will to repay Advances as per agreement. Margin of Safety should be carefully considered by the banker. If it is as unsecured advance, its repayment depends on the creditworthiness of the borrower, and that of guarantor. The banker should consider the Charter, Capacity and Capital or reliability, Responsibility and resources of the borrower and the guarantor.

iv. Purposes

The banker has to carefully examine applied. Of course the exact purpose the purpose for which the advance has been for which the advance is actually utilized. There is always the possibility that the advances, once granted, may be diverted for purpose so that indicated by the borrower at the time application. Hence, proper analysis of purpose needs to be done.

v. **Social responsibility**

While admitting that bankers are essentially commercial ventures, a bank should not forget the fact that it is not enough that only people of means are given banks finance. The identification of property sectors for the purpose of extending bank credit should be considered as a positive development in the banking system, aimed at effectively discharging its responsibility towards society. Along with the social responsibility, banks should pay enough attention to the qualitative aspects of lending. Social responsibility is, no doubt, highly exacting.

Loan or credit concept

A specified amount sanctioned by a bank to the customer for certain purpose is called a 'loan' or 'credit'. Loan is generally granted for a fixed period for example three months, six months or a year. Loan and advance administration involves the creation and management of risk assets. The process of lending takes into consideration about the people and system required for the evaluation and approval of loan request, negotiation of terms, documentation, disbursement, administration of outstanding loans and workouts, knowledge of the process and awareness of its strength and weakness and important in setting objectives and goals for lending activities and for allocating available funds to various lending functions such as commercial, installment and mortgage portfolios (Johnson, 1994).

Credit is the amount of money lent by the creditor (bank) to the borrower (customers) either on the basis of security or without security. Sum of money lent by bank is the credit (Oxford Advanced learners Dictionary, 1992).

Loan and advances is an important item on the asset part of the balance sheet of a commercial bank. Bank earns interest on loans and advances, which is one of the major source of income for banks. Bank prepare credit portfolio, otherwise it will not only add bad debts but also affect profitability adversely (Varshney and Swaroop, 1994).

Loan management objectives

Loan objectives establish specific, measurable goals for the bank. The board of directors must ensure that loans are made with the following three basic objectives in mind: (Crosse, 2004)

- To grant loans on a sound and collectible basis.
- To invest the bank's funds profitably for the benefit of shareholders and the protection of depositors.
- To serve the legitimate credit needs of their communities.

Types of loan or credit

1. Overdraft

An instant extension of credit from a lending institution is more precisely a draft for more than the balance in the account on which the draft is drawn. A bank may accept an overdraft, depending on the significance of the customer and on prior arrangements (if there are any) to cover the overdrafts.

2. Cash credit

Cash Credit refers to a short-term cash loan provided to a company. This type of funding is provided by the bank only after obtaining required and adequate security to secure the loan. Once the security for repayment has been obtained by the bank, the business that receives the loan are able to continuously draw from the bank up to a certain specified amount. This type of financing is similar to a line of credit (Chhabra, and Taneja, 1991).

3. Direct credit

i) Term credit

Term credit is medium and long term credits which are given for purchase of assets, like land, building, machinery and equipment. The amounts of term credits are fixed primarily in relation to the total costs of the projects.

ii) Working capital credit

A credit is whose purpose is to finance everyday operations of a company.

iii) Priority or deprived sector credit

With a aim to give freedom to commercial banks during the selection of their loan portfolio, the NRB has taken a decision to gradually phase out the priority sector-lending program.

iv) Hire purchase financing (Installment credit)

Hire purchase credits are characterized by periodic repayment of Principal and interest over the maturity of credit.

v) Housing credit (Real estate credit)

Commercial banks also extend housing credit to their customers who have regular income or can earn revenue from housing project itself.

vi) Project credit

Project viability is considered while granting project credit by the bank. The debtors need to invest certain proportion to the project from their equity and the remaining portion will be financed as project credit by the bank.

vii) Consortium Credit

Consortium credit refers to the credit facility granted by two or more institutions in collaboration. It reduces the risk of project among them.

viii) Credit cards and revolving lines of credit

Banks are increasingly utilizing charge cards and revolving lines of credit to make unsecured consumer credit. Revolving lines credit lowers the cost of making credit since operating and processing cost are reduced.

Charge cards and credit lines tied to demand deposit accounts are the most common revolving credit agreements. It can be further divided into credit cards, automatic overdrafts lines and large credit lines.

ix) Bank guarantee

It is used for the sake of the customers in favor of the other party (beneficiary) up to the approval limit. Generally, a certain percent amount is taken as margin from the customer and the customer's margin account is credited.

x) Letter of credit (L/C)

LC are a means by which non-payment risk in the use of commercial draft may be further reduced by substituting the credit worthiness of a bank for that of the purchaser when, because of the excessive credit risk factors both in the buyer and in

his environment, the buyer bank will for a fee, guarantee payment in the form of LC (Chhabra, and Taneja, 1991).

4. Discounting of bills

It is the main function of commercial banks. Discounting of bill means made payment of bill, which are issued by commercial banks as well as central banks, NRB, before their expiration date or matured time. Therefore, payment should be less than the total amount because of their uncertainty (Chhabra, and Taneja, 1991).

Lending criteria or criteria of creditworthiness

1. Character

Those inherent qualities and activities of debtor that prompt him to pay his debts; that sentiment of obligation to fulfill the promise of payment; sometimes generalized as willingness to pay. Generally, the following documents are reviewed while considering character:

- Memorandum and Articles of Association
- Registration certification
- Tax registration certificate with latest renewal
- Resolution to borrow
- Authorization-person authorizing to deal with the bank
- Information about other creditors who have referred the applicant, or a statement from the customer's bank account.

2. Capacity

Those means and faculties which provide the funds with which payment is made; resources possessed or incoming; the “ability to pay” even well-founded credit approval may subsequently be reserved by change in the debtor’s ability to fulfill his credit promise. Changes in his employment, earning capacity or indebtedness militate against the integrity of his promise and produce an unexpected specific risk.

3. Capital

Those possessions or equities from which payment might be expected when character and capacity become lacking; that from which payment may be taken under duress, if necessary.

Capital, as viewed in the appraisal of creditworthiness, represents a residual or cushion of equities available for the payment of debt if other means of payment fail.

4. Collateral

Special forms of capital which are usually negotiable or readily represented by conveyance of claim or title; specific security offered for credibility of the credit promise. The banks commonly look to collateral in their transactions, taking securities, negotiable instruments, post-dated checks, and chattel and real estate mortgages as pledges.

5. Conditions

Those circumstances external and usually beyond the control of debtors which nevertheless affect their paying behavior.

6. Country

Those conditions of foreign and international character, reflecting cultural and political circumstances, which may further qualify creditworthiness as determined by other factors.

Steps involved in lending

Before issuing of loan commercial banks follow up certain procedures for providing loans. In spite of several technical aids, such as ratio analysis of financial statements, cash flow statements available to the modern banker, the ability to make a correct loan decision very much depends on the shrewd and critical judgment, common sense, perceptive intelligence and discriminating sense of the lending banker. However the usual steps involved in lending are as follow:

1. Loan application

When a customer needs loan they ask for loan procedure in the bank according to the type of loan which may be a corporate loan or a retail loan. A loan application or a

proposal is made if the customer finds all the process and information is reasonable. For corporate loan, it becomes necessary to consult loan officer. Loan officer can also contact to big account holder possessing business organization and ask if they are in need of loan.

2. Initial interview with the customer ascertaining the following few criteria

- The character, capacity and integrity of the borrower.
- Prospects of proposal- success or failure.
- Repayment capacity of the borrower including a consideration of the source of repayment.
- The collateral that being offered as security must be investigated as to the following:
 - Whether it is easily marketable
 - Value of the security at present
 - Whether the value is likely to be stable or it is the security such that its value fluctuates considerably and
 - Is it easily transferable in case of default in payment or not?

3. Credit investigation of the customer

For credit investigation of the customer, the banker looks for:

- Past history of the account.
- Reports from other bankers and people in the same line of business in the case of new customer.
- Search of documents like memorandum of articles, registration papers, annual report available with the Registrar of Joint Stock companies.
- A visit to customer's place of business.
- Analysis of balance sheet and profit and loss account and funds flow analysis in the case of existing companies.
- In case of new companies or new projects which includes the following:

- Examination of technical feasibility.
- Whether the project is economically viable.
- The competence of the managerial personnel to successfully complete and run the project.
- Examination of the cash budgets to ensure the repayment programs.

Document that are generally required for Providing Loans and Advances through Commercial Banks

1. Personal loan

- Mortgage (Registered charge) over the fixed assets.
- Demand Promissory Note
- Guarantee (personal) and/or undertaking to repay loan.

2. Loans to company/ firms

- Personal guarantee of promoters/ shareholders.
- Corporate guarantee of the concerned company/ firm.
- General Letter of Hypothecation- Hypothecation of stocks or machinery or both in the case of Working Capital Loan
- Mortgage (Registered charge) over the fixed assets.
- Demand Promissory Note.

3. Loans against cash (account) pledge

- Cash and Cash equivalent pledge deed.
- Demand Promissory Note.
- Undertaking for repayment of loan and/or personal guarantee.

4. Loans against pledge of shares

- Deed of Pledge of Shares.
- Demand Promissory Note.

- Undertaking for repayment of loan and/or personal guarantee.

5. Loan against pledge of saving bonds

- Deed of Pledge of Saving Bonds.
- Demand Promissory Note.
- Undertaking for repayment of loan and/or personal guarantee.

6. Loan secured against authority to deduct from your own or a third party account

- Deed of Authorization to Deduct Account.
- Undertaking for repayment of loans and/ or personal guarantee.
- Letter of Set Off.
- Demand Promissory Note.

Role of Nepal Rastra Bank in banking supervision of Nepal

Nepal Rastra Bank (NRB) holds a critical role in overseeing banking activities in Nepal, ensuring the stability and trustworthiness of the financial system. Serving as the central regulatory body, NRB develops and enforces prudent rules and guidelines to protect the interests of depositors, investors, and the wider economy. It actively monitors commercial banks, development banks, and financial institutions, ensuring their adherence to regulatory standards, effective risk management, and adequate capital reserves. NRB conducts routine examinations, audits, and evaluations to evaluate the health and performance of financial entities, intervening as needed to address emerging risks or weaknesses. Through its vigilant oversight and regulatory measures, NRB cultivates trust in the banking sector, advances financial inclusivity, and fosters sustainable economic development across Nepal.

Amidst the ongoing recovery from the pandemic and unstable economy, the financial sector is confronting a new and significant challenge. This challenge arises from increased geopolitical unrest, disruptions in supply chains, mounting inflationary pressures, and tightening global financial conditions. Despite Nepal's economy being affected by the global crisis, its banking sector has demonstrated resilience in the face of the ensuing macroeconomic shock.

NRB took on the role of supervisor and regulator of banking sector of the country along with its establishment in 1956. Since its establishment its scope and areas of impact have been increasing only. The guidelines and regulations set by NRB set limitations, provide opportunities, give support and pave path for banking sector. NRB plays the role of guardian, regulator, supervisor, lender to the banks.

Promotion of financial stability, development of safe and efficient payment systems, regulation and supervision of banking and financial system and the promotion of healthy and competitive financial system are some of the objectives of functioning of Nepal Rastra Bank. To attain the above objectives Section 84 of the Nepal Rastra Bank Act 2002 has entrusted Nepal Rastra Bank with the necessary powers to perform inspection and examination of any commercial banks or retrieve necessary information with the purpose of supervision of the commercial banks. The provision on section 84 of Nepal Rastra Bank also mentions that the Board may, after making appropriate decision on matters contained in the report submitted pursuant to sub section 7 of section 84, issue appropriate directions to the Governor about the actions to be taken in the matter and it shall be the responsibility of the Governor to implement or cause to implement such directions.

Methodology of NRB supervision

Bank Supervision Department of NRB adopts and implements the core principles and guidelines recommended by the Basel Committee. NRB conducts its supervision through both on-site and off-site programs. NRB has adopted Risk Based Supervision approach since 2014 which has been emphasizing on the assessment of the quantity of risks and the quality of the risk management in bank and financial institutions.

