

CHAPTER 1

INTRODUCTION

1.1 Background

The word 'bank' came from the different words of different languages. Some of the words are Italian word 'banco' and 'banca', Latin word 'bancus' and French word 'banque' meaning 'bench' on which the bankers would keep money and all records. Banks are the business houses established to safeguard peoples' money. Banks use the money deposited to give out as loans and for other investments. Banks provide an easy way to pay bills through current account mostly known as cheque account. Money that is deposited in bank accounts earns additional amounts for depositors in terms of interest. Banks provide many services such as accepting various types of deposits, safeguarding deposits, giving out loans, providing means of payment, electronic banking and other services such as money orders, Draft, Promissory Notes, Bill of Exchange, traveler's cheque, Telex Transfer and SWIFT Service etc. It also provides services that don't involve real money like **Letter of Credit** and Guarantees. There are several authors defining the term bank in their own way. Some of the definitions are:

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

According to Sayer, "Ordinary banking business consists of changing cash for bank deposit for cash, transferring bank deposit from one person or another giving bank deposit in exchange for bills of exchange, government bonds, the secured or unsecured promises of businessman to repay etc."

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

Development of Modern Banking

With reference to historical undertakings, the origination of modern banking took place in medieval Italy, despite of strong Christian prohibitions against usury (the charging interest) according to the canon law. By the twelfth and thirteenth century Florence, Genoa and Lucca had become the centre of finance and trade.

The first bank called “Bank of Venice” was setup in the year 1157 A.D. to finance the monarch during wars. Then came “The Bank of Barcelona” which was established in 1401 A.D. and “Bank of Genoa” in 1407 A.D. . Through this the banking concept slowly spread to the rest of the Western Europe.

The bankers migrated to England and other parts of the country from Italy and spread the idea of modern banking in general. Their contributions are considered highly significant for the development of modern banking. The Bank of England was founded in 1694 A.D. through which the growth of the bank accelerated with the Banking Act, 1833 A.D. in United Kingdom. In terms of popular category, Bank of Amsterdam held a prestigious position and has even been claimed responsible for modern day stock exchange as well.

History of Banking in Nepal

In our country, the banking industry has always been acting as a major force towards economic development and enhancing the financial market. This industry in our country has always been a reason for economic prosperity. Banking industry is completely service-oriented, and from decades has been providing various kinds of banking services and facilities.

Like in the other countries, goldsmiths, merchants and moneylenders were the ancient bankers of Nepal. In ancient time private moneylenders used to grant loan to public. For granting loan, they used to charge very high interest rates. Therefore, they frequently failed

to pay back the loan, their securities used to be forfeited, and people were exploited. At that time, there were no organized institution to fulfill the need of the money; people were compelled to depend on private moneylenders.

During the tenure of King Jayasthiti Malla, around 14th century, people were divided into 64 groups. TANKADHARI is one of them who dealt with lending of money to the people. As the main objective of the TANKADHARI was to earn profit from the higher interest charged.

In order to protect people from exploitation, Prime Minister Ranodip Singh established TEJARATH ADDA in the 19th century. The TEJARATH ADDA was responsible for providing loans to the people working in the government office based on the security and the public based on collateral. It was the first step towards the institutional development of banking in Nepal. TEJARATH ADDA was not able to satisfy the needs of public, as it did not accept deposits from them.

Thus the government felt the need of organized institution to provide banking services and established Nepal Bank Limited in 1937 A.D. as the first bank of Nepal. Nepal entered the modern banking system from this period and is known as the golden age in the history of banking. Nepal Rastra Bank (NRB) was established in 2013 Baishak 14th (1956 A.D.), as the Central Bank under NRB Act 2012 B.S. The main function of the Central Bank was to supervise banking industry and to guide the basic monetary policy of the nation. NRB's major aims were to regulate the issue of paper money, secure countrywide circulation of Nepalese currency, achieve stability in its exchange rate, mobilize capital for economic development and for trade and industry growth, develop the banking system in the country thus ensuring the existence of banking facilities and maintaining the economic interests of the public. NRB was also to oversee foreign exchange rates and foreign exchange reserves.

The total numbers of commercial banks existing in Nepal are:

Table 1

Banks	Year of Establishment
1) Nepal Bank Ltd	1937 A.D
2) Rastriya Banijya Bank Ltd.	1966 A.D
3) Nabil Bank Ltd.	1984 A. D
4) Nepal Investment Bank Ltd.	1986 A. D
5) Standard Chartered Bank Nepal Ltd.	1987 A. D
6) Himalayan Bank Ltd.	1993 A. D
7) Nepal SBI Bank Ltd.	1993 A. D
8) Nepal Bangladesh Bank Ltd.	1994 A. D
9) Everest Bank Ltd.	1994 A. D
10) Bank of Kathmandu Ltd.	1995 A. D
11) Nepal Credit and Commerce Bank Ltd.	1996 A. D
12) Nepal Industrial and Commercial Bank Ltd.	1998 A. D
13) Lumbini Bank Ltd.	1998 A. D
14) Machhapuchhre Bank Ltd.	2000 A. D
15) Kumari Bank Ltd.	2001 A. D
16) Laxmi Bank Ltd.	2002 A. D
17) Siddhartha Bank Ltd.	2002 A. D
18) Agriculture Development Bank Ltd.	
19) Global Bank Ltd	2006 A. D
20) Citizen Bank Ltd.	2007 A.D
21) Prime Commercial Bank Ltd.	2007 A.D
22) Bank of Asia Ltd.	2007 A.D
23) Sunrise Bank Ltd.	2007 A. D
24) Development Credit Bank Ltd.	
25) NMB Bank Ltd.	
26) Kist Bank Ltd.	2009 A.D

SOURCE : Nepal Rastra Bank.

In the mid-1980s, three foreign commercial banks opened branches in Nepal. The Nepal Arab Bank co-owned by the Emirates Bank International Limited (Dubai), the Nepalese government and the Nepalese public. The French partners, Rastriya Banijya Bank, Rastriya Beema Sanstha (National Insurance Corporation), and the Nepalese public jointly owned the Nepal Indosuez Bank. Nepal Grindlays co-owned by a British firm called Grindlays Bank, Local financial interests, and the Nepalese public, which now is known as Standard Chartered Bank Nepal Limited. In 1993 A.D., Himalayan Bank Ltd was established under a joint venture with Habib Bank Ltd of Pakistan and Nepal SBI under a joint venture between employee's provident fund and SBI. In 1994 A.D., Nepal Bangladesh Bank Ltd established under a joint venture with IFIC Bank Ltd of Bangladesh. After 1995 A. D Bank of Kathmandu, Nepal Credit and Commerce Bank Ltd, NIC Bank, Lumbini Bank, Machhapuchhre Bank Ltd, Kumari Bank Ltd, Laxmi Bank Ltd, Siddhartha Bank Ltd, and very recently Global Bank Ltd, Prime Bank Ltd., Sunrise Bank Ltd., Bank of Asia has also came in operation.

1.2 Statement of the Problem

In the past, people used to buy or sell any goods and commodities in the shops or market in the physical presence of both the buyer and seller. Payment may be done at the same time or may be after certain time period as per the understanding of both parties. However the industrialization gave birth to present foreign trade where goods and services are bought and sold from one country to another. When goods are bought and sold abroad then such transactions could become very complicated for a number of reasons like time hazard of journey, custom formalities, import/export and exchange control regulations etc, and the fact that buyer and seller are most likely in opposite sides of this world and two parties may not have even seen each other and their business standing and integrity.

Hence, it becomes indispensable for the existence of some means that will protect the interest of both parties while practicing such transactions. The buyer should know what he is getting for the money that he paying. And on the other hand, the seller would definitely be interested in receiving prompt payment. Hence in order to satisfy both the parties, “Letter of Credit” (L/C) was developed. L/C is written instrument issued by the bank (The issuing bank) on the behalf of the buyer (The applicant) in favor of the seller expressing its definite undertaking to effect payment for the specific amount, provided the seller (beneficiary) complies with the terms and conditions stipulated in the letter.