As part of Risk Based Supervision, the key areas included are capital adequacy, asset quality, risk management, board and senior management oversight, internal controls, compliance, audit functions and others. NRB provides necessary directions for improvement and also takes actions for non-compliance issues. Risk Based Supervision manual has set guidelines for conducting risk based supervision which guides supervisors for Bank's risk assessment and profiling. Risk profiling enables NRB to decide upon the supervisory regime for each bank and helps NRB to channel its resources in high-risk areas. NRB also plans and conducts subsequent on-site

inspections in accordance with the risk profile of the banks. The onsite inspection is supported by an offsite surveillance function which involves continuous monitoring of the banks by analysing the returns/reports received from banks. Similarly, the enforcement function oversees implementation of supervisory directions given for corrective action on issues identified during the on-site inspection process (NRB, 2023).

Off- site supervision

Off- site supervision is performed by studying the documents provided by commercial banks. This function includes the analysis of balance sheet, profit and loss account, other statements and documents received from the commercial bank. Generally, documents and reports are received on a weekly/monthly/quarterly/bi-annually or annually basis. This helps the central bank to judge whether they have accomplished the legal requirements and the instructions regarding the following issues:

- a. Capital adequacy
- b. Cash reserve ratio
- c. Priority sector loan
- d. Deprived sector loan
- e. Classification of loan and provision
- f. Profitability

On-site supervision

On-site supervision is carried out by the inspector or a team of inspectors. They have to do field visit to conduct such supervision. They check various fields and examine whether they are recorded and maintain as per rules and regulations. Especially, the documents about loan accounts, expenses, letter of credit, bank guarantee, remittance should be checked properly while on- site supervision. For conformity, the inspector can randomly verify the physical balance of cash and other assets with records.

Special supervision

Special supervision is conducted only for special purpose. It is not conducted regularly. Depending upon the nature of crisis and objective, the process and method

of special supervision may vary from one case to another. Generally, following are the situations that meet the conditions for special supervision:

- a. When a bank suffers a great loss or economic crisis,
- b. When government or NRB feels that a bank is involved in major fraud,
- c. When majority of shareholders request the central bank for the special supervision,
- d. When a bank opts to go into liquidation.

In the course of supervision, when inspectors find minor mistakes, they provide suggestion and guidelines for correction. The inspectors should prepare a report containing all the findings after conducting each supervision. If a bank is found violated or neglected the rules and regulations the central bank, on the recommendation of supervision department, may take necessary action. The action may be a simple warning to tuff penalty like snatching license, penalty charge etc.

Review of NRB directives

The Nepal Rastra Bank (NRB) is the authorized entity responsible for regulating, controlling, and developing the banking system in Nepal. It grants permission for the establishment of new commercial banks and financial institutions and serves as a lender of last resort to these entities. The NRB's mandate encompasses the supervision, regulation, and monitoring of all commercial banks and financial institutions to ensure their effective functioning. To achieve this, the NRB issues directives, which are guidelines designed to ensure the stability and healthy development of the banking and financial system, thereby enhancing public confidence in these institutions. Financial sector reform in Nepal began in the mid-1980s, and since then, the NRB has played a pioneering role by issuing these directives to commercial banks, striving to align their operations with international standards.

The directives issued by the NRB to commercial banks and financial institutions aim to:

1. Maintain financial stability.
2. Promote healthy development within the banking sector.
3. Enhance public credibility and trust in the banking system.

The number of guidelines issued by NRB to commercial banks and financial institutions are as follows:

1. Provisions of Capital Adequacy
2. Provisions of Classification of Loans/advances and Loan Losses
3. Provisions of Single Borrower and Limitation of the Sectoral Credit and Facilities
4. Provisions of Accounting Policies and Format of Financial Statements
5. Provisions of Mitigation of Risks in Transactions of Licensed Institutions
6. Provisions of Good Corporate Governance
7. Provisions of Timeframe for Implementation of Regulatory Directives Issued in connection with Inspection and Supervision
8. Provisions of Investment
9. Provisions for submission of statistical returns by authorized institutions to Nepal Rastra Bank
10. Provisions of Transfer or Sale of Promoters Shares of licensed institutions
11. Provisions of Consortium Financing
12. Provisions of Credit Information and Blacklisting
13. Provisions of Compulsory Reserve/Statutory Liquidity
14. Provisions of Opening of Branch/Offices
15. Provisions of Interest Rates
16. Provisions of Collection of Financial Resources
17. Provisions of Lending to Deprived Sector
18. Provisions of Amalgamation, Merger and Upgrading
19. Provisions of Know Your Customers
20. Provisions of Subsidiary Companies
21. Miscellaneous Provisions

Source: NRB Circular 2080

Classification of Loan and Advance and Loan Loss Provision

Performing Loans

Pass Loan: Those loans and Advances whose installment (repayment) are not due or due up to one months are classified as pass loan, loans with the collateral of government bonds, T-bills and gold loans amounting up to 10 lakhs etc. such loans are defined as performing loans (Nepal Rastra Bank, 2023).

Watch List: Those loan and Advances lies under pass loan and having principal and interest payments are due for more than one month up to three months, not renewed on time but temporarily maturity period extended short term and working capital loan, loan supplied to a borrower has been classified as non-performing loan of other bank and financial institutions and those loan and advances having poor cash flow during inspection by bank and order to classify as watch list (Nepal Rastra Bank, 2023).

Non-performing Loan

Sub-Standard Loan: Those loans and Advances whose installment (repayment) are due for more than three months but less than six months are classified as sub-standard loan (Nepal Rastra Bank,2023).

Doubtful Loan: Those loans and Advances whose installments (repayment) are due for more than six months but less than one year are classified as doubtful loan (Nepal Rastra Bank, 2023).

Bad Loan (Loss) Those loans and Advances whose installment (repayment) are due for more than one year must be classified as bad loan (loss) (Nepal Rastra Bank, 2023)

Provision for Loan Losses

The loan loss provisioning, on the basis of the outstanding loan and advances and bills purchases classified as per this directives, shall be provided as follows:

Table 1
Loan Loss Provision

S.N.	Classification of loan	Loan loss provision
1.	Pass	1%
2.	Watch List	5%
3.	Sub-standard	25%
4.	Doubtful	50%
5.	Loss	100%

(Source: NRB/Unified Directives, 2023)

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". Where the banks provide for loan loss provisioning in excess of the proportional required under the directives of NRB, the whole amount of such additional provisioning may be included in General Loan Provision under the supplementary capital.

Principles of bank supervision

The Basel Committee on Banking Supervision issued 'Core Principles of Effective Banking Supervision.' These principles are universally implemented in the process of banking regulation and supervision, which increases financial stability. It has two sets of principles; one is supervisory powers, responsibilities and functions and second is prudential regulations and requirements. The principles are as under (Bank for International Settlement, 2011):

Principle 1: Responsibilities, objectives and powers

Principle 2: Independence, accountability, resourcing and legal protection for supervisors

Principle 3: Cooperation and collaboration

Principle 4: Permissible activities

Principle 5 : Licensing criteria

Principle 6: Transfer of significant ownership

Principle 7 : Major acquisitions

Principle 8: Supervisory approach

Principle 9: Supervisory techniques and tools

Principle 10: Supervisory reporting

Principle 11: Corrective and sanctioning powers of supervisors

Principle 12: Consolidated supervision

Principle 13: Home-host relationships

Principle 14: Corporate governance

Principle 15: Risk management process

Principle 16 : Capital adequacy

Principle 17: Credit risk

Principle 18: Problem assets, provisions and reserves

Principle 19: Concentration risk and large exposure limits

Principle 20: Transactions with related parties

Principle 21: Country and transfer risks

Principle 22: Market risks

Principle 23: Interest rate risk in the banking book

Principle 24: Liquidity risk

Principle 25: Operational risk

Principle 26: Internal control and audit

Principle 27: Financial reporting and external audit

Principle 28: Disclosure and transparency

Principle 29: Abuse of financial services

Nepal accepts these standards in its regulatory and supervisory framework (Acharya, 2020).

Implementation of NRB directives in commercial banks

Commercial banks incorporate and implement the directives issued by NRB by taking various actions and measures. Some of the actions or measures of implementation of NRB directives in commercial banks are:

- Development of internal policies in line with the directives issued and update them according to the updates in directives.
- Follow the procedures as prescribed by directives to verify the information of customers in CIB.
- Develop various forms in relation to loans and advances such as loan request form, KYC forms
- Development of detailed analysis measures of personal guarantees
- Development of guidelines and checklists for collateral evaluation

Supervision of commercial banks is based on the implementation of NRB directives.

2.3 Empirical review

Boubacar and Bans-Akutey (2023) studied the effect of supervision on bank performance and ascertained the effect of regulation on bank performance. The researchers also assessed the challenges faced by banks in the implementation of bank regulations. This study adopted a descriptive survey approach using data collected from all employees of a commercial bank in Accra Newtown. Data were analyzed using descriptive and inferential statistics from IBM SPSS Statistics. They found that there is a need for closer collaboration between banks and external regulatory bodies considering the positive effect of bank regulation on bank performance. The researchers found a need for continuous monitoring and evaluation of processes to ensure that banks comply with regulations. A positive relationship was found between banking regulation and bank performance and between supervision and bank performance. The study identified poor communication, lack of resources, resistance to change, and inefficient processes as the major challenges faced by banks in implementing strategies and achieving their objectives.

Forson et. all (2023) examined the determinants of nonperforming loans through the impact of supervisory devices in credit risk management in Africa. The paper

employed bank-specific, macroeconomic and institutional data for a panel of 14 universal banks over the period 2009 to 2020. The research developed models that capture the role of regulatory supervision on credit risk. Findings from the Panels Corrected Standard Errors (PCSE) and the system GMM showed that previous year's NPL and inflation significantly affect NPLs in the banking space of Ghana. Bank size and financial development were found to be inversely associated with NPLs. The interactive term of regulatory quality and government effectiveness on NPLs was found to have net negative effect. The study suggested that regulatory quality enhances the reductive effects of government effectiveness on NPLs. The researchers' findings in general lend credence to the financial instability theory as NPLs in the Ghanaian context had been the outcome of activities of speculative borrowers.

Tingen (2021) assessed the role of central banks supervision on commercial banks credit business based on post epidemic environment. The aim of this research was to strengthen the efficiency and level of central bank's supervision and provide corresponding theories and references for the subsequent research. This research aimed to solve the problem of imbalance of credit business of the commercial banks by analyzing the central banks supervision. This study used various information and data mainly based on the methods of literature research, exploratory research and qualitative analysis rather than quantitative analysis. The researcher conducted exploratory research on the central bank's supervision of commercial bank's loan operations based on those existing data. This study identified the issues in central bank supervision and provided a more comprehensive understanding of the research. The limitation of this study is the lack of a specific application to support the analysis. Consequently, the paper's practical applicability is reduced.

Mburu et al., (2020) studied on role of regulation and supervision of the central bank in Kenya. The study aimed to investigate the moderating role of central bank regulations on the relationship between credit management practices and loan performance, rooted in the credit risk theory. Employing an explanatory research design and adopting a positivist research philosophy, the study targeted the entire population of 44 commercial banks in Kenya using a census approach. Both primary and secondary data were utilized, with primary data collected through structured questionnaires and secondary data obtained from a review of existing bank loan records spanning four years from 2015 to 2018. Multiple regression analysis was

employed to test the study hypothesis, ultimately concluding that Central Bank Regulations did not exhibit a significant moderating effect on the relationship between credit management practices and loan performance. As a result, the study recommended continuous assessment and updating of credit management practices and central bank regulations by the central bank of Kenya, alongside the establishment of comprehensive credit policies by government regulatory bodies to regulate traditional and emerging credit practices among financial institutions.