L/C often called ‘Documentary Credit’ is one of the most widely used and universally accepted means of conducting commercial transaction. L/C mechanism provides security to both the buyer and seller. The seller can demand the payment from the issuing bank after presenting the required documents. Sellers also have option to avoid shipment of goods, when he feels that any term and condition not met. On the other hand, buyer also have the right to put any terms and conditions in the L/C. If the document does not fulfill his terms and conditions, he has the option to reject the document. This report studies all the aspects involved in the process of ‘Letter of Credit Business’ in the context of Nepal Investment Bank Ltd. Thus the problems specifically related to the subject are briefly presented as under.

1. Is Nepal Investment Bank Ltd (NIBL) performing up-to-the expectation as it has targeted in terms of its L/C business?
2. Is the existence of the ‘Letter of Credit’ benefiting the organizations that are involved in the International Trade?
3. Is ‘Letter of Credit’ truly a financial instrument while making payment without receiving the goods from abroad?
4. Is the Central Bank monitoring the L/C operations of the commercial banks in order to control money laundering?
5. What are the pre-requisites for opening L/C in NIBL?

6. What are the procedures of opening L/C in NIBL?
7. What are the problems existed during the L/C transactions in NIBL?

1.3 Objectives of the study

The objective of this study is to study all the aspects of the Letter of Credit transaction and to examine how it facilitates the International Trade in today's world. The basic objectives are:

1. To examine the pre-requisites of Letter of Credit business.
2. To assess the processes and operations in respect to Letter of Credit.
3. To evaluate the benefits of L/C.
4. To find out the trend of L/C operations.
5. To identify the problems in L/C operations.
6. To make suggestion and recommendations based on the study.

1.4 Significance of the study

In today's world, due to high competition in the business sector, import and export plays a vital role in every country. But it is very risky to send money directly from a buyer of one country to a seller in another. So the '**Letter of Credit**' is a guaranteed mean of payment for both buyer and seller. Being a developing country, Nepal must do import and export transaction through a safe mean and the L/C is a very important tool for the same. It is due to this reason this report is prepared and also to aware general public moreover to the people or entrepreneurs who are trying to start or already engaged in the import export business.

Letter of credit is one of the most important financial instrument in today's industrial world. L/C is a guarantee that the Bank provides on behalf of its customer (buyer) to any supplier of the goods that upon delivering the goods to the buyer, the supplier will promptly get the payment. Generally, while importing goods from one country to another it takes around 3 to 4 weeks depending on the means of transportation. There are of course other means of payment like Telex Transfer or Draft, but If the payment is made via Telex Transfer or Draft, the buyer has to pay cash now and receive the goods only after 3 to 4 weeks days. This unnecessarily blocks his fund for that period which he may use for some other purpose. If the same transaction is done through a Bank's L/C, the buyer has to deposit normally only 5% to 10% of the total value of the goods to be imported, (this is called margin or cash 'Margin') which gives him opportunity to use the fund until he physically receives the goods. But 'Margin' depends upon the creditworthiness of the customer. Bank may ask the buyer to provide some other collateral along with the 'Margin' if it is not sure about the creditworthiness of the buyer. But whatever the arrangement It's confirmed that the client will pay the remaining amount only after he received the goods and It's also confirmed that he use his fund for 3 to 4 weeks for some other purpose. This is an important aspect of 'Letter of Credit'.

1.5 Limitations of the study

This report is prepared simply in Partial fulfillment of the requirement for the degree of Masters of Business Studies (MBS). The limitations are as follows:

Duration of the study:

This thesis writing is the part of academic requirement of MBS. The report is to be completed in the stipulated time. Hence the duration of the study is not sufficient to make the study more realistic and wide.

Data availability:

This study is based on the secondary data source such as annual report of the concerned bank, and other related journals, magazines, books. Moreover there are not much written articles or books available in the market on Letter of Credit. Also the up-to-date and complete data were very difficult to obtain from the bank due to inability of concerned authorities to provide the required data. Moreover the bank did not provide some data that they considered as its business secrecy.

Period Covered:

The present study is undertaken for a period of Five years from F.Y. 2003/04 to 2007/08 .The secondary data are collected form annual general meeting's (AGM)'S report and this is the basis to express the Strength and weakness concerned to the International Trade Finance specially L/C business of NIBL. Hence the conclusion drawn, confines only to the extent of above period. Data for the current FY is not available yet.

1.6 Organization of the study

This study has been divided into five chapters to make the study more systematic. It consists of Introduction, Review of Literature, Research Methodology, Presentation and analysis of data and last summary, conclusion and recommendation.

Chapter 1. Introduction

The first chapter includes background, statement of problems, objectives limitation and organization of study.

Chapter 2. Review of Literature

The second chapter includes the conceptual framework of the topic letter of credit and the profile of the bank and reviews the issues related to the study.

Chapter 3. Research Methodology

The third chapter is concerned with the research methodology consisting of research design, Methods of data collection, & Tools of Data analysis etc.

Chapter 4. Presentation and Analysis of Data

The fourth chapter presents the presentation and analysis of the performance of Nepal Investment Bank Ltd in terms of Import L/C, Export L/C, and Income from Commission on L/C transaction.

Chapter 5. Summary of findings, Conclusion and Recommendation

The fifth and final chapter consists of summary of findings, conclusion and recommendation and various suggestions for the improvement of future performance of Nepal Investment Bank Ltd.

CHAPTER 2

REVIEW OF LITERATURE

Review of literature comprises of previous research study articles concerned with this study and other studies with a view for supplement the present research and such review adds to the dimension of the study. This chapter deals with review of books, review of reports, review of research papers, review of articles, review of Unpublished Publication etc.

2.1 Conceptual Framework

Letter of credit is widely used instrument in the field of international trade. It is basically a mechanism, which allows importers/buyers to offer secure terms of payment to exporters/sellers in which a bank (or more than one bank) gets involved. The need of L/C generally arises whenever any two parties (i.e. exporter and importer) get into contract to buy and sell something. As the buyer and seller are far away from each other and may not know each other. Therefore, the issue of confidence or credit worthiness arises. A party will always think from negative view i.e. the other party might default. Such problems between both the parties have been resolved after introduction of “Letter of Credit” in the trade.

The operations of L/C are governed by UNPDC (Universal Custom and Practice in documentary credit) on force published by ICC (International Chamber of Commerce). The popularity and reliability of the L/C is such that in the present day scenario, one cannot visualize of foreign trade as well as of domestic trade without the presence of L/C.

The ICC Banking commission has designed some common code of practice having wide application and uniform interpretation. The ICC established in 1920 at Paris and the UCPDC is the joint effort of the bankers, transporters, insurance companies,

buyers, sellers etc. The UCPDC shall apply to all Documentary Credits. They are binding on all parties thereto, unless otherwise stipulated in the credit.

2.1.1 Meaning of Letter of Credit

Letter of credit is written instrument issued by the bank (The issuing bank) on the behalf of the buyer (The applicant) in favor of the seller expressing its definite undertaking to effect payment for the specific amount, provided the seller (beneficiary) complies with the terms and conditions stipulated in the letter.

L/C often called 'Documentary Credit' is one of the most widely used and universally accepted means of conducting commercial transaction. L/C mechanism provides security to both the buyer and seller. At the very outset one must understand is that Letters of credit deal in documents, not goods. The idea in an international trade transaction is to shift the risk from the actual buyer to a bank. . The seller can demand the payment from the issuing bank after presenting the required documents. Sellers also have option to avoid shipment of goods, when he feels that any term and condition not met. On the other hand, buyer also have the right to put any terms and conditions in the L/C. If the document does not fulfill his terms and conditions, he has the option to reject the document.