Podtserkovnyi and Vozniakovska (2020) researched on the discretionary powers of central banks in issuing stabilization loans amidst the economic repercussions of the Covid-19 pandemic. In light of the negative impact of governmental measures to curb the pandemic on the economy, the authors argue that stabilization loans, particularly those provided by central banks, serve as crucial instruments in preventing sectors such as the banking industry from bankruptcy.

Employing various scientific methods including dialectical analysis, comparison, elementary-theoretical analysis, synthesis, hermeneutic analysis, and forecasting, the authors examine the dynamics of legislative consolidation of discretionary powers, particularly those of the National Bank of Ukraine (NBU) in the issuance of stabilization loans. Their research highlighted the legal framework underpinning the NBU's decision-making process regarding stabilization loans, citing constitutional provisions and laws governing its functions. Notably, the study emphasized the NBU's role in ensuring the stability of the national currency and the banking system, as enshrined in the Constitution of Ukraine and relevant legislation. The authors also discussed the nature of stabilization loans as a form of refinancing mechanism employed by the NBU for effective monetary policy regulation, liquidity management, and as a lender of last resort. Drawing from empirical data, they underscored the significance of such loans in stabilizing the financial market, particularly during economic crises such as the Covid-19 pandemic. Furthermore, the study addressed the legal limits of the NBU's powers in issuing stabilization loans, emphasizing the necessity of adhering to constitutional and statutory provisions governing its functions. It highlights the NBU's autonomy as a central government body, mandated to act within the framework of Ukrainian laws and the Constitution.

Overall, the research advocated for an expanded approach to the discretion of central banks in issuing stabilization loans, aligning with constitutional principles and legal frameworks to ensure effective economic stabilization amidst crises such as the Covid-19 pandemic.

Hirtle et. al (2019) delved into the impact of supervision on bank performance, a topic that has received relatively limited attention despite its critical importance in ensuring financial stability. The overarching objective of the research was to examine the effectiveness of supervision in identifying and addressing factors that pose risks to the immediate health or long-term viability of banks. Specifically, the study aimed to investigate the comprehensive range of supervisory activities involved in prudential supervision, which includes traditional compliance efforts as well as modern approaches aimed at monitoring unsafe or unsound business practices. By analyzing Federal Reserve supervisory expectations outlined in Supervision and Regulation Letters (SR Letters), the research seemed to provide insights into the role of supervision in promoting the stability and soundness of the banking sector. Through detailed analysis and robust methodology, the authors demonstrated that heightened supervisory attention contributes to lower risk exposure for banks without compromising profitability or growth.

Furthermore, the research offers valuable insights into the mechanisms through which supervision influences bank behavior, suggesting that it plays a pivotal role in improving risk management practices and fostering long-term efficiency. By analyzing data on supervisors' time allocation and employing a sophisticated matched sample approach, the study revealed that banks receiving more supervisory attention tend to maintain less risky loan portfolios, exhibit reduced volatility, and display greater resilience during industry downturns. These findings highlighted the unique contribution of supervision in mitigating risk within the banking sector, offering valuable insights for policymakers and industry practitioners seeking to enhance regulatory frameworks. This study made a significant contribution to the literature by providing empirical evidence of the distinct benefits of supervision, complementing traditional regulatory measures. Overall, the findings underscored the critical importance of effective supervision in bolstering financial stability and mitigating systemic risk, underscoring the ongoing need for vigilant attention to supervisory practices in the banking sector.

Dhar (2015) analyzed the changing role of reserve bank of India in bank supervision and corporate governance with the introduction of risk based parameters. The objective of this research paper was to identify the changing role of the RBI, interpret the changes that have occurred with the implementation of Basel norms, analyze the central bank's role as a controller of national liquidity, demonstrate the challenges of measuring, mitigating, and managing different types of risks, develop strategies to combat non-performing assets (NPAs), and critically analyze the corporate governance frameworks of banks. The proposed research incorporates secondary information on risk management in banking, the scope and direction of successive Basel norms, and the corporate governance practices followed by Indian banks.

Their research is pertinent as it underscores the role of effective supervision and regulatory frameworks in enhancing bank performance. The findings suggest that focusing solely on regulatory and supervisory measures may not be sufficient; broader institutional reforms, including legal system overhauls and promoting transparency, are also crucial for reducing bad loans and enhancing bank profitability. This insight is valuable for understanding the comprehensive role of the RBI in the Indian context, particularly in its efforts to implement Basel III norms and manage systemic risks effectively.

This paper focused on the paradigm shift in the role of the RBI. It aimed to provide a new dimension in the literature on corporate governance, risk management in banking, and the ethical obligations of banks, as well as the successful implementation of international Basel norms on capital adequacy through the issuance of relevant norms and guidelines. In conclusion, the RBI has evolved significantly, adapting to new regulatory frameworks like Basel II and Basel III. While many Indian banks have made strides in implementing these norms, the transition to Basel III poses significant capital adequacy challenges. Thus, the RBI must balance its roles as supervisor, monitor, liquidity controller, and policy maker to optimize benefits for all stakeholders.

Bouheni (2013) studied on the effects of supervision on banking performance. The primary objective of this research was to assess the impact of banking supervision on performance within the banking industry. The study aimed to provide clarity by analyzing the effects of supervision on bank performance. Specifically, the research

utilized the generalized method of moments (GMM in system) to investigate the influence of supervision on the performance of the ten largest European banks from France, Germany, the UK, and Greece over the period 2005-2011. By examining a range of variables capturing specific, macroeconomic, institutional, and financial development indicators, the study aimed to discern the effectiveness of banking supervision in enhancing or impeding bank performance. The research also explored how the implementation of banking supervision may vary based on the institutional environment and political landscape of different countries.

The study revealed that while there is an apparent association between banking supervision and performance, this relationship diminishes when considering additional factors such as specific indicators, macroeconomic conditions, institutional characteristics, and financial development metrics. These findings highlighted the nuanced influence of banking oversight, contingent upon the intricacies of a nation's institutional framework and political dynamics. Through this analysis, the study contributed to understanding the nuanced relationship between supervision and bank performance in diverse regulatory contexts.

Abdennour and Khediri (2010) examined the effect of bank supervision on bank profitability in the Middle East and North Africa (MENA) region from 1999 to 2006. The main objective of the research was to examine the effect of bank supervision on bank profitability in the 1999–2006 period. They found that supervision differences significantly impact profitability. Higher profitability was associated with countries where supervisors could take legal action against external auditors for negligence and where the central bank was responsible for supervision. Conversely, profitability was negatively related to the unification of financial supervision and the existence of Deposit Insurance (DI). The study also highlighted that several bank characteristics and macroeconomic factors significantly influenced bank profitability.

Arora (2009) researched on banking risk management in India and RBI supervision. This study aimed to critically examine the current risk management practices and supervisory processes as directed by the Reserve Bank of India (RBI). The objective was to understand how banks identify, manage, and mitigate risks in compliance with regulatory guidelines. The study focused on three anonymized banks, utilizing a judgment sampling method to gather both primary and secondary data. Primary data

was collected through questionnaires and interviews, while secondary data was sourced from published reports, RBI circulars, and bulletins. Analysis of risk management practices, based on RBI guidelines, revealed several key components: organizational structure, comprehensive risk measurement approaches, board-approved risk management policies, guidelines governing risk-taking, robust management information systems (MIS) for reporting and monitoring risks, and a clear delineation of responsibilities for risk management independent of operational departments. Furthermore, periodic review and evaluation were essential. The literature suggested that banks should manage risks that could be efficiently handled at the firm level rather than absorbing unnecessary risks or those better transferred to other participants. Effective risk management entailed identifying risks that could be transferred, eliminated through business practices, or must be actively managed internally.

Boudriga et al (2009) assessed banking supervision and nonperforming loans as a cross-country analysis. The research aimed to empirically analyze the determinants of nonperforming loans (NPLs) across 59 countries from 2002 to 2006, focusing on the potential impact of regulatory factors on credit risk exposure. It sought to assess the relationship between various regulatory measures, such as capital adequacy ratios, provisioning policies, private ownership, foreign participation, bank concentration, and the levels of problem loans. Additionally, the study aimed to evaluate the effectiveness of market discipline and regulatory interventions in mitigating credit risk, particularly in countries with varying levels of institutional strength, business environment integrity, and democratic governance. To evaluate the role of regulatory supervision on credit risk, the paper examined various interactions between institutional features and regulatory mechanisms. A cautious provisioning strategy and a greater capital adequacy ratio (CAR) were found to lower the number of problem loans, based on empirical data. The advantages of bank concentration, international participation, and private ownership were also covered in the paper. The findings, however, ran counter to the notion that market discipline produces better economic performance. In the end, the study showed that, rather than concentrating on regulatory and supervisory difficulties, the most efficient strategy to reduce bad loans is to overhaul the legal system and promote transparency and democracy.

Pasiouras et al (2009) dwelled on the impact of banking regulations on banks' cost and profit efficiency. The principal aim of the study was to examine the factors that contribute to nonperforming loans (NPLs) in various nations throughout a designated duration. By examining regulatory elements such as capital adequacy ratios, ownership structures, provisioning policies, and bank concentration, the study sought to identify the most productive regulatory approaches for mitigating credit risk exposure and augmenting stability in the banking industry. A panel dataset containing aggregate banking, financial, economic, and legal environment data for 59 nations between 2002 and 2006 was used in the study. The researchers examined the association between regulatory characteristics and the amount of non-performing loans (NPLs) using econometric methodologies, accounting for several factors unique to each nation. This methodological technique made it possible to identify important factors that influence non-performing loans and to evaluate.

Shrestha (2004) conducted a study on non-performing loans (NPLs) and loan loss provisioning in NBL, NABIL, and SCBNL, identifying key issues such as economic instability, inconsistent NRB policies, political pressure to lend to unworthy borrowers, and weak loan sanctioning processes. These factors contributed to high levels of NPLs, particularly in NBL, which, despite its significant investment in income-generating loans, operated at a loss. NABIL also had higher-than-acceptable NPL levels. It is also recommended that banks improve their credit appraisal systems, enhance credit monitoring and supervision, and utilize data from the Credit Information Bureau to avoid bad debts. Additionally, the researcher suggested regular supervision and follow-up on loan utilization, employee training programs, and more stringent yet supportive regulatory measures from the NRB to help reduce NPLs and improve financial stability.

Bhattarai (2004) conducted a research on implementation of directives issued by NRB. The study examined the NRB's norms on capital adequacy, loan classification, and provisioning. The research found that continuous review and classification of loans help banks monitor loan portfolio quality and take corrective actions. Both banks were found to fall short in supplementary capital but could meet total capital requirements under the new directives. Changes in NRB directives led to reduced loan exposure, decreasing interest income but increasing depositor protection, higher operational costs, and increased demand for shareholder contributions. The researcher

concluded that while the new provisions would lead to higher loan loss provisions and reduced profitability, they would provide a clearer picture of asset quality. She recommended that banks carefully analyze the repayment capacity of their credit clients to avoid increased provisions and reduced profitability due to longer past-due periods.