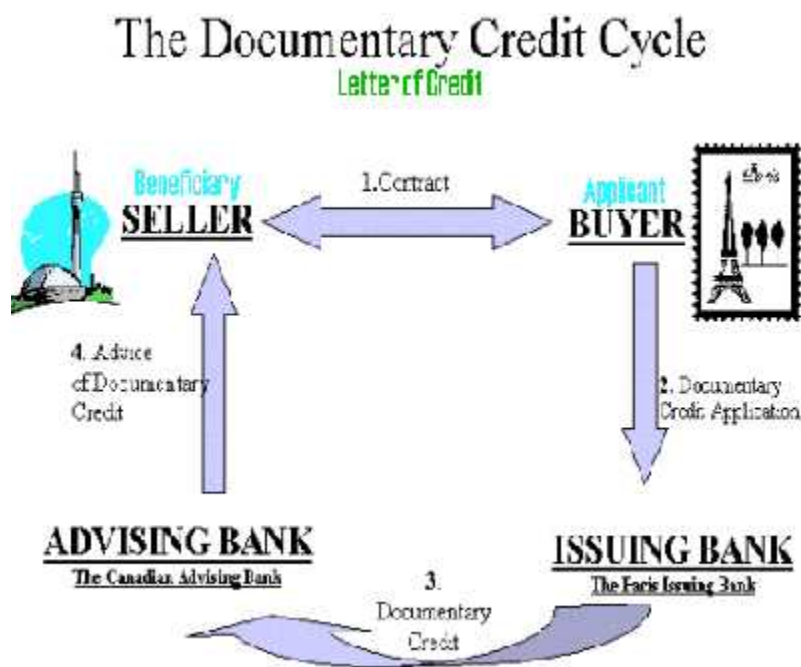
Thus a L/C (as it is commonly referred to) is a payment undertaking given by a bank to the seller and is issued on behalf of the applicant i.e. the buyer. The Buyer is the Applicant and the Seller is the Beneficiary. The Bank that issues the L/C is referred to as the Issuing Bank which is generally in the country of the Buyer. The Bank that Advises the L/C to the Seller is called the Advising Bank which is generally in the country of the Seller.

The specified bank makes the payment upon the successful presentation of the required documents by the seller within the specified time frame. Note that the Bank scrutinizes the 'documents' and not the 'goods' for making payment. Thus the process works both in

favor of both the buyer and the seller. The Seller gets assured that if documents are presented on time and in the way that they have been requested on the L/C the payment will be made and Buyer on the other hand is assured that the bank will thoroughly examine these presented documents and ensure that they meet the terms and conditions stipulated in the L/C.

Letter of credit in effect is a guarantee to the exporter from the bank that he will receive the payment if the terms and conditions of the L/C are complied with and simultaneously assures the importer that he will receive the goods for which payments has been assured.

2.1.2 Parties Involved In Letter Of Credit



1. Applicant: An applicant is the one who requests his bank to issue a letter of credit in favor of an exporter to cover the purchase of goods and agrees to pay as per the terms of the contract/L/C. He should furnish the documents to the issuing bank as required to issue the L/C and abide by the rules and regulations mentioned in the contract. The

applicant should be well aware of the status of the beneficiary and understand the terms and conditions mentioned in the underlying contract.

2. Issuing Bank: The issuing bank is the bank, which issues L/C on behalf of the applicant. It is the customer's bank. The buyer mentions the term and condition of the credit to issuing bank. The issuing bank should ensure that the regulatory conditions are fulfilled and the instructions are precise and specific. The issuing bank will select a bank in the exporter's country to act as its agent, and will notify that the credit been opened.

3. Advising Bank: The advising bank is the correspondent situated in the place where the seller is situated. It is the bank where credit has sent. The advising bank gives message to the seller about the opening of credit in his favor through a cable message.

4. Settlement Bank: The Settlement bank is the bank, which negotiates the bills of exchange or drafts under the L/C. It is the bank where sellers present document for settlement. Generally, the same bank acts as the notifying bank/negotiating bank. This bank must see carefully that the documents are strictly according to the terms and conditions of the credit.

5. Confirming Bank: Sometimes the sellers insist that a bank in his own country must confirm credit. Bank giving confirmation is known as confirming bank. Here, one of the merits from seller point of view is that he can receive the payment as soon as documents are presented at his own center.

6. Beneficiary: The beneficiary or seller is the exporter of goods or merchandise. He is the beneficiary of the L/C. The issuing bank makes assumptions that the terms and condition mentioned in the credit should be strictly followed and relevant documents

produced. The exporter ships the goods before the credit expires and sends the shipping documents to the agent bank, which checks the document against the condition and pay him; or they may ask to draw a bill of exchange on them; and will discount the bill for him so that he can get his money immediately.

2.1.3 TYPES OF LETTER OF CREDIT

1. Revocable and irrevocable:

The Applicant (buyer), usually with the prior agreement of the Beneficiary (seller), requests its bank to issue the Letter of Credit in either a revocable or irrevocable form.

A Revocable Letter of Credit may be amended or canceled by the Issuing Bank at any time with or without prior notice to, or agreement of, the Beneficiary. In its function, the Revocable Letter of Credit is not an assurance of payment, but rather provides the buyer and the seller with a means of settling payments. Because a Revocable Letter of Credit may be canceled or amended without prior notice to the Beneficiary, the Beneficiary should not depend on a Revocable Letter of Credit for financial protection. The Beneficiary must have faith that the Applicant will abide by the underlying contract of sale or other agreement, and will not instruct the Issuing Bank to revoke its Letter of Credit. The convenience afforded the Beneficiary under a revocable letter of credit is that payment to the Beneficiary will be made by the bank nominated to pay in the Letter of Credit and on which the draft is drawn (Paying Bank), provided that the documents comply strictly with the Letter of Credit and that the Letter of Credit has not been revoked. Once the payment is made by the Paying Bank, the obligation of the Issuing Bank to reimburse the Paying Bank, if not previously revoked, becomes irrevocable. The Paying Bank is thus protected and will receive funds from the Issuing Bank in accordance with the Letter of Credit.

An Irrevocable Letter of Credit is a definite undertaking by the Issuing Bank to pay, provided the Beneficiary complies strictly with the Letter of Credit. The Letter of Credit

cannot be amended or canceled without the consent of the Issuing Bank, the Confirming Bank (if the Letter of Credit is confirmed) and the Beneficiary. Citibank's obligation to pay is set forth at the bottom of the undertaking. The Beneficiary holds the undertaking of Citibank (in addition to that of the Applicant), but does not hold the undertaking of any other bank.

2. Confirmed and unconfirmed:

When using a Letter of Credit, it is important to know which bank is giving its irrevocable undertaking. Some Advising Banks attach a letter to the Issuing Bank's Letter of Credit stating whether the Advising Bank is merely advising or is advising and also confirming the Letter of Credit. Other Advising Banks advise the irrevocable undertaking of an overseas Issuing Bank to the Beneficiary by incorporating it into the text of the Advising Bank's advice. If the Advising Bank is merely advising, the advice, whether it attaches or incorporates the overseas issuing banks undertaking, will likely bear a notation by such Advising Bank that it makes "no engagement" or words to that effect.

An unconfirmed Advice of a Correspondent Bank's Irrevocable Letter of Credit .Beneficiaries of such advices are dependent on the commercial stability of the Issuing Bank and the political and foreign exchange stability of the country in which the Issuing Bank is located. Beneficiaries are not always willing to rely on the stability of an Issuing Bank—particularly when that bank is in another country or is unknown to the Beneficiary. Consequently, a Beneficiary may request that the Applicant instruct the Issuing Bank to have its Irrevocable Letter of Credit confirmed by a bank in the Beneficiary's country. A Confirming Bank is the bank which, at the request or with the consent of the Issuing Bank, adds its own irrevocable undertaking to that of the Issuing Bank. An example of Advice and Confirmation of Correspondent is, If an overseas bank (buyer's bank) issues its Irrevocable Letter of Credit and requests that Citibank, New York, add its confirmation and advise the Beneficiary, then Citibank, as Advising and

Confirming Bank, could use its own form of advice and confirmation. Confirmed Letter of credit includes the confirmation from the Advising bank. The advising bank also takes responsibilities for honoring drawing. In the case of Unconfirmed L/C, advising bank does not add confirmation and neither take responsibilities for honoring drawing.

3. Back-to- Back: The term used to describe a credit issued by the bank for its customer against the banking of another credit received in the customers favor.

4. Transferable and non –transferable: In Transferable L/C, beneficiary has power to transfer the credit to the party. Such credit is possible to pass on to more than one party by way of breaking the original value of the credit. Here beneficiary gives the power of drawing bill to someone else. Non-transferable L/C means beneficiary has no right to transfer the power of drawing bills to someone else.

5. Red Clause and Green Clause: Red Clause L/C gives authority to advising bank to make cash advance to beneficiary before he presents document, to enable him to purchase raw material needed to produce finished product required for shipment under terms of credit. In Green Clause L/C, it authorize advising bank to make cash advance in the line of Red Clause of L/C, to enable beneficiary for procurement of raw material to produce finished product for shipment with storage facility. In both the cases, advance recovered from the amount payable to beneficiary upon presentation of document.

6. Sight and Usance L/C: In sight L/C, payment done to the beneficiary is as soon as documents presented to the paying bank. In case of Usance L/C, terms of the credit made are for 30, 60, 90, and 120, 180 days or even more. Therefore, settlement of payment would be on the future date depending on the terms of credit. In other words, all such L/C is required to be open only on sight basis. The exception on this provision is the L/C opened for machinery and capital goods.

1. Assignable Credit: When the first beneficiary fails to effect shipment because of any reason what so ever paved to second beneficiary without getting advising bank involved. The title of L/C remains with original beneficiary.

2. Revolving Credit: If the amount of drawing is re-instated and made available to the beneficiary for shipment the L/C is called revolving L/C. In revolving L/C the original value or a part of the original value or any other value as per the terms is re-instated after certain occurrence i.e. upon completion of first shipment or upon completion of certain period or upon notification is made by the issuing bank or applicant.

2.1.4 BENEFITS OF LETTER OF CREDIT

The main objectives of L/C system in Nepal are as follows:

1. Facilitates Financing

Letter of Credit:

- Provides a specific transaction with an independent credit backing and a clear cut promise of payment
- Satisfy the financing needs of the seller and the buyer by placing the bank's credit standing, distinguished from the bank's funds, at the disposal of both parties.
- May allow the buyer to obtain a lower purchase price for the goods as well as longer payment terms are possible.
- Reduces or eliminates the commercial credit risk as payment certainty is by the bank, which issues an irrevocable L/C. The seller no longer needs to rely on the willingness and capability of the buyer to make payment.
- Reduces certain exchange risk and political risk while not eliminating them.

- May not require actual segregation of cash, since the buyer is not always required to collateralize his L/C obligation to the issuing bank and
- Expand sources of supply for the buyers since certain sellers are willing to sell only against cash in advance or a L/C.

2. Provides Legal Protection

L/C supported by a wide variety of laws and regulations are such:

- Legislative and semi - legislative law.
- Codified law- in most countries the law for L/C has been codified, e.g. in
 - Civil law code countries, and in
 - Common law code countries.
- Decisional law- statutory law governing L/C found in various jurisdictions. There are also extensive legal cases that have interpreted these statutory provisions and well known in judicial circles.
- Contractual law customary law- in addition to codified and case law L/Cs' are usually governed by the International Chamber of Commerce's Uniform custom and Practices (UCP500 in practice) for L/C. These rules are periodically revised and have been in effect since 1933 and are the set of universally recognized rules that are helping L/C to operations grow.
- The UCP rules are adopted by the banks through collective notification to the International Chamber of Commerce, by the respective National Committees of the ICC, by the national banking association of the country, by a bank's individual adherence and notification to the ICC, or by incorporation of the UCP in the L/C itself.

3. Assures Expert Examination of Documents

- The buyer is assured that the documents required by the L/C (if issued subject to the UCP) must be presented in compliance with the terms and conditions of the L/C and the UCP rules.
- The buyer is assured upon documents presented will be examined by banking personnel knowledgeable in L/C operations, and
- The buyer is confident that payment will only be made to the seller after the terms and conditions of the L/C and the UCP rules are complied with.

2.2 Brief profile of Nepal Investment Bank Ltd. (NIBL).

Nepal Investment Bank was established in 1986 A.D., in the name of Nepal Indosuez Bank Ltd., as a joint venture between Nepalese and French partners. The French partner (holding 50% of the capital of NIBL) was Credit Agricole Indosuez, a subsidiary of one the largest banking group in the world.

With the decision of Credit Agricole Indosuez to divest, a group of companies comprising of bankers, professional, industrialists and businesspersons, has acquired on April 2002 the 50% shareholding of Credit Agricole Indosuez in Nepal Indosuez Bank Ltd.

The name of the bank changed to Nepal Investment Bank Ltd. with the approval of NRB, Company Registrar's office and from Bank's AGM with the following shareholding structure:

Capital

Table 2

Shareholders	Percentage
1. Group of companies	50
2. Rastra Banijya Bank	15
3. Rastra Beema Sanstha	15
4. General Public	20

The holding of shares by public also implies that NIBL is one of the listed companies in NEPSE. Nepal Investment Bank Limited came into existence under company act 2021 B.S and commercial Bank act 2031, in the year 2042 B.S., Magh 6th (1986 / 02 /27). Under Commercial Bank Act 2031, the bank started its operation as a commercial bank with the permission of NRB, on 2042 B. S., Magh 22nd.

Goals and Objectives

- To provide the reliable, prompt and high standard of banking service adopting the latest version banking technologies in compliance with the need and demand of the market.
- To develop life – long relationship with clients and build profits through customer oriented service and customer satisfaction.
- To widespread its branch – network in different parts of the country covering all different development regions facilitating large number of clients as far as possible.
- To provide possible co-operation and support for the improvement of the economic condition of the country.
- To perform banking transaction within Nepal and outside Nepal, receive deposits, give out loans and advances, discounting bills, promissory notes, foreign

exchanges, buy and sale of bills of lading, delivery order and other business papers, opening letter of credits as well as issuing bank guarantee.

- To perform all the functions noted in the Memorandum of Association, Article of Association and as per the rules and regulations.

Branches of NIBL

The registered office of NIBL is located at Durbar Marg, Kathmandu. This is also the head office of the bank and all the major functioning including making rules and policymaking, issuance of securities, treasury operations, payment and settlement, international banking are done through this branch. The banking facilities of Nepal Investment Bank is not only limited to Durbar Marg but also spread over 27 more locations within the country and four more branches are going to open soon which will be in Baneshwor, Bhotahiti, Dhumbarahi and Dang. NIBL has aimed to open 50 branches within in 2010. The branch offices of NIBL including their official addresses and corresponding addresses are:

Table 3

Branches	Address
1. HEAD OFFICE	DURBARMARG, P.O. BOX 3412, KATHMANDU TEL: (997-1) 4230374, 4242858, 4227032 FAX NO: (977-1) 4227050
2. SEEPADOLE	ARNIKO HIGHWAY, SURYABINAYAK, BHATAPUR TEL: 6615617, 6612832 FAX: 6616617
3. BIRGUNJ	ADARSHANAGAR, P.O. BOX 101 TEL (051) 523327, 525277 FAX: (051) 525297

4. PUL/CHOWK SANCHAYA KOSH BUILDING,
PUL/CHOWK, LALITPUR
TEL: 5010188, 5010042
FAX: 5010142
5. BANEPA BANEPA, KAVRE
TEL: (011) 664315,662401
FAX NO: (977-11) 662402
6. JEETPUR JEETPUR, BARA
TEL: (997-53) 520297
FAX NO: (977-53) 520877
7. NEWROAD NEWROAD, KATHMANDU
TEL: 4242858, 4230374
FAX: 4227050
8. BIRATNAGAR GOL/CHA CHOWK, BIRATNAGAR
TEL: (997-21) 534523, 534524, 534525
FAX NO: (977-21) 534526
9. BUTWAL TRAFFIC CHOWK, BUTWAL
TEL: (997-71) 549991, 549992, 549993
FAX NO: (977-71) 549888
10. BHAIRAHAWA MAITRIPATH – 5, SIDDHARTHA NAGAR
TEL: (997-71) 526991, 526992, 526993
FAX NO: (977-71) 526990
11. POKHARA CHIPLE DUNGA
TEL: (997-61) 538919
FAX NO: (977-61) 538920
12. PUTALISADAK PUTALISADAK, KATHMANDU,
TEL: (997-1) 4445303, 4445302
FAX NO : (977-1) 4445304
13. NARAYANGARH PUL/CHOWK, NARAYANGARH
TEL: (997-56) 532921, 532922
FAX NO: (977-56) 532925