Table 2
Summary of Review

Author/s	Methodology	Variables	Findings
Boubacar et. all, (2023)	Descriptive and inferential statistics from IBM SPSS Statistics 24	ROE, Loan, Lending	A positive relationship was found between banking regulation and bank performance and between supervision and bank performance. The study identified poor communication, lack of resources, resistance to change, and inefficient processes as the major challenges faced by banks in implementing strategies and achieving their objectives
Forson et. All (2023)	Bank-specific, macroeconomic and institutional data for a panel of 14 universal banks over the period 2009 to 2020	NPL Bank Profitability	Findings in general lends credence to the financial instability theory as NPLs in the Ghanaian context has been the outcome of activities of speculative borrowers.
Tingen et. All (2021)	Exploratory research and qualitative analysis.	-	The central bank's credit supervision of commercial banks determines the scale of social credit, the quantity of money supply. It regulates the balance of social supply and demand at money supply side

Podtserkovnyi and Vozniakovska (2020)	Dialectical analysis, comparison, elementary-theoretical analysis, synthesis, hermeneutic analysis, and forecasting	Expanded approach to the discretion of central banks in issuing stabilization loans, aligning with constitutional principles and legal frameworks to ensure effective economic stabilization amidst crises such as the Covid-19 pandemic.
Mburu et. All (2020)	Explanatory research design, structured questionnaires, Multiple regression analysis	Debt Collection Policy, Client Appraisal, Lending Policy, Central bank regulations,
Hirtle et. All (2019)	Matched sample approach	Bank profitability Bank profitability Bank characteristics Return on Asset (ROA) Risk weighted Asset Non-performing loans SD ROA
Sujoy Dhar (2015)	Descriptive and explanatory analysis	The study recommended continuous assessment and updating of credit management practices and central bank regulations by the central bank of Kenya The results underscore the distinct role of supervision in mitigating banking sector risk Focusing solely on regulatory and supervisory measures may not be sufficient; broader institutional reforms, including legal system overhauls and promoting transparency, are also crucial for reducing bad loans and enhancing bank profitability

Bouheni (2013)	Generalized method of moments (GMM in system) Wald Statistics	Bank performance: ROAA, ROAE, NIM,CIR GDP Bank Size Banking Supervision Index Inflation GDP	The findings support the view that the implementation of banking supervision differs greatly depending on the institutional environment and the country's politics
Abdenmour and Khediri (2010)	Differences in the profitability of MENA publicly quoted banks, descriptive statistics, Correlation analysis	Return on Average Assets(ROAA) Equity to total assets(ETA) Net loan to total assets(NLTA) Cost Income Ratio(CIR) Annual Inflation Rate(INF) Gross Domestic Product Growth(GDP)	Supervision differences significantly impact profitability
Arora and Agrawal (2009)	Questionnaires and interviews, Judgment sampling method	NPA CAR	Banks should manage risks that could be efficiently handled at the firm level rather than absorbing unnecessary risks or those better transferred to other participants

Boudriga et. All (2009)	Baseline model	Aggregate rate of NPL	Rather than concentrating on regulatory and supervisory difficulties, the most efficient strategy to reduce bad loans is to overhaul the legal system and promote transparency and democracy.
	regression Panel data regression	Diff between CAR and min. required Bank Provision to NPL Bank Return on Assets Gov5. owned bank assets divided by total bank asset Percentage of asset held by five largest banks GDP growth rate	
Fotios Pasiouras et. All(2009)	Battese and Coelli Model Profit Frontier model	Total cost of bank Time Profit before Taxes Capital Requirement Power of the supervisory agencies Indicator of private monitoring	The study observed opposite effect in the case of restrictions on bank activities, with higher restrictions having a negative influence on cost efficiency but positive influence on profit efficiency.

2.3 Research gap

From the study it has been found that lending practice of commercial banks in the present context of Nepal plays important role in the utilization of resources /assets of the bank. Some research have been done in the international level where the impact of supervision of central banks on commercial banks have been done. Among them many are focused on the impact on loans and advances of the bank. Some research were done in which matters relating to recovery procedures, supervisory role of NRB and impact of NRB directives has been discussed. However not much research was found in detailed analysis of impact of regulation and supervision on lending practices of commercial banks ultimately affecting the profitability of the bank. Hence the

researcher had attempted to fill this research gap by taking reference of Rastriya Banijya Bank Ltd, Nabil Bank Ltd and Global IME Bank Ltd. This research will be able to deliver some of the present issues of lending practices, its relation with various other parameter and its impact on profitability of the bank. After receiving the relevant literatures, the next chapter concentrates in the research methodology applied in the study.

Chapter III

Research Methodology

This chapter describes methodology employed in this study. It has five sections. The first section is research design followed by Population and sample and sampling design. Similarly, the third section describes nature and sources of data and the method of data collection. Fourth section which explains methods of analysis is followed by last section research framework and definition of variables.

3.1 Research design

The research design for this study is predominantly quantitative, employing a cross-sectional approach. This design allows for the collection of data at a specific point in time, enabling a snapshot analysis of the impact of NRB supervision on the performance of commercial banks of Nepal. This research is based on secondary data. It is simply a descriptive research. The descriptive research design is used to find out and compare the situation of lending practices among sample banks. It covers the data from 10 years. The collected data are analyzed by using financial as well as statistical tools such as ratios, arithmetic mean, standard deviation, correlation etc. In addition, causal comparative research design is used to identify the cause and effect relationship between various aspects of lending practices.

3.2 Population and sample and sampling design

There are 20 commercial banks operating in Nepal from mid July 2023 (NRB report, 2023). They constitute the population sample. Among them only three commercial banks are selected as sample each from three categories respectively viz. State Owned Commercial Bank, Joint Venture Commercial Bank and Non-state owned commercial bank. The sample banks are selected on the basis of loans and advances. Among state owned commercial banks RBB has highest amount of Loans and advances for FY 2079/80. Among Joint venture commercial banks Nabil Bank Ltd has the highest amount of Loans and Advances. And among non-state owned commercial banks GBIME banks ltd has highest loans and advances. The sample of three commercial banks cover 15% of the total population i.e 20 commercial banks.

The population under consideration for this study comprises commercial banks operating within the regulatory purview of Nepal Rastra Bank. A purposive sampling

technique is employed to ensure representation from commercial banks. The sample size is determined through a purposive sampling method taking into account the size and significance of each category.

3.3 Nature and sources of data and the instrument of data collection

This study is mainly based on secondary data. Concerned banks, Nepal Rastra Bank, SEBO, and different library are the providers of the data. The review of literature of the proposed study was based on the text books, official publications, journals, unpublished thesis, reports, web site etc. Various necessary data and information at macro level have been collected from relevant institutions and authorities such as Nepal Rastra Bank, Ministry of Finance, NEPSE, SEBO and their respective publications similarly the required micro level data derived from annual reports of selected banks, SEBO and NEPSE. In addition to above, additional data and information were collected from different sources such as library of Shankar Dev Campus, T.U. Central library, SEBO library etc. The major sources of data and information are NRB Economic Report, Non-Banking Financial Statistics (NRB), Banking and Financial Statistics (NRB), Economic Survey (Ministry of Finance), Annual Reports of Concern Banks, Annual Report of SEBO Nepal, Trading Report of NEPSE, Journal of Finance & Business, Previous Research Studies, Dissertation and Articles on the Subject, Various Text Books and Different Library.

As the study is based on secondary data, the necessary data were directly collected from annual reports of the concerned banks, research department of NRB and visiting different websites

3.4 Methods of analysis

Data were collected from various sources in raw form. Such raw data were classified and tabulated as per the requirement of the study and in accordance with the nature of data. Financial tools such as (Ratio analysis) and statistical tools such as (Arithmetical Mean, Standard Deviation, and Coefficient of Variation) are used. The detailed calculations, which cannot be included in the body part of the report, are presented in annexes at the end.

3.5 Data analysis tools

3.5.1 Financial tools

To evaluate the financial position and performance of any firm ratio is used as a key tool of financial analysis. Financial analysis is the process of determining the financial strength and weakness of the firm by correctly establishing relationship between the items of the balance sheet and profit and loss account. Financial analysis uses the financial statements to analyze a company's financial position and performance and to estimate future financial performance.

Ratio analysis

Financial ratio gives relationship between two accounting figures in mathematical terms. Ratio analysis is a part of the whole process of analysis of financial statements of any business or industrial concern specially to take output and credit decisions. Thus ratio analysis is used to compare a firm's financial performance and status to that of other firm's to it overtime. The qualitative judgment regarding financial performance of a firm can be done with the help of ratio analysis. Even though there are many ratios, only those ratios have been calculated which are related to the subject matter. Following ratios have been calculated and analyzed in this study.

(a) Loans and Advances to Total Assets Ratio

Total assets side of a bank is composition of different assets among them some generated income and some do not generate income. Among income generating assets loan and advances are the high income generating assets therefore the management is always trying to increase the portion of loan and advances in total assets and is keen on decreasing non income generating portion of assets from total portfolio of the bank. The ratio of loans and advances to total assets measures the volume of loans and advances in the structure of total assets. Loans and advances of commercial and Development banks represent the major portion in total assets. The high degree of ratio indicates the good performance of the banks mobilizing its fund by way of lending functions. However, in its reverse side, the high degree indicates low liquidity with the banks. Loans and advances always carry certain degree of risk. Thus this asset of banking business is regarded as risky assets. The low ratio indicates low

productivity and high degree of safety in liquidity and vice versa. This ratio is calculated as follows.

$$\text{Loan \& Advances to Total Assets Ratio} = \frac{\text{Total Loan \& Advances}}{\text{Total Assets}}$$

(b)Credit Deposit Ratio (CD Ratio)

CD ratio is one of the most important tools for analyzing the profitability of a bank. Since all depositors has to pay interest and if any deposit is not utilized in profit earning way it will decrease net interest income of that bank .CD ratio is the parameter which ascertain fund deployment efficiency of bank. In other words this ratio is calculated to find out how successfully the banks are utilizing their total deposits on credit or loans and advances for profit generation purpose as credit generates high rate of return. Greater CD ratio indicates the better use of total deposits and better yield, however, liquidity requirements are also needed to take in consideration. Hence management should always try to make better combination of risk and return. This ratio is obtained by dividing total loan and advances by total deposit of the bank.

$$\text{Credit Deposit Ratio} = \frac{\text{Total Loan \& Advances}}{\text{Total Deposit}}$$

(c)Loan Loss Provision to Loan and Advances ratio

Loan loss provision to Loan and advances shows percentage of loan is covered against the possible future loss due to nonpayment of loan. This ratio describes the quality of assets in the form of loan and advances that a bank is holding. Since there is risk inherent in loan and advances, NRB has directed banks to classify its loan and advances into different category and accordingly to make provision for possible loss. Loan Loss provision signifies the cushion against the future contingencies created by the default of the borrower in payment of loan and ensures the continuous solvency of the bank. Since high provision has to be made for non-performing loan, higher provision for loan loss reflects increasing non-performing loan in volume of total loan.

The low ratio signifies the good quality of assets in the volume of total loan. It indicates how efficiently it manages loan and advances and make efforts to cope with

probable loan loss. Higher ratio implies higher portion of NPL in the total loan portfolio. The ratio is calculating as follows.

$$\text{Loan Loss Provision Ratio} = \frac{\text{Loan Loss Provision}}{\text{Total Loan \& Advances}}$$

(d) Non Performing Loans to Total Loan

Total loan and advances is generally divided in to two categories namely performing loan and non-performing loan. Nonperforming loan to total loan ratio determines the proportion of non- performing loan in the total loan portfolio. Higher ratio implies the bad quality of assets of banks in the form of loan and advances. Hence lower NPL to total credit ratio is preferred. The ratio is calculated as follows

$$\text{NPL to Total Loan \& Advances Ratio} = \frac{\text{Non Performing Loan}}{\text{Total Loan \& Advances}}$$

(e) Total Provision to non-Performing Loan

NRB had directed all banks to provide provision for all types of loan and advances. Even performing loan needs to provide loan loss provision at the rate of 1% and 12.5%. This ratio determines the proportion of provision held to non-performing loan. This ratio measures up to what extent of risk inherent in NPL is covered by the total loan loss provision. More than 100% ratio signifies that the bank is safeguard against future contingencies that may create due to bad loans, where as lower than 100% may create huge provision in coming future due to requirement of high provision to substandard loan and advancers. This Ratio is calculated as follows.

$$\text{Loan Loss Provision to NPL Ratio} = \frac{\text{Loan Loss Provision}}{\text{Non Performing Loan}}$$

(f) Return on Loan and Advances

Net profit is the amount recovered after deducting all kinds of liabilities therefore various ratios are calculated in relation with the net profit. Return on loan and advances Ratio indicates how efficiently the bank has employed its resources in the forms of loan and advances. Net profit of a bank largely depends upon interest earn from loan and advances and there is positive correlation between effective utilization of loan and advances and net profit. This ratio measures the bank's profitability with

respect to loan and advances. Generally, high ratio is considered better for the performance of the bank and vice versa. This ratio is calculated as follows:

$$\text{Return on Loan \& Advances} = \frac{\text{Net Profit}}{\text{Loan \& Advances}}$$