14. JANAKPUR MILLS AREA, JANAKPUR
Tel: (997-041) 527331
FAX NO: (977-41) 527332
15. NEPALGUNJ DHAMBOJI, NEPALGUNJ
TEL: (081) 525978,525682
FAX: (081) 521664
16. THAMEL CHAKSIBARI, THAMEL
TEL: 4218431,4218434
42,184,854,218,486
FAX: 4218434
17. KALIMATI KALIMATI CHOWK, KALIMATI
TEL:4672493,4672494
4672495,4672548 FAX: 4272612
18. BIRTAMOD TRAFFICCHOWK, BIRTAMOD
TEL:(023)543810,543811543811
FAX: (023) 543811
19. BATTISPUTALI BATTISPUTALI, KATHMANDU
TEL:4471690,4471790
FAX: 4470202
20. DHANGADI CHAURAHACHOWK, DHANGADI
TEL:(091)523620,523706
FAX: (091) 524090
21. GONGABU GONGABUCHOWK, KATHMANDU
TEL:4365318,4365077
FAX: 4365302
22. SURKHET NETACHOWK, SURKHET
TEL:(083)524330,524331
FAX: 524332
23. JUMLA KHALANGBAZAAR, JUMLA
TEL:(087)520132

24. BOUDHA	BOUDHA, KATHMANDU TEL: 4480121, 4480122 FAX: 4480123
25. HETAUDA	BANKROAD, HETAUDA TEL: (057) 526001, 525946 FAX: (057) 526005
26. PALPA	TANSEN, PALPA TEL: (075) 520832, 520833 FAX: (075)-520891
27. LUKLA	CHAURIKHARKA, LUKLA TEL: (038) 550120 FAX: (038) 550220

The above listed are the total number of branches currently existing of NIBL. These branches have been trying their best to render their services to the public. Since, this bank has received license from NRB, in the future period this bank can open its branches all over the country and provide service to enhance the banking industry.

NIBL is managed by a team of experienced bankers and professionals and have proved to be a reliable bank, which is also reflected by the fact that NIBL had been awarded “The Bank of the Year 2003 , 2005 and 2008” by the banker of the London based financial times group. NIBL is committed to be “The Nepali Bank with Global connection.”

2.3 Review of related research works

During any research work, the previous studies cannot be ignored because they provide foundation to the present study. In other words, there has to be continuity in research. This continuity in research is ensured, by linking the present study with the past

research. Literature review is basically a “stock taking’ of available literature in this field of research.

The main purpose of literature review is to find out what studies have been done in the field of study and what remains to be done. It provides the foundation for developing a comprehensive theoretical framework and minimizes the risk of pursuing the dead ends in the research. Thus some books, unpublished materials and previous research studies in the topic of “Letter of Credit” have been reviewed. Though sufficient literature does not exist related to this subject, it has been tried to include all possible information in this report.

From the Library of Nepal Investment Bank Ltd., I found that Mr. Kunjan K.C. (2006 A.D.) has conducted a Study titled “Letter of Credit Process of Nepal Investment Bank Ltd.”. Its main objective was to find out the process of Letter of Credit especially in context of Nepal Investment Bank Ltd. and to provide recommendations for the improvement of the company in the subject matter.

Mr. K.C.’s conclusion in his own words was that “NIBL has played a great role in the development of the International Trade Finance. From the transaction of Letter of Credit of NIBL, we can say that this bank really has helped in the International Trade, which has also helped to uplift the national economy. The terms and procedures used in the Letter of Credit may vary from country to country and also from bank to bank. It is advised that banks in Nepal should follow the Directives of NRB as well as ICC Guidelines before opening of L/C. Due to efficient and effective management and modernized technology used by NIBL, there should be further improvement in the technology so that there is drastically rise in the L/C transaction.

Mr. Sajjan Kansakar(2007 A.D.) conducted a Study on “ Letter of Credit Information System of Nepal Investment Bank Ltd. This study was conducted basically to explore the Letter of Credit Process of the Bank and to learn about the use of

Information Technology in the field of International Trade in the field of L/C transactions.

His conclusion was that Letter of Credit is becoming a popular way of payment and is particularly suited to cross-boarder trade. A customer arranging for a letter of Credit to be opened can specify precisely what goods he/ she is ordering, and the documentation that evidences they have been dispatched according to his/her wishes. The customer does not make any inspection himself so the bank is required to scrutinize documents. The text of the letter of credit will specify whether the documents will be negotiated and accepted by the issuing bank (which may be in the suppliers country) or by the advising or confirming bank.

2.4 Research Gap

The researches previously conducted were on the whole performance of the banks whereas this research focuses particularly on the performance of L/C business and in the context of NIBL. There were no reports available specifically written on this subject. This report is related exclusively to L/C business of NIBL.

CHAPTER 3

RESEARCH METHODOLOGY

3.1 Concept

Research methodology is the way to solve systematically about the research problem. This study aims to examine, analyze and interpret the Letter of Credit Business of NIBL. Research methodology may be express in other words as process of arriving to the solution of the problem through planned and systematic dealing with collection of the data and analysis of the figure.

3.2 Research Design

Research work is designed to obtain answers for the research question. Research design is the plan, structure and strategy of investigation conceived so as to obtain answer to research question. This study is mainly concerned with the examination and evaluation of Letter of Credit Business of NIBL. Therefore the study is closely related with the subject matter. In course of preparation of this thesis regular discussion was made with the Supervisors of Trade Finance Dept. of NIBL and from the discussions and the provided materials, the study has been conducted.

3.3 Nature and Source of Data

Information is the lifeblood of any research. So, the significance of the research depends upon the nature, availability and accuracy of the information, together the true information, the data collection matters the most to fulfill the objectives of his study.

Data and information that have been used in this study were collected from the following sources.

- Financial Statements of NIBL
- Different & Periodical reports of Trade Finance Dept. of NIBL
- Published as well as unpublished matters
- Various Reports and Directives of NRB.
- Books related to the subject matter
- Related materials available in the Library of NIBL.
- Some sites on the Internet

3.4 Research Variables

The research variable of this study mainly related with periodical reports that are prepared in the Trade Finance Dept. of NIBL. and the available matters related to the subject in NRB.

3.5 Tools Used

The data collected are managed and organized in the tables and formats. Interpretation and explanations are made wherever necessary. To analyze the collected data; tables, graphs and diagrams have been used as per the requirement. Both financial tools as well as statistical tools are used to analyse the collected data which are discussed below.

3.5.1 Financial tools:

Analysis of financial statement is the process of determining financial strength and weakness of the company by establishing strategic relationship between the items of balance sheet. Among various tools, ratio analysis and trend analysis will be used for this

study purpose. The data are collected from balance sheet of the company as well as different data which are calculated and submitted for the quarterly meetings are presented as a record.

3.5.2 Statistical tools:

There are different statistical tools; here few statistical tools are used to analyze the study as per requirements.

i) Correction coefficient (r)

Correlation coefficient is the important tool to analyze the degree of relationship between two or more variables. It is used to describe the degree to which one variable in the linearly related to other variables. It refers the closeness of the relationship between two or more variables. In other words, it is an analysis of covariance between two or more variables.

It is the statistical measure of the relationship, if any, between series of numbers representing data of any kind, from returns to test scores. If two series move in the same direction, they are positively correlated; if the series move in opposite direction, they are negatively correlated.

The degree of correlation is measured by the correlation coefficient, which ranges from +1 for perfectly correlated series to -1 for perfectly negatively corrected series. Symbolically, correlation coefficient can be expressed as follows:

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

Where,

r = Correlation coefficient between X and Y

N = Number of product observation and sum of product X and Y

$\sum X$ = Sum of product X and sum of product Y

ii) Probable error (P. E.)

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

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

where,

r = Correlation coefficient

N = Number of pairs of observations

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

Here, the researcher has been calculating the correlation coefficient between import and export L/C to know the relationship of these variables. This relationship result helps the management for policy formulation in the coming days.

3.6 Limitations of the methodology:

To carry out the research work, various financial and statistical tools are used. Similarly, descriptive as well as analytical analysis of letter of credit has been carried out however these tools and techniques have been some limitations.

For research purpose, the five-year data are used in analyzing the financial and statistical tools, which may mislead the research work, as it is not sufficient to make projections for future regarding the performance of the bank. As far as the financial tools concerned, only ratio and trend analysis has been carried out to know the performance of the bank however there are various financial tools to measure the financial performance of the bank. With regard to statistical tools, the researcher carried out different statistical tools to make the result more concise but it may not be the valid measurement. Although, there were certain limitations during the research work, it is not so crucial that it can weaken the basic findings of the study.

CHAPTER 4

DATA PRESENTATION AND ANALYSIS

4.1 Introduction

The main purpose of this study is to examine the Performance in terms of Letter of Credit Business of NIBL. Here various comparative figures related to Letter of Credit (such as Import L/C outstanding, Export L/C outstanding, commissions earned) for 5 years are presented for growth analysis and another banks figures for the same period is also presented for competitive analysis.

4.2 SWOT analysis

Everyone has some certain strength and weak points. These may be either visible or concealed. Strength and weakness are within us and to some extents are under our control. We can manipulate these to suit a particular situation on the other hand opportunities and threats are beyond our control. An organization should try to exploit the opportunities and avoid the threats. A successful organization is the one that may carry its own SWOT analysis. SWOT is basically a common sense approach to management that can be applied to any situation with a little bit of imagination.

Now let's see a brief SWOT analysis of

S – Strength

) Quality Service:

The services offered by the bank are faster and reliable which has enabled it to be one of the leading banks in Nepal

) Established Presence

It has been established in Nepal since 1986 that means it has been here for more than 20 years of quality service and had earned goodwill in the financial market.

) Location

The bank has taken time to decide on the location of its outlets very sensibly and has managed to provide its services from the locations that are convenient to its customers

) Innovative attitude

It has always welcomed technological changes and implemented the latest technologies that make it No. 1 technologically. It is the first to introduce the Visa Debit Card in Nepal. It is the first one to provide Internet banking (though limited access and facility only).

W – Weakness

) Promotional Activities

It spends a lot of money on promotional activities each year but not as successful compared to other banks due to well-trained team of such activities. It should build up a team for the same to get better results or the activities and to save a lot of unnecessary effort and money

) Limited Outlets

It has limited branches as compared to other Govt. banks as well as commercial banks specially in the rural area. Hence it should open more branches including in the rural areas.

O – Opportunities

) Increasing earnings of people

A slow but steady growth of Lower class to Middle and Middle class people to Upper middle class and Upper Middle Class people to High class due to growing remittance

from abroad as hundreds of people are going abroad for employment. It should focus on this sector for

) Growth in Industries

Though due to present political situation the industries have not been able to perform up to the expected level, there are still lots of possibilities. should explore the market to capture its share on time.

T – Threats

) Competition and New Entrants.

The growing No. of Finance companies and then turning to development banks, moreover NRB has licensed to few more Banks to operate recently and also planning to allow international banks to open their outlets in Nepal. In this scenario has to face a lot of competition in the days ahead so it better prepare for the situation on time

The above is just a glimpse illustration of a SWOT analysis of Nepal Investment Bank Ltd. It is highly recommended that should do a SWOT analysis taking all the variables into account to get a clear picture and to help it draw a future course of action.

4.3 Context Analysis.

In this part of the study, an analysis of the context of the letter of Credit such as Contents of L/C, Documents used in L/C, Discrepant Documents found in L/C, Amendments made in the L/C, Pre-requisites for opening L/C etc are carried out.

CONTENTS OF LETTER OF CREDIT

Letter of credit must contain the following information:

1. Name and address of issuing Bank
2. A statement regarding application of UCPDC (Uniform Customs and Practice for Documentary Credit).
3. L/C number and date
4. Name and address of the applicant
5. Name and address of the beneficiary
6. L/C value (currency and amount)
7. Terms of delivery
8. Tenor of bills of exchange
9. Nominated Bank
10. Details of the goods(amount, quality, brand name etc)
11. Method of shipment
12. Document Required
13. Date and Place of expiry
14. If any further instructions

DOCUMENTS USED IN LETTER OF CREDIT

Documentation constitutes a very important element in smooth execution of export order. It is therefore essential that the exporter clearly prepares and assembles the document called for the contract of L/C. Documents usually required is classified as follows:

1) Transport document

The transport document describes about the means through which the buyer is receiving the goods. If the credit calls for marine or ocean Bill of Lading (**B/L**), bank accepts the document which indicates the name of the carrier and is signed or authenticated by the

carrier or his agent, or the master or his agent. B/L indicates that the goods have been loaded on board or shipped on named vessel. The B/L should indicate the port of loading and port of discharge and should be as per the credit. The B/L must indicate "Freight Prepaid" or "Freight Payable". The terms like "Freight to be prepaid" or "Freight pre-payable" will not be accepted. If the credit is silent, bank accept transport document stating "Freight yet to be paid". The transport document may also include about **transshipment** i.e. unloading and reloading of vessel to another during the course of ocean carriage.

If the credit calls for a transport document covering at least two different modes of transport, bank accept the document which indicates the name of the carrier or **multimodal transport** operator and is signed or authenticated by the carrier, multimodal transport operator or the master; or their named agent. Similarly, the credit may call for an **air transport document**, i.e., the goods have been sent through airway. The date of issuance of the air transport document will be deemed the date of shipment. The credit consists of the airport of departure and the airport of destination. The transshipment in air way means unloading and reloading from one aircraft to another aircraft during the course of carriage from the airport of departure to the airport of destination stipulated in the credit. If the credit calls for a road, rail, or inland waterway transport document; banks will accept the document which contains the name and signature of the carrier; bears the indication of the receipt; indicates that goods have been received for shipment; mentions the place of shipment and destination as per credit; and meets all other requirements of credit.

2) **Commercial Invoice And Packing List:**

The commercial invoice is a document that is sent to the bank by the beneficiary's bank after the goods has been shipped. It is same as the pro-forma invoice but it consist the invoice No. and date as well as the buyer's order No.. The INCOTERMS i.e., a

universally recognized set of definitions of international trade terms, such as FOB, CIF, C&F etc is also presented in the document. The number of packages, description of goods, quantity, rate and amount is specified along with the eight digit harmonic code. The proforma invoice details and the commercial invoice details should match each other.

3) Insurance Document:

Insurance Document is one of the important documents required for L/C transaction. UCP 500 devotes article 34 - 36 to this document as it is of very complex nature. All the originals of insurance document issued and signed by insurance companies, underwriters or their agents are to be presented. The cover notes issued by the broker are not acceptable. Date of issuance must be on or before the date of shipment or it must be proved by the specific notation that the cover is effective from the date of shipment. The insurance cover must be in the currency of credit and at least for 110% of CIF value.

4) Certificate of Origin:

The origin of the goods is precisely stated in a credit and in many cases (e.g., commodities) the origin can considerably influence the price of the goods; hence, it needs to be exact. The Certificate of Origin should be certified by the Chamber of Commerce of the origin country, or it can be valid if the buyer accepts to purchase the goods that is certified by the beneficiary himself.

5) Proforma Invoice:

It is the document which gives detail information about the exporter and the consignee and the invoice contains of the harmonic code of the goods that is going to be purchased. The country of origin of the good is also specified in it. The invoice consists

of the terms of payment and the detail information about port of discharge, port of loading and the final destination of the goods.

6) Other Documents:

Other documents demanded by the L/C besides these mentioned above are Bill Of Exchange, Draft and Inspection Certificate. There can be others too.