(g)Return on Assets

This ratio indicates how efficiently the bank has employed its resources in the form of total assets. This ratio measures bank's profitability with respect to total assets. Higher the ratio better is the performance of the bank and vice versa. This ratio is calculated as per followings:

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

3.5.2 Statistical Tools

Statistical tools help to find out the trend and movements of financial position of the bank. It also analyzes the relationship between variables and helps banks to make appropriate investment policy regarding to profit maximization and deposit collection, fund utilization through providing loans & advances or investment on other companies. Various statistical tools are used to analyze the collected and tabulated data and to obtain the objectives of the study. Simple analytical tools such as standard deviation, Karl Pearson's coefficient of correlation, regression analysis etc are applied in this study which are as follows:

A. Arithmetical Mean

A single value represents the entire data through arithmetical mean. It provides the gist and gives the bird's eye view of the huge mass of unwieldy numerical data. It is calculated as:

$$\bar{X} = \frac{\sum X}{N}$$

Where:

$$\bar{X} = \text{Arithmetic mean}$$

N = Number of observations

$\sum X$ = Sum of observations

B. Standard Deviation

Standard deviation is an important and widely used tool to measure dispersion. A standard deviation is obtained as the positive square root of the arithmetic mean of the squares of the deviations of the given observations from their arithmetic mean. It is denoted by the letter σ (sigma). Standard deviation of various ratios are calculated in this study.

$$\sigma = \sqrt{\frac{\sum X^2}{N} - \left(\frac{\sum X}{N}\right)^2}$$

Where,

σ = Standard Deviation

$\frac{\sum X^2}{N}$ = Sum of Squares of Observation

$\left(\frac{\sum X}{N}\right)^2$ = Sum of Squares of Mean

C. Coefficient of Variation

The Coefficient of variation is the most commonly used measure of relative variation. These are relative measures of dispersion, comparable in distribution, and are defined as the ratio of the standard deviation to the mean, expressed as a percentage. When the researcher wants to compare the data variability of more than two years, coefficient of variation is used. A series with smaller C.V. is said to be less variable or more consistent or more homogeneous or more uniform or more stable than the others and vice versa. It is calculated as;

$$\text{Coefficient of variation} = \frac{\text{Standard Deviation}}{\text{Mean}} \times 100\%$$

$$C.V. = \frac{\sigma}{\bar{X}}$$

Where,

$$\begin{aligned}\bar{X} &= \text{Mean} \\ \sigma &= \text{Standard Deviation} \\ C.V. &= \text{Coefficient of Variation}\end{aligned}$$

(D) Correlation coefficient (r)

Correlation analysis is another important tool of statistic. It describes the relationship between variables and shows the degree of dependency of one variable with another variable. Correlation refers the degree of relationship between two or more variable. It determines the association between the variables. Two variables are said to be correlated when the change in one variable result in change in other variables. Different model for correlation analysis has been formulated and we have used Karl Pearson coefficient of correlation to determine the relationship between variables studied. Karl Pearson coefficient of correlation is calculated as :

$$\text{Coefficient of correlation (r)} = \frac{\sum xy}{N\sigma_x\sigma_y}$$

Where, $x = (X - \bar{X})$, $y = (Y - \bar{Y})$

The result of coefficient is always between -1 to $+1$, when $r = +1$, it means there is positive relationship between two variables and when $r = -1$, It means there is negative relationship between two variables.

(E) Regression Analysis

In statistical analysis, regression analysis is a set of statistical processes for evaluating the relationships between variables. It involves a variety of multivariate modeling and analysis techniques where the focus is on the relationship between the dependent variable (ROA and ROE) and one or more independent variables (credit deposit ratio, non-performing loan ratio, loan loss provision ratio, return on loan and advances). More specifically, regression analysis helps one understand how the typical value of the dependent variable (or 'criterion variable') changes when any one of the

independent variables is varied, while the other independent variables are held fixed (Yadav, Dhakal, Tamang, Shrestha, & Panta, 2010).

3.6 Research Framework and Definition of Variables

The research framework will be based on a conceptual model that illustrates the relationships between regulatory supervision and various performance indicators of commercial banks. As being the research based on loans and advances and loan loss provision, its different parameter was the major research variables. Total loans and advances of the bank, loan loss provision ratio, non-performing loan ratio, return on assets, return on equity, and number of NRB inspections are the variables taken in this study.

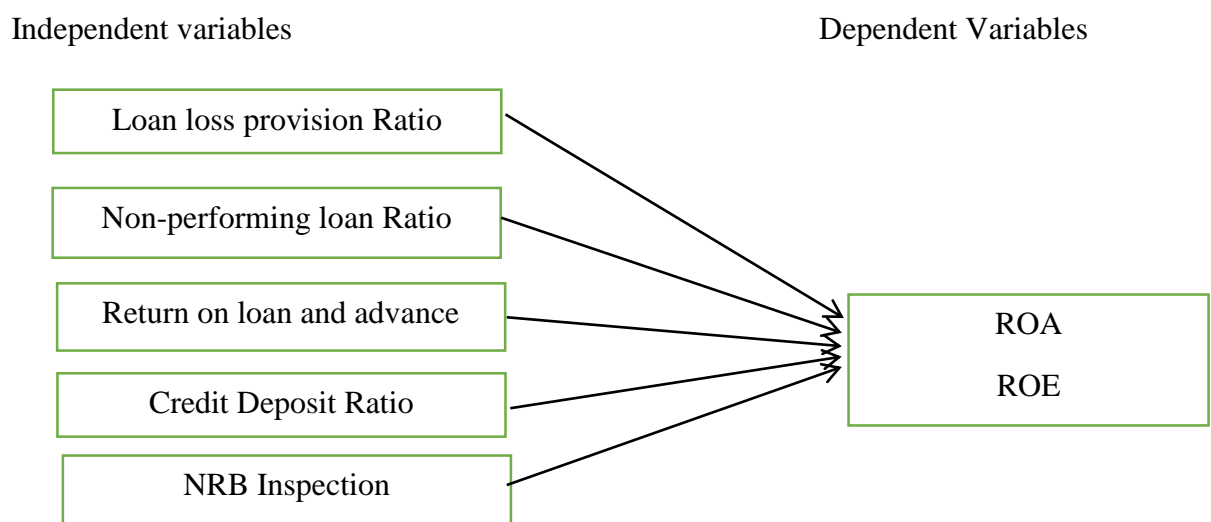


Figure 1 *Research Framework*

Source: Shah (2023), Shrestha (2023), Boubacar (2023)

Definition of Variables

Credit Deposit Ratio

Loan and advance to total deposit ratio is used as a measure to find the credit risk variable of the bank. Previously (Shah, 2016) and (Shrestha, 2020) have used credit deposit ratio of the banks as a measure of credit risk.

Non-performing Loan Ratio

This ratio determines the non-performing assets in the total loan and advances portfolio' greater ratio implies the bad quality of loan of the bank.

Loan Loss Provision Ratio

Loan loss provision ratio refers to the ratio of provision set aside by bank for future contingency of loan loss to total loan and advances. The amount is calculated on the basis of NRB directives.

Return on Assets

Return on total assets ratio measures the profitability of a firm that explains the capacity of a firm to earn satisfactory return on all financial resources. This ratio explains net income for each unit of asset.

Return on Equity

Shareholders fund represents that part of long term source of funds which is collected by using equity shares and preference shares. To measure the return earned by shareholders, return on shareholders' equity is used or this ratio is calculated to find out the profitability on the owners capital or investment.

Return on Loans and Advances

Return on loans and advances is the ratio of Net profit to total loans and advances of the bank.

NRB Inspection

NRB Inspection refers to the number of inspection done by NRB on banks including on site inspections and special inspection in a year.

Chapter IV

Results and Discussion

4.1 Results

In this segment we analysis the data available and interpret them in meaningful manner. Various statistical and financial tools have been employed while analyzing data. Data presentation and analysis is the most important part of this thesis or say it is the heart of whole study. All Findings, conclusion and recommendation are based on the result of analysis.

4.1.1 Data presentation and analysis of sample banks

Analysis of Total Loans and Advances

Position of total loans and advances during the study period in RBB, Nabil and GBIME are analyzed in this section. Comparative total loans and advances position and variation in total loans and advances of the banks are analyzed here under.

Table 3

Total Loans and advances of sample banks (Rs. In Crores)

Fiscal Year	RBB	Nabil	GBIME
79-80	24,294	33,941	37,435
78-79	22,672	31,057	27,221
77-78	19,597	20,662	24,244
76-77	15,652	15,389	20,000
75-76	14,812	13,356	11,406
74-75	12,087	11,362	9,337
73-74	10,643	9,247	7,896
72-73	8,178	7,821	5,921
71-72	7,207	6,550	5,022
70-71	6,085	5,469	4,301
Mean	14,123	15,485	15,278
SD	6440.77	10051.30	11324.85
CV	46	65	74

Source: Appendix 1

Table 3 shows the distribution of total loans and advances of RBB, Nabil and GBIME during the ten-year study period starting from FY 2070-71 to FY 2079-80. The total loans and advances of all three banks reached maximum in FY 2079-80. The total loans and advances of the banks are in increasing trend over the study period. The average total loans and advances of Nabil is highest among three banks i.e. Rs. 15,485

Crores while RBB has lowest average loans and advances i.e. Rs. 14,123 Crore, meaning that growth of Nabil in terms of loans and advances is highest among three banks. It is clear that there is higher variation in total loans and advances of GBIME during the study period with highest standard deviation of 11,324.85. There is more consistency in growth of loans and advances of RBB in comparison since there is lowest coefficient of variation i.e. 46 percent in total loans and advances of the bank.

4.2 Ratio Analysis

Financial analysis is the process of identifying the financial strength and weakness of the organization presenting the relationship between the items of balance sheet. For the purpose of this study, ratio analysis has been mainly used any with the help of it, data can be analyzed.

Various financial ratios related to the loans and advances are presented and discussed to evaluate and analyze the impact of NRB directives under the supervision on performance of three banks Rastriya Banijya Bank, Nabil Bank Ltd & Global IME Bank Ltd. Financial ratios are calculated and data is analyzed with the help of those ratios. Some important financial ratios are only calculated from the point of view of the loan and advances, NPL and profitability. The ratios are calculated and analysed to highlight the relationship between financial items and figures. It is a kind of mathematical relationship and procedure dividing one item by another. All of these calculations are based on data obtained from financial statements of respective sample banks. The important and needed financial ratios, which are to be calculated for the purpose of these studies, are mentioned below.

4.2.1 Loan and Advances to Total Assets

Loan and advances is the major portion of the assets of any balance sheet of banks. Loan and advances directly generates income to the bank therefore it is essential to analysis the ratio of loan and advances to total assets. The more the portion of loan and advances in total assets the more the effective utilization of assets of the bank. Granting loan is a risky decision because each loan carries certain level of risk therefore loan and advances are also known as risky assets. Therefore, if Loan and advances to total assets ratio is low it indicates low risk to management and low profitability and vice versa. It is one of the major ratios that NRB focuses while supervising any bank.

Total loan and advance and Total Assets of selected banks can be seen in the table 4 below

Table 4
Loan and Advances to total assets (in percentage)

FY	RBB	Nabil	GBIME
2070-71	49.60	62.70	71.70
2071-72	51.60	56.50	72.60
2072-73	49.10	59.50	66.80
2073-74	61.30	64.20	67.00
2074-75	61.30	70.60	74.20
2075-76	65.40	66.40	75.20
2076-77	58.70	64.70	73.00
2077-78	63.20	70.90	70.20
2078-79	68.70	74.00	75.50
2079-80	61.70	70.50	71.10
Mean	59.10	66.00	71.70
SD	6.70	5.60	3.10
CV	11.40	8.40	4.30

Source: Appendix 1

Table 4 presents the ratio of total loans and advances to the total deposit of the sample banks during the ten year study period. For RBB, the percentage is increasing from FY 70/71 to FY 71/2 then decreasing at 72/73 and then increasing up to 65 percent in FY 75/76 and fluctuate and has reached 62 percent in FY 79/80. For Nabil bank the ratio decreases at first and then increased to 71 percent in FY 74/75. The ratio then fluctuated and returned to 71 percent in FY 79/80. For GBIME bank the percentage increases from FY 70/71 to FY 71/72. It decreased in FY 72/73 and FY 73/74 and increased to 75 percent in FY 75/76. It then fluctuated and reached 71 percent in FY 79/80. There is higher variance in the ratio of RBB bank during the study period with standard deviation of 6.70 percent. There is more consistency in the loan flow of GBIME as compared to total assets since there is lowest coefficient of variation i.e 4.30 percent.