DISCREPANT DOCUMENT:

After receiving the documents, it needs to be thoroughly checked with terms and condition of L/C. If any documents contain any discrepancies which is not be accepted by the issuing bank, then the bank immediately informs the settlement bank and the client within seven working days as per UCP Act. If the issuing bank fails to inform the settlement bank then the bank is bound to remit the payment even though the documents contain any discrepancies. If the client accepts the discrepancies then he immediately has to submit an acceptance letter to the bank before retiring the documents and remitting the payment.

AMENDMENTS IN THE DOCUMENTARY CREDIT

The issuing bank, the beneficiary and advising/conforming bank are entitled to reject any amendment under an irrevocable credit that may either create embarrassment or additional involvement for violate the beneficiary contract. Any issuing bank as a rule, acts in accordance with buyer's wishes, if the Documentary credit is still feasible, and for itself further unwanted liability.

PRE REQUISITES FOR OPENING AN L/C

Before opening Letter of Credit following pre-requisites are to be fulfilled by the opener.

1. The company/Firm should be registered in concerning Ministry /Department /Authority (to obtain operational permission from concerning authority or submitted yearly renewal certificate, if required)
2. Income Tax Certificate, PAN Certificate, VAT Certificate (any one)
3. The customer should be current account holder.
4. The photocopies of the Citizenship of the Proprietor/Partners/Directors.
5. The Proprietor/Partners/Directors name should not be registered in black list or defaulter list.
6. Limit approval or review period bank should collect the copy of Customer/Firm's financial document, CIB report or Board Minute (if Co is P. Ltd).
7. Customer should be better creditworthiness in the market
8. For the import of following merchandise prior approval is, required before opening of the L/C.
 - a. For import & export of Liquors VAT approval must be taken.
 - b. Ministry of Commerce has determined / restricted not to import certain quantity like Post Dana (Poppy seed) so if some importer wants to import Poppy seed more than determined quantity he must submit the approval from Ministry.
 - c. Trading firms do not import old clothes, Scrap and machinery but if somebody wants to import those goods he must get the permission from Ministry of Population & Environment.
 - d. To get the permission from Ministry of Population & Environment for import of merchandise which destroys the Ozone layer
9. Approval/recommendation letter is required from concerning authority for import like wool, cotton & medicine etc.

10. Permission letter is required from NRB in case of importer is an individual or non-registered firm.
11. Either approved limit or cash margin (cash or equivalent cash) required before L/C opening.
12. Import Restricted Items:
 - a. Arms and Explosive Products
 - b. Radio Frequency transmission products
 - c. Narcotic Products – Cigarette, Tobacco, Heroin
 - d. Gold, Silver and Precious Metals (Gold is very recently removed)
 - e. Liquors, Wines – *Inland Revenue Department's approval is required*
 - f. Products made of Recycled Plastics granules
 - g. Ozone Deflecting products – *must be CFC free.*
 - h. Beef

Operations of Letter Of Credit.

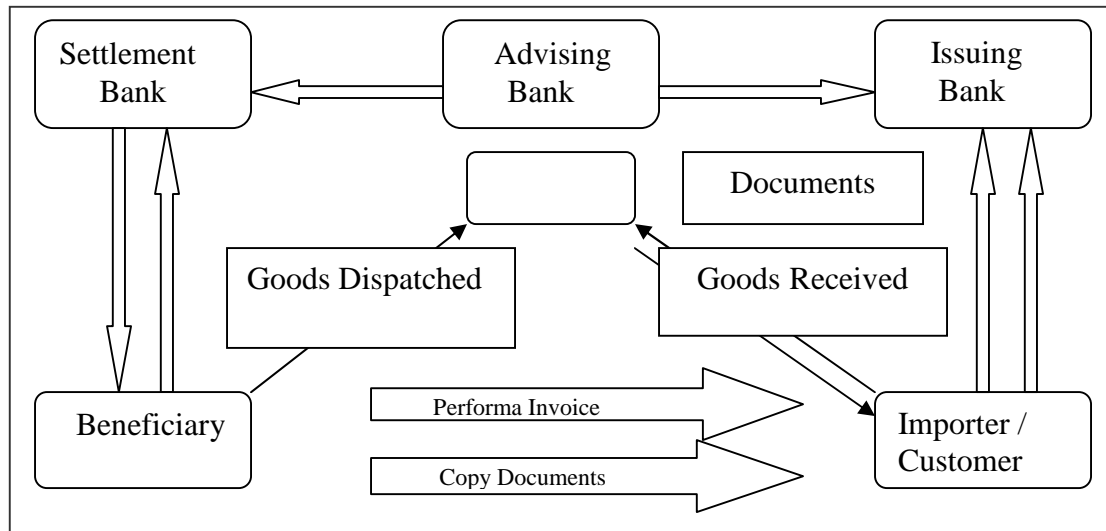


Figure: 2

PROCESS TO OPEN IMPORT LETTER OF CREDIT

Scrutinizing of application

- L/C application must be filled properly.
- Under Open General License (OGL) only L/C can opened for products.
- The Bi.Bi.Ni form no.3 should be filled and signed properly.
- The firm's registration and income TAX/VAT must be updated.
- Proforma Invoice should be attached with quantity amount, harmonic code and certificate of origin.
- Signature of authorized person and the stamp of the company should be verified.

Process of approval

- When the application is certified, it is sent for approval from the concerned authority.
- If the case is within limit and without any dues it is approved.
- In case of non-limit holders or new client approval is made through concerned authority
- L/C has to be processed and passed the same day the application is received. A register is maintained clearly showing the time application was received, processed from the department. Proper monitoring and follow up is done by the TFD.

After approval has been obtain

- The margin for L/C is taken and held in the L/C margin account prior to the issue of the L/C.
- Bank's margin for L/C is 10 % or above depending on the client, however this can be lowered for selected clients by special approval.
- The commission and the telex charges have to be charged.
- The L/C liability has to be booked properly
- The Bi.Bi.Ni form no3 needs to be separated and copies should be sent to NRB and custom and original filed by the bank.

Formation of L/C

-) After the above process, the L/C format has to be made according to the application and other documents.
-) Selection of the transmission means and format should be made accordingly.

Transmission of L/C

- L/C can be sent through mail, courier, telex and SWIFT
- The date and time should be noted after L/C has been sent.

Amendment on L/C

- Proper request for amendment should be made.
- Amendments must be signed by the authorized person.
- Bi.Bi.Ni. form no.3 must be filled and signed properly as well.
- Amendment must not violate any NRB directives.

Cancellation of L/C

- Applicant must request the issuing bank for the cancellation of L/C. Then the issuing bank informs the advising bank and advising bank informs the beneficiary for consent. Under mutual understanding of the buyer and seller the L/C is cancelled.

Documents required under import L/C

- Draft
- Commercial invoice
- Packing list
- Certificate of origin
- Insurance copy
- Transport documents

Documents required to release the goods from customs

- For industry 2% margin is taken and for trading 10% margin is taken for the custom purpose.
- Bi.Bi.Ni. form no.4 is filled in quadruplicate as follows:
 - a. First two copies to importers, for the submission to customers.
 - b. Third copy to be sent to NRB.
 - c. Fourth copy to be retained by the Bank
- Each copy of the documents mentioned in L/C along with copy of L/C and Pro-forma invoice is separated.
- These documents are compiled and kept in an envelope for sealing.

Settlement of L/C after arrival of original Documents

- It must be checked whether documents are as per the L/C terms and orders and any discrepancies found.
- Exchange rate details should be confirmed with the Treasury Department before giving them to the client.
- If the documents are found to have discrepancies in them, client should be informed and a telex should be sent to the settlement bank mentioning the discrepancies.
- Refusal of discrepant documents has to be informed within seven days from the receipt of documents as per UCP-500.

Mode of payment

- **Sight payment credit:** In this type of credit the draft is at sight basis i.e. when the documents are presented to the buyer's bank, the payment should

be made immediately after receiving the documents. The normal time for the payments given by UCP-500 is seven working days after receiving the drafts at sight.