4.2.2 Loan and Advances to Total Deposit (Credit Deposit Ratio)

This ratio determines the proportion of total lending to total deposit ratio. Loan and advances yield high rate of return but liquidity requirement also needs due consideration. Greater ratio implies the better utilization of total deposit and better earning. Hence, 70% to 80% ratio is considered as appropriate.

Table 5
Analysis of Loans and Advances to total deposit ratio (in percentage)

FY	RBB	Nabil	GBIME
2070-71	56.70	72.50	82.30
2071-72	58.00	62.80	83.50
2072-73	55.90	70.90	79.30
2073-74	69.30	77.80	77.50
2074-75	71.40	83.60	87.70
2075-76	77.10	81.30	91.60
2076-77	67.20	79.70	88.20
2077-78	73.60	90.60	85.60
2078-79	87.80	94.20	95.00
2079-80	75.50	84.20	85.20
Mean	69.30	79.80	85.60
SD	10.20	9.30	5.30
CV	14.70	11.70	6.20

Source: Appendix I

Table 5 present the credit deposit ratio of the banks during the ten year study period starting from FY 2070-71 to FY 2079-80. Total lending to total deposit of RBB is not constant. In FY 70/71 the lending is 57 percent increased to 77 percent in FY 75-76 and decreased again in FY 76-77 and then increased again till FY 79-80 to 76 percent. The total lending percentage of Nabil bank is fluctuating throughout the years. Its decreasing at first from 73 percent to 63 percent and fluctuating every year and increasing to 84 percent in FY 79-80. The total loans and advances of GBIME bank increased to 92 percent in FY 75-76 and decreased again and then increased to 95 percent in FY 78/79 and decreased to 85 percent in 79/80. The high percentage i.e 95 percent of GBIME in FY 78/79 suggests that majority of the deposit was utilized as the loan. The average credit deposit ratio of RBB, Nabil and GBIME are 69.30, 79.80 and 85.60 percent respectively. RBB and Nabil have not crossed the threshold of 80% . It is clear that there is higher variation oin credit deposit ration of RBB during the study period with highest standard deviation of 10.20 percent. There is more consistency in the loan flow if GBIME with coefficient of variation of 6.20 percent in credit deposit ratio of the bank.

4.2.3 Analysis of Non-performing Loan Ratio

The ratio determines the proportion of non performing loan to total lending of the bank. High ratio indicates bad effect and decrease in the profitability of the bank and lower ratio indicates better performance and increase the profitability.

Table 6
Analysis of Non-performing Loan Ratio (in percentage)

FY	RBB	Nabil	GBIME
2070-71	6.40	2.20	2.50
2071-72	5.20	1.80	2.20
2072-73	4.30	1.10	1.90
2073-74	3.80	0.80	1.60
2074-75	4.70	0.50	0.80
2075-76	4.60	0.70	0.50
2076-77	4.10	1.00	1.80
2077-78	3.20	0.80	1.40
2078-79	2.10	1.60	1.30
2079-80	3.80	3.40	3.10
Mean	4.20	1.40	1.70
SD	1.20	0.90	0.80
CV	27.50	62.30	45.80

Source: Appendix I

Table 6 presents the non-performing loan ratio of the banks during the ten year study period starting from FY 2070-71 to FY 2079-80. NPL of all bank has been decreasing till FY 2077/78. However, after 2078/79 the NPL ratio of all bank has slightly increased. The decrease in NPL ratio indicates that the impact of supervision has been positive on the banks. However, the increase in the ration in latest year doesn't mean that the impact of supervision has been reduced, rather it seems to be the result of economic environment where interest in lending had reached highest level ie. More than 15%. It resulted in borrowers failing to repay in time hence the increase in NPL.

RBB, Nabil, and GBIME started from 6.38 percent, 2.23 percent and 2.53 percent of NPL in total lending in FY 2070/71 and have been able to decrease the NPL percentage to 2.09, 1.62, 1.67 in FY 2078/79. GBIME have maintained their NPL level very low making 0.54 percent in minimum in FY 75/76 and 3.15 percent in maximum FY 79/80. In average NPL of 10 years Nabil has maintained low NPL level of 1.41percent as compared to other two banks. This indicates that these banks have been making continuous effort to maintain their NPL low. If we compare the NPL of RBB , the ten year average was 4.22 percent but NPL of RBB also gradually decreased till FY 78/89 which shows good loan management by all these banks during this time.. This indicates that the NRB supervision has positively impacted to maintain lower NPL in these banks. The average non performing ratio of RBB is highest among three banks i.e 4. Percent while Nabil has the lowest non performing ratio on average. It indicates Nabil has better adherence to the directives issued by

NRB. It is clear that there is higher variation in non-performing ratio of RBB during the study period with highest standard deviation of 1.20 percent.

4.2.4 Loan Loss Provision to Loan and advances

Loan loss provision to Loan and advances shows percentage of loan is covered against the possible future loss due to nonpayment of loan. Since there is risk inherent in loan and advances, NRB has directed banks to classify its loan and advances into different category and accordingly to make provision for possible losses. Loan Loss provision signifies the cushion against the future contingencies created by the default of the borrower in payment of loan and ensures the continuous solvency of the bank. Since high provision has to be made for non-performing loan, higher provision for loan loss reflects increasing non-performing loan in volume of total loan. The low ratio signifies the good quality of assets in the volume of total loan. It indicates how efficiently it manages loan and advances and make efforts to cope with probable loan loss. Higher ratio implies higher portion of NPL in the total loan portfolio.

Table 7

Loan Loss provision to Loans and Advances (in percentage)

FY	RBB	Nabil	GBIME
2070-71	1.30	2.80	2.90
2071-72	1.10	2.50	2.50
2072-73	1.30	2.10	2.70
2073-74	1.70	1.70	2.30
2074-75	5.00	1.60	1.70
2075-76	4.50	1.60	1.50
2076-77	4.30	2.00	2.50
2077-78	3.60	2.00	2.60
2078-79	3.40	2.50	2.50
2079-80	4.30	3.90	3.80
Mean	3.00	2.30	2.50
SD	1.50	0.70	0.60
CV	50.10	30.90	24.60

Source: Appendix I

Table 7 presents the loan loss provision ratio of the banks during the ten year study period starting from FY 2070-71 to FY 2079-80. The loan loss provision ratio of RBB reached maximum 5 percent in FY 2074-75 and minimum 1.10 percent in FY 2071-72. Similarly, there is maximum and minimum loan loss provision ration of 3.9 percent and 1.6 percent respectively in Nabil in FY 2079-80 and FY 2074-75. Likewise, the minimum loan loss ratio of GBIME is 1.5 percent in FY 2075-76 and maximum 3.8 percent in FY 2079-80. The average loan loss provision of RBB is

highest i.e. 3 percent among three banks while Nabil has lowest i.e. 2.30 percent indicating that the Nabil has better loan management and adherence to NRB directives. It is clear that there is higher variation in loan loss ratio of RBB during the study period with highest standard deviation of 1.5 percent. There is more consistency in loss provisioning of GBIME in comparison since there is lowest coefficient of variation i.e. 24.60 percent in loan loss provision of the bank.

4.2.5 Return on Loan and Advances

Return on loan and advances Ratio indicates how efficiently the bank has employed its resources in the forms of loan and advances. Net profit of a bank largely depends upon interest earn from loan and advances and there is positive correlation between effective utilization of loan and advances and net profit. This ratio measures the bank's profitability with respect to loan and advances. Higher ratios indicate the better performance of the bank and vice versa.

Table 8
Analysis of Return on Loans and Advances (percentage)

FY	RBB	Nabil	GBIME
2070-71	3.00	4.20	2.30
2071-72	6.40	3.20	1.90
2072-73	2.90	3.60	2.30
2073-74	2.70	3.90	2.60
2074-75	3.00	3.50	2.20
2075-76	3.40	3.20	2.40
2076-77	2.80	2.20	1.50
2077-78	1.70	2.20	1.70
2078-79	1.90	1.40	1.80
2079-80	1.50	1.90	1.80
Mean	2.90	2.90	2.10
SD	1.40	0.90	0.40
CV	47.00	32.40	17.90

Source: Appendix I

Table 8 explores the return on loans and advances of the banks during the ten year study period from FY 2070-71 to FY 2079-80. The return on loans and advances of RBB reached maximum 6.4 percent in FY 2071-72 and minimum of 1.5 in FY 2079-80. Similarly, there is maximum and minimum return on loans and advances of 4.20 and 1.40 percent respectively in Nabil in FY 2070-71 and FY 2079-80 respectively. Likewise, maximum return on loans and advances of GBIME is 2.60 percent in FY 2073-74 and minimum of 1.5 percent in FY 2075-76.

The average return on loans and advances of RBB and Nabil is high and equal among three banks i.e. 2.90 percent while GBIME has lowest average return on loans and advances i.e. 2.10 percent. In comparison RBB and Nabil have earned more from utilization of Loans and Advances during the study period. It is clear that there is higher variation in return on loans and advances of RBB during the study period with highest standard deviation of 1.40 percent. There is more consistency in loans and advances utilization of GBIME in comparison since there is lowest coefficient of variation i.e 17.90 percent in return on loans and advances of the bank.

4.2.6 Total Provision to Non-Performing Loan

This ratio determines total loan loss provision held to total non-performing loan. NRB has directed all commercial bank to provide provision for all types of loan and advances. This ratio measures up to what extent of risk inherent in non-performing loan is covered by the loan loss provision of the bank. More than 100% ratio signifies that the bank is safeguard against future contingencies that may create due to bad loans, whereas lower than 100% may create huge provision in coming future due to requirement of high provision to substandard loan and advancers.

Table 9

Ratio analysis of Loan Loss provision to Non-Performing Loan(percentage)

FY	RBB	Nabil	GBIME
2070-71	20.90	123.80	113.80
2071-72	20.90	138.70	114.30
2072-73	29.90	182.00	142.10
2073-74	45.10	217.60	143.40
2074-75	104.90	288.70	219.70
2075-76	97.50	221.20	283.90
2076-77	104.50	200.00	144.60
2077-78	112.30	232.80	183.90
2078-79	163.10	155.30	194.80
2079-80	113.30	114.90	119.70
Mean	81.20	187.50	166.00
SD	48.60	55.00	54.80
CV	59.90	29.40	33.00

Source: Appendix I

Table 9 represents the ratio of loan loss provision to non-performing loan of the banks during the ten-year study period starting from FY 2070-71 to FY 2079-80. The ratio of RBB reached maximum 163.10 percent in FY 2078-79 and minimum if 20.90 in

FY 2070-71. Similarly, there is maximum and minimum ratio of 114.9 percent and 288.70 percent in FY 2079-80 and FY 2074-75 respectively of Nabil Bank. Likewise, maximum ratio of GBIME reached 283.9 percent in FY 2075-76 and reached minimum of 113.8 percent in FY 2070-71. Nabil has highest average ratio of LLP to NPL i.e. 187.50 and RBB has lowest i.e. 81.20 percent over the period. It is clear that there is higher variation in the ratio of Nabil bank since the standard deviation is highest i.e. 55 percent. There is more consistency in the ratio of LLP to NPL of Nabil in comparison since lowest coefficient of variation i.e. 29.4 percent.

4.3 Correlation Analysis

4.3.1 Correlation between Return on Assets, Return on Equity, Return on Loans and Advances, Credit Deposit Ratio, Non-performing Loan Ratio, Loan loss provision Ratio

In this part of data analysis, the relationship of Return on Assets, Return on Equity, Return on Loans and Advances, Credit Deposit Ratio, Non-performing Loan Ratio, Loan loss provision Ratio:

Table 10
Correlation Analysis

Variables	ROA	ROE	ROLA	CD Ratio	NPL Ratio	LLP Ratio	No.I
ROA	1						
ROE	.529** 0.003	1					
ROLA	.949** <.001	.699** <.001	1				
CD Ratio	-.365* 0.047	-.682** <.001	-.603** <.001	1			
NPL Ratio	0.025 0.895	.579** <.001	0.252 0.18	-.683** <.001	1		
LLP Ratio	-0.331 0.074	-.440* 0.015	-0.341 0.065	0.106 0.577	0.331 0.074	1	
No.I	0.35 0.058	.733** <.001	.487** 0.006	-.467** 0.009	0.349 0.059	-0.291 0.118	1

** Correlation is significant at the 0.01 level (2-tailed).

* Correlation is significant at the 0.05 level (2-tailed).

Source: Appendix I

Table 10 reveals the correlation results of ROA and ROE with return on loan and advances, credit deposit ratio, non-performing loan ratio, loan loss provision ratio. The table shows that return on assets has high degree positive correlation with return

on loans and advances with the coefficient 0.949, which means the return on assets of the banks increases when return on loans and advances increases. The high degree positive relation between ROA and return on loan and advances of the banks is significant (i.e. p-value is less than 1 percent) in the population. Return on assets and credit deposits are low degree negatively correlated i.e. -0.365 which means return on assets decreases when Credit Deposit ratio increases. The relation is significant. Return on assets and non-performing loans of the banks are low degree positively correlated with coefficient 0.025. which means that profitability of the bank increases when non-performing loan increases. The relation is insignificant in the population as p-value is higher than 5 percent. In contrast, return on assets of the bank is negatively correlated with Loan loss provision ratio with the coefficient of -0.031 which means the profitability of the bank increases when loan loss provision decreases. The relation is insignificant in the population (i.e p-value 0.895 is higher than 5 percent).

Similarly, table also shows that return on equity has moderate degree positive correlation with return on loan and advances, which means with increase in return on loans and advances there is increase in return on equity. The relationship is significant in the population. Also, the relation between return on equity and credit deposit ratio is negatively correlated with the coefficient of -0.682 . The relation is significant on the population. Similarly, return on equity has moderate positive correlation with non-performing loan ratio of the banks with the coefficient 0.579. This means with increase in NPL there is increase in return on equity. The positive relation between NPL ratio and ROE is significant in the population. In contrast, loan loss provision of the bank is negatively correlated with return on equity with the coefficient -0.440 which means with the increase in loan loss provision ratio there is decrease in return on equity. Since the value of p is less than 5 percent, the relation is significant in the population. Similarly, the correlation between number of NRB inspection and return on assets and return on equity is positive. While the relation with return on asset is insignificant relation with return on equity is significant. There is moderate degree of positive correlation between number of inspection and return on loan and advances i.e. 0.487. It means that with 1 percent increase in NRB inspection there is 0.487 percent increase in return on loans and advances of the particular bank. Also, since the p value i.e. 0.006 is less than 1 percent, the positive relation between NRB inspection and return on loans and advances is significant. Likewise, the correlation between

number of NRB inspection and return on equity is 0.733 which is high degree positive relation. This relation is significant in the population as the value of p is less than 1 percent.

4.4 Regression Analysis

Table 11
Regression Analysis for dependent variable ROA

Variables	Coefficient	Std. Error	t-statistics	p
(Constant)	-0.007	0.003	-2.776	0.011
ROLA	0.602	0.022	27.718	<.001
CD Ratio	0.011	0.003	4.127	<.001
NPL Ratio	-0.041	0.018	-2.263	0.033
LLP Ratio	0.034	0.02	1.657	0.111
No.I	0.00001	0.00008	-1.352	0.189
R squared	0.974			
SE of regression	0.00088			
F-statistics	215.43			
Prob (F-statistics)	<.001			

Source: Appendix I

Table 11 shows multiple regression analysis using return on assets as dependent variable and return on loan and advances, credit deposit ratio, non-performing loan ration, loan loss provision ratio as independent variables. The R^2 value of the regression model is 0.974 which means that 97.4 percent change in assets of the sample banks is explained by independent variables and remaining 2.6 percent change in return on assets is not explained by this regression model. Since the p value of F-statistics of the regression model is less than 5 percent i.e 0.001 the variables in the model are strong enough to explain the change in dependent variable and this shows the goodness of fit of the regression model.

The result reveals that the coefficient of credit deposit ratio is 0.01 which means that credit deposit ratio has negative effect on return on assets of the banks. The negative effect of credit deposit ratio on return on assets is significant since p-value i.e. 0.002 is less than 5 percent. On the other hand, the coefficient of non-performing loan ratio is -0.041 which means that NPL ratio has negative effect on return on assets of the bank. The negative assets of the NPL ratio on ROA is insignificant as p-value is higher than 5 percent. The coefficient also states that 1 percent increase in NPL ratio decreases return on assets by 0.041 percent. Similarly, coefficient of return on loan and advances is 0.602 which is positive. The positive effect of return on loans and

advances on return on assets is significant as p value is less than 1 percent. This means with 1 percent increase in return on loan and advances there is 0.602 percent increase in return on assets. Similarly, there is positive effect of loan loss provision on return on asset. The effect of loan loss provision is insignificant on the population as p-value is higher than 5 percent. There is very low degree positive effect of Number of inspection on return on assets. The effect is insignificant as p-value is higher than 5 percent.

Table 12
Regression Analysis for dependent variable ROE

	Coefficient	Std. Error	t-statistics	p
(Constant)	-0.081	0.141	-0.575	0.571
ROLA	4.611	1.14	4.043	<.001
CD Ratio	0.196	0.144	1.363	0.186
NPL Ratio	6.324	0.94	6.73	<.001
LLP Ratio	-6.977	1.072	-6.51	<.001
No.I	0.017	0.004	3.796	<.001
R squared	0.906			
SE of regression	0.046166			
F-statistics	57.101			
Prob (F-statistics)	<.001			

Source: Appendix I

Table 12 shows the result of multiple regression analysis using return on equity as dependent variable and credit deposit ratio, return on loan and advances, loan loss provision ratio, non-performing loan ratio as independent variables. The R^2 value of the regression is 0.906, which means that 90.6 percent change in return on equity of the sample banks is explained by independent variables and remaining 9.4 percent change in return on equity is not explained by this regression model. Since the p-value of F-statistics of the regression model is less than 1 percent i.e 0.0000 the variables in the mode are strong enough to explain the change in dependent variables and this shows the goodness of fit of the regression model.

The result reveals that coefficient of credit deposit ratio is 0.196 which is low degree positive effect on return on equity. The positive ratio is insignificant in the population as p-value is higher than 5 percent. This states that 1 percent increase in credit deposit ratio decrease the return on equity by 0.096 percent. On the other hand, non-performing loan ratio has coefficient of 6.33 which means with 1 percent increase in NPL ratio the increase in ROE is 6.33 percent. This is significant as the p-value is less than 1 percent. Also, the coefficient of loan loss provision ratio is -6.977 which means

1 percent increase in loan loss provision ratio leads to decrease in return on equity by 6.977 percent. The effect is significant in the population as p-value is less than 1 percent. Similarly, the effect of ROLA on return on equity is positive with coefficient of 4.61. This means one percent increase in ROLA leads to 4.61 percent increase on return on equity. The effect is significant as p-value is less than 1 percent. Similarly, no. of NRB inspection have low degree positive effect on the return on equity of the bank. The effect is significant as the p-value is less than 1 percent.

4.5 Discussion

The lending practices of Rastriya Banijya Bank Ltd., Nabil Bank Ltd., and Global IME Bank Ltd. during the study period revealed that there is more consistency in the growth of loans and advances of RBB in comparison. The loans and advances of all three sample banks are in increasing trend. The increasing trend in overall loans and advances signals towards the adherence of NRB directives by the respective banks. The ratio of loans and advances to total assets of three sample banks over the study period of ten years is consistently growing in case of Global IME bank in comparison to RBB and Nabil. In terms of credit deposit ratio, Nabil has not crossed the threshold of 80 percent and Global IME is way above the threshold of 80 percent on average and RBB has distributed less than 70 percent of deposit as loan and advances during the study period. Average non performing ration of RBB is highest among the three banks i.e 4.20 percent while Nabil has lowest average non performing ratio i.e. 1.40 meaning that Nabil has comparatively better loan management practice than other two banks during the study period. The ratio of loan loss provision is highest for RBB bank during the study period. The lowest average ratio of loan loss provision of 2.30 percent of Nabil bank once more indicates the better management of loan and advances by Nabil bank in comparison to other two banks during the study period.

Return on loans and advances for both RBB and Nabil is 2.90 percent in average during the study period which is better than the average 2.10 percent of GBIME bank. ADBL and Nabil have earned more from utilization of loan and advances during the study period as compared to GBIME bank. Total provision to Non performing ratio of RBB in average is just 80 percent, which indicates the risk that the losses if occurred due to loan loss may not be covered by the provision. The loan and advances of RBB

appear to be risky in average as compared to the loan and advances of Nabil and GBIME bank.

The relationship analysis found that there is high degree positive and significant correlation between total loans and advances and total assets of commercial banks. It indicates the increase in loans and advances leads to increase in total assets and vice versa. It also shows positive and significant correlation between Non-performing loan, loan loss provision and net profit of the bank and its total loans and advances. It indicates that positive changes in each component results in positive changes in total loans and vice versa. Non- performing loan ratio and return on loans and advances have low degree positive correlation between them but it is not significant in the population which is consistent with the finding of Shah (2023) who had found positive correlation between Return on asset of the banks and non-performing loan.

The relationship analysis found that return on assets has low degree negative relation with credit deposit ratio and this result is opposite with the finding of Shah(2023) who found the relation to be positive. On the other hand return on equity has negative relation with credit deposit ratio with the coefficient -0.682 and Shah(2023) also found negative relation between credit deposit ratio and return on equity. The relation between number of inspection and return on equity is found positive with coefficient 0.733 . which is similar with the findings of Boubacar (2023) who found positive relationship between supervision and bank performance.

Return on assets and Return on Equity of the banks and non-performing loan are positively correlated with the coefficient 0.025 and 0.579 respectively and the result is not consistent with the finding of Shrestha (2017) but consistent with the finding of Shah (2023). The relation between return on asset and NPL is not significant which is similar to the finding of Boudriga (2009) who did not find any evidence of the relationship between NPL and ROA.

In contrast, return on assets has negative correlation with loan loss provision with coefficient 0.331 . Return on equity also has negative correlation with loan loss provision with coefficient 0.440 which is significant in the population. The relationship analysis between NRB inspection and return on loans and advances found that there is moderate degree positive correlation between NRB inspection and return on loans and advances. The relationship is also significant in the population. This

result is consistent with the results obtained by Boubacar (2023) who found that there is positive relationship between banking regulation and bank performance. The result is also consistent with the findings of Abdennour et. all (2010) who found that supervision differences significantly impact profitability. Similarly, Hirtle et. All (2019) found that there is distinct role of supervision in mitigating banking sector risk. The relationship analysis shows that the impact of NRB inspection on Return on Loans and advances is significant.

The regression analysis found that credit deposit ratio has significant positive effect (0.011) on return on assets of the banks and the result is consistent with the findings of Risal and Poudel (2020) . Similarly, non performing loan has negative effect on ROA which is significant. The finding is consistent with the finding of Charles (2013), Shrestha (2017), Risal and Poudel (2020), Yeasin (2022) and Boudriga (2009). Whereas, this study reveals that the effect of loan loss provision on return on assets is positive and insignificant which is in line with the analysis of Bouheni(2013). The regression analysis also reveal the positive effect of number of NRB inspection on return on assets but the effect is not significant. This finding is in line with the finding of Boudriga(2009) who emphasizes that rather than concentrating on supervisory aspects, efficient strategy is to improve lending practices.

Another regression analysis revealed that credit deposit ratio has positive effect on return on equity of the bank which is consistent with the result of Risal and Poudel (2020), who revealed that increasing credit deposit ratio increases earnings and profitability of the bank. Non-performing loan ratio has positive effect on return on equity. This result is inconsistent with the finding of Shah (2023). The regression analysis also shows that loan loss provision ratio has negative effect on return on equity with coefficient 6.97. This effect is significant. The finding is in line with the study of Bouheni (2013). The return on loan and advance has positive effect on return on equity with coefficient 4.62 which is significant. Similarly, number of bank supervision has positive effect on return on equity and the effect is significant. This finding is consistent with the finding of Boubacar (2023) who found the positive effect of supervision on the lending practices of the bank.

Chapter V

Summary and Conclusion

5.1 Summary

This research is aimed at studying about the NRB Supervision through directives and its impact on the lending practices of commercial banks of Nepal. In first chapter, the study deals about basic assumption of the study. Basically, it highlighted the concept and importance or significance of the study. It also presents research issue, research problems, and basic objectives of the study, rationality of the study, Limitation of the study. Second chapter helped to cast light upon the development and progress made by the earlier researcher on the concerned field or similar topic of the study. It also tried to know some concepts used in this study. Moreover, it reviewed and summarized the finding of the previous studies to provide knowledge about the background of the work done by them and to stop the duplicity of the previous work.

Third chapter of the study discussed about the various research methodologies used for the study. Basically, research methodology here signifies the research design, source of data, population and sample of data, data collection techniques, data collection methods and tools etc. For this purpose, descriptive cumulative analytical research design was adopted. Out of total population of 20 commercial banks, 3 banks were taken as sample using purposive sampling method. The selected major commercial banks are RBB, Nabil and GBIME. Secondary data have been used in the study, annual reports and other publications form the basis of secondary data. Beside this, newspapers, relevant thesis, journals, articles, related websites etc. are also taken for this research. Data collected from various sources is systematically recorded and presented in forms consistent with tables and graphs and can also be used for mathematical, statistical, financial and graphical purposes for data analysis. The data obtained of 10 consecutive years from FY 2070-71 to 2079-80 of three selected banks have been analyzed to meet the objectives of the study. This study includes analysis tools as different financial ratios relating to loan management of banks, descriptive statistics, correlation analysis and multiple regression analysis. The regression analysis is major factor of this research to make this study different than from other study done in this topic before. The regression model tries to fulfill the gap o the

study on exact impact of number of NRB inspection, credit deposit ratio, non-performing loan ratio, loan loss provision ratio on profitability of the sample banks. Based on the several articles and journals, appropriate variables were selected for the analysis. Each of the variables were properly defined. For the data analysis excel and SPSS software are used in the study.

For the reliable result of the study, 10 years secondary data has been analyzed, interpreted and discussed. Based on financial and statistical tools, this study shows the statistical significance level between the dependent and independent variables of the commercial banks in Nepal.

This study while analyzing supervision, lending practices and profitability of the Rastriya Banijya Bank Ltd., Nabil Bank Ltd. and Global IME Bank Ltd. during the study period found that there is more consistency in the growth of loans and advances of RBB in comparison. Nabil has not crossed the threshold of 80 percent credit deposit ratio and RBB has distributed less than 70 percent of deposit as loan and advances during the study period. The average non performing loan ratio of RBB is highest during the study period i.e. 4.20 percent while Nabil has the lowest i.e. 1.40 percent.

While analyzing the relationship between loan and advance and non performing loan, the relation is found to be positive by their correlation coefficient. It points out the fact that the changes in each variables are taking place in the same direction i.e. the increase in total loan is supported by an increase in non-performing loan. The correlation coefficient between number of NRB supervision and return in equity and return on loan and advances are positive and significant. It indicates that the effect of NRB supervision on loans and profitability of the bank is positive and significant. This finding is similar to the finding of Boubacar (2023). The interpretation of regression model concludes that there is positive effect of number of NRB inspection on return on equity and return on assets. The effect on return on equity is significant.

In the final chapter of the study, the chapter briefly explains the summary of the study and tries to fetch out conclusions and attempts to show the implications of the study to other users of this research study. This study mainly focused on the implementation of NRB directive through NRB supervision by analyzing the sanction of loan and advances, maintenance of loan loss provisions, relation between NRB inspection and

return on loan and advance. Among 20 commercial banks, 3 banks have been selected as the sample. The required data has been collected either from the annual report of the banks or Nepal Rastra Bank. All banks have been selected on the basis of total assets and close competitors to carry out the study.

5.2 Conclusion

The analysis of supervision and lending practices (loans and advances, loan loss provision, Non-performing loan) of RBB, Nabil and GBIME bank conclude that the credit flow of the banks is quite consistent during the study period. Although there is higher non-performing loan in the starting years, banks have managed enough fund as provision against non-performing loans which makes lower credit risk of the banks. The profitability of the banks in terms of return on loans and advances conclude that there is consistent return on loans and advances of the banks. The relationship analysis concludes that Non-performing loan, loan loss provision, total assets, total deposits, net profit all have positive significant relation with loans and advances of the banks. NRB supervision impacts on the loan loss provision and non-performing loans while considering loans and advances of the bank. Since, loan loss provision and non-performing loan have positive relation with loans and advances of the bank, we can conclude that NRB supervision has positive correlation with loans and advances of the banks.

The effect analysis in the study conclude that NRB inspection (supervision) has significant positive effect on the lending practices of the commercial banks. Since the relationship between NRB inspection and return on loan and advances, return on assets and return on equity of the commercial banks in positive and significant, we can conclude that NRB supervision has positive impact on the lending practices of the commercial banks.

The study also shows that NRB supervision has impact on the policy development of the commercial banks which ultimately impacts the lending practices of the banks. The loan policies are developed on the basis of directives issued by NRB. Various procedures involved in the lending practices are based on directives and circulars issued by NRB, hence we conclude that supervision has significant impact on the lending practices of the commercial banks.

5.3 Implications

The findings of the study have following major implications to management. Policy makers, investors and researchers who are interested on related field.

- Almost all banks have more than 60% of their assets in the form of loans and advances and loans and advances itself is the major earning assets of the banks. Therefore, management should be very cautioned while disbursing loan. As ‘one bad loan can wipe out the profit from hundred good loans’ therefore before providing loan viability of business as well as financial status of borrower and their repaying capacity should be closely analyzed.
- To maintain the high profitability of the banks, strong credit risk and loan service process management must be adopted which helps to maintain the level of NPL as low as possible.
- Banks should focus on managing the important variables of credit risk so as to ensure that no stakeholders of the banks should face any disadvantageous situation regarding loan management.
- As per NRB directives, banks should divide their loans and advances into two parts, performing and non-performing loans and the loan are required to make provision as per the category of each loan. Since, these directive have created great control measure and safeguard to depositor and other stakeholders of the banks, banks should strictly follow the directives. In addition to these, loan loss provision provide safeguard against the future contingencies which may be created due to non payment of loan in future. Management should provide adequate loan loss provision as per NRB directive to save the banks from possible future losses
- Banks should properly follow the guidelines, directives, circulars issued by NRB and strictly implement and respond to the issues observed during supervision.
- Further, this study is also hoped to be useful to academicians as a source of knowledge for further research. The study is concentrated only on factors related to loans and advances and thus, further study should be carried out on

the topic to point out the other factors that enhance mitigation of loan management to improve performance of Nepalese commercial banks

- Banks need to reduce their loan loss provisions by investing their funds in less risky assets. Reducing loan loss provisions results in increase in the banks profit and also increase the banks goodwill thereby increasing market share price of banks.

This study will help the bank members, Board of directors of sample banks to analyze the impact of loan and advance on the financial performances of the banks. This study will also help students, researchers, scholars as well as common people providing some valuable information about financial performances of the banks. So, this study will be helpful to those who are curious to study in further detail and widely in this area.

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Appendix I

Loan and Advances of sample commercial bank

FY	Loan & Advances		
	RBB	Nabil	GBIME
2079-80	24294	33941	37435
2078-79	22672	31057	27221
2077-78	19597	20662	24244
2076-77	15652	15389	20000
2075-76	14812	13356	11406
2074-75	12087	11362	9337
2073-74	10643	9247	7896
2072-73	8178	7821	5921
2071-72	7207	6550	5022
2070-71	6085	5469	4301

Source: Annual Reports of RBB, Nabil and GBIME.

Total Assets of sample commercial banks

FY	Total Assets		
	RBB	Nabil	GBIME
2079-80	39402	48120	52688
2078-79	33024	41982	36053
2077-78	30999	29124	34542
2076-77	26677	23768	27387
2075-76	22641	20114	15165
2074-75	19733	16097	12584
2073-74	17354	14401	11789
2072-73	16643	13134	8868
2071-72	13956	11598	6918
2070-71	12256	8727	6001

Source: Annual Reports of RBB, Nabil and GBIME.

Total Deposits of sample commercial banks

FY	Total Deposit		
	RBB	Nabil	GBIME
2079-80	32165	40312	43934
2078-79	25814	32958	28656
2077-78	26620	22798	28334
2076-77	23298	19304	22664
2075-76	19199	16437	12449
2074-75	16933	13598	10651
2073-74	15358	11889	10191
2072-73	14621	11027	7468
2071-72	12422	10424	6017
2070-71	10727	7539	5229

Source: Annual Reports of RBB, Nabil and GBIME.

Loan Loss provision of sample commercial banks

FY	Loan Loss Provision		
	RBB	Nabil	GBIME
2079-80	1038	1323	1410
2078-79	773	781	676
2077-78	711	405	629
2076-77	668	302	509
2075-76	663	219	176
2074-75	602	179	156
2073-74	181	161	185
2072-73	104	162	162
2071-72	79	165	128
2070-71	81	151	124

Source: Annual Reports of RBB, Nabil and GBIME.

Non-performing Loan of sample commercial banks

FY	Non-Performing Loan		
	RBB	Nabil	GBIME
2079-80	916	1151	1178
2078-79	474	503	347
2077-78	633	174	342
2076-77	639	151	352
2075-76	680	99	62
2074-75	574	62	71
2073-74	401	74	129
2072-73	348	89	114
2071-72	378	119	112
2070-71	388	122	109

Source: Annual Reports of RBB, Nabil and GBIME.

Net profit of sample commercial banks

FY	Net Profit		
	RBB	Nabil	GBIME
2079-80	360	640	669
2078-79	429	425	495
2077-78	342	452	416
2076-77	437	346	290
2075-76	505	424	276
2074-75	365	398	210
2073-74	290	361	206
2072-73	235	281	138
2071-72	464	209	96
2070-71	183	232	97

Source: Annual Reports of RBB, Nabil and GBIME.

Number of NRB inspections of sample commercial banks

FY	No. of inspection		
	RBB	Nabil	GBIME
2079-80	2	3	2
2078-79	2	2	3
2077-78	0	0	1
2076-77	1	2	1
2075-76	2	3	1
2074-75	2	1	4
2073-74	1	2	0
2072-73	1	6	6
2071-72	9	6	4
2070-71	10	3	2

Source: Annual Report of BSD, Nepal Rastra Banks.

Return on Equity of sample commercial banks

FY	Return on Equity		
	RBB	Nabil	GBIME
2079-80	0.07095	0.11700	0.14190
2078-79	0.14015	0.09800	0.13930
2077-78	0.11929	0.15200	0.13530
2076-77	0.18975	0.13610	0.12880
2075-76	0.23390	0.17760	0.18470
2074-75	0.19140	0.20940	0.16190
2073-74	0.27672	0.22410	0.19330
2072-73	0.27294	0.25610	0.16990
2071-72	0.69461	0.22730	0.13000
2070-71	0.76569	0.27910	0.16000

Source: Annual Reports of RBB, Nabil and GBIME.

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