- **Acceptance Credit:** In this type of credit, the draft are drawn at certain time from sight i.e. the issuing bank must sent payment of the draft value from the days mentioned in the draft from the acceptance of the draft by the buyers. When the issuing bank receives the documents, it informs the applicant for its acceptance. When the buyers accept the draft value, the buyer's bank advice the due date i.e. the date of payment according to the days mentioned in the draft.
- **Draft Payment Credit:** If a credit is issues deferred payment until a future date without stipulating that the draft are to be drawn, it falls into the category of deferred payment credit and the advising bank will not call for drafts.
- **Negotiating Credit:** A credit can be "Freely negotiable" which means negotiable with any bank but negotiation can also be restricted to a particular bank. If a credit is freely negotiable, then any bank may negotiate it.
- **Transferable Credit:** A transferable credit is that where one credit can be transferable between more than one party by way of breaking the original value or the full amount.
- **Back to Back Credit:** This type of credit is opened against the backing of another credit received on the customer favor i.e. the payment under the back to back credit will be made after the full and final realization of payment of documents received under the credit received in the customers favor.

The customer who also exports goods abroad submits their export L/C to import the raw material to prepare the goods for export against their export L/C in the bank. When they make shipment of the goods and presents documents for negotiated. The bank makes the payment of the import L/C.

SOME OF THE IMPORTANT DIRECTIVES OF NRB

1. Applicant for opening L/C should mandatory fill in the presented form.
2. At the time of retirement of document Bi.Bi.Ni. form no. 4 should be prepaid in quadruplicate. First two goes to importer for submission to custom office and clearance of goods. Third to NRB and fourth is retained by bank.
3. Documentary credit serial Number for the L/Cs payable in Indian currency should be separate.
4. Bi.Bi.Ni. form 3 & 4 should be submitted to NRB on daily basis by bank situated in KTM valley and weekly in other case (out of valley). A copy of BBN 3 must be sent to the custom office.
5. Requirement for the opening L/C firm registration certificate, Performa invoice or contract specifying value and quantity of the goods to be imported.
6. Documentary credit with clauses like “all discrepancies acceptable” shall not be open nor shall be amended resulting to such arrangement.
7. No documentary credit shall be amended to enhance the L/C amount by more than 10 % without prior approval. However such approval is not required; where amended amount is US \$1000 or less.
8. The central office of each commercial bank shall compulsorily follow up all documentary credit for more than US \$50,000.

9. In the case of cancellation of import L/C all documents made available by bank to the importer shall compulsorily be received back.
10. Documentary credit received through correspondent bank should only be accepted.
11. Payment to the beneficiary must be made through correspondent bank. Direct payment to the beneficiary by way of draft is strictly prohibited.
12. Payment of import bill than US \$ 1000 by demand draft requires NRB approval.
13. No payment or otherwise transaction can be made of the transport document prior to the date of opening of documentary credit or the date of amendment (if any).
14. Commercial bank accepts a “transport document” if that is presented to bank within 45 days of issue.
15. All commercial bank should inform NRB within 7 days of opening L/C with a cash margin of 50% or more.
16. Along with Bi.Bi.Ni. form no. 4, all commercial banks should forward following documents to the concerned customs office. Amendments in L/C if any, commercial invoice, transport document, certificate of origin, packing list.
17. Procedure should be followed before submitting Bi.Bi.Ni form no. 4 to the concern customs office. Document must be submitted in sealed envelope. Bank should maintain separated file for each customs office. Non-receipt of document from customs office within reasonable time or document receipt does not matched with the bank copy must be informed to NRB.
18. A bank can issue Bi.Bi.Ni form no. 4 on the basis of copy document only, if concerned bank had received full payment from the value of goods. The original document must be submitted to bank within 21 days from the date of issue of Bi.Bi.Ni form no. 4, if the bank does receive original documents within such time it must refer to NRB, further bank should not accept other copy of document of defaulter.
19. No commercial bank can issue a documentary credit with “Red Clause”.

20. Concerned authority must issue the certificate of origin. However if importer abroad accepts the certificate issued by the producer, above rule can be exempted.
21. Pro-forma invoice or indent must contain description of goods, country in which the goods are produced, unit price, quality and total price.
22. Half yearly internal audit report of each bank licensed to issue L/C must be sent to NRB.
23. If original document do not match with copy documents bank should inform NRB and hold the L/C till NRB gives clearance.
24. The back-to-back L/C can be opened against confirmed and irrevocable L/C only. Payment shall be made only out of the proceed of export of the finished product of the concern raw material.

PROHIBITION REGARDING THE OPENING OF L/C:

Opening of Letter of credit for certain things are prohibited by the NRB, Nepal Govt. and the Head Office of related bank. Opening of Letter of Credit for things like Tetracycline, Boron, Readymade Garments, Clove, Video Cassette, Plastic Scraps, Titanium Dioxide, Shoes Doxycycline, and Raw material for Medicine, Flasks, Lunch Box are prohibited. Apart from these if the applicant requests the bank to open the L/C for other things that do not have harmonic code, bank should open only after taking the permission of the Loan Investment Department. However, if the above-mentioned products are going to be used as raw materials then the L/C can be opened in favor of those products to be imported in the country. Ministry of Commerce has prohibited opening up the L/C relating the import of the Poppy Seed, which is used for making opium. L/C cannot be opened for import of the illegal products. Government has prohibited the opening of the L/C for the export of the rice. Besides these, Nepal Investment Bank prohibited these things:

- Arms and Ammunitions
- Jewelries /Precious Stones
- Narcotics
- Wild Life Products Like Elephant Tusk, Skin and Beef
- Walkie Talkie

PROBLEMS WHILE OPENING L/C

Opening procedure of L/C is long, legal and complicated process. Therefore, parties involved in this process face many problems. The main problem faced by the opening banks and customers can be follows:

1. NRB has instructed all the commercial banks to open L/C on the basis of the status of the client. Commercial banks find the term 'status' very vague.
2. Employees of Commercial Banks involved in L/C transaction have to be responsible if anything goes wrong in the transaction. However, employees of Nepal Govt.'s Department of Commerce and Taxation Department from where people get import license and income tax clearance certificate respectively to open L/C are not responsible.
3. Government makes valuation for goods to be imported, is usually undervalued, and gives foreign currency accordingly. As the given currencies are not sufficient to pay the bill, importers are compelled to get foreign currency illegally.
4. Sometimes the client of the bank turns out to be fraud. In such case bank has to face many problems. Sometimes client does not come to collect the document; bank has to pay to the exporter even though the goods are in the banks possession.

5. The new customer has to deposit around 100% margin and the L/C takes around 15-30 days for settlement. Therefore the customer cannot use the amount, as it gets freeze.
6. If the party is new then exporter does not believe and asks for advance payment to deliver goods for which NRB does not provide permission. For this purpose, they have to use the other reputed importer's account to pay them.
7. If a firm's has not exceeded more than one year period from its registration, they have to pay tax in advance of L/C amount. Issuing bank charges 10% tax of L/C amount and send it to the tax office. Within that one-year, they have to pay advance tax payment every time they open L/C.
8. The major problem of L/C is as per UCP up to 5% tolerance is allowed but as per NRB rules; no specific tolerance on the value and quantity is allowed.

Above are some of the most important elements of Letter of Credit transactions.

4.4. Analysis of Basic Indicators:

Ratio analysis

Ratio analysis is one of the tools of financial analysis. Under ratio analysis, various ratios have been calculated and interpreted. For the sake of interpretation and analysis of those ratios calculated, both the methods of vertical and horizontal analyses have been implemented. Specifically, the following groups of ratios have been selected for analysis:

4.4.1 Total loan & advances to total deposit ratio

Commercial banks utilize the outsider's fund for profit generation purpose. Loan & advances to total deposit ratio shows whether the banks are successful to utilize the outsiders funds (i.e. total deposits) for the profit generating purpose on the loan & advances or not. Generally, a high ratio reflects higher efficiency to utilize outsider's fund and vice-versa. The ratio can be calculated by using following formula

$$\text{Total loan \& advances to total deposit ratio} = \frac{\text{Total loan \& advances}}{\text{Total deposits}}$$

Table 4.4.1 Total loan & advances to total deposit ratio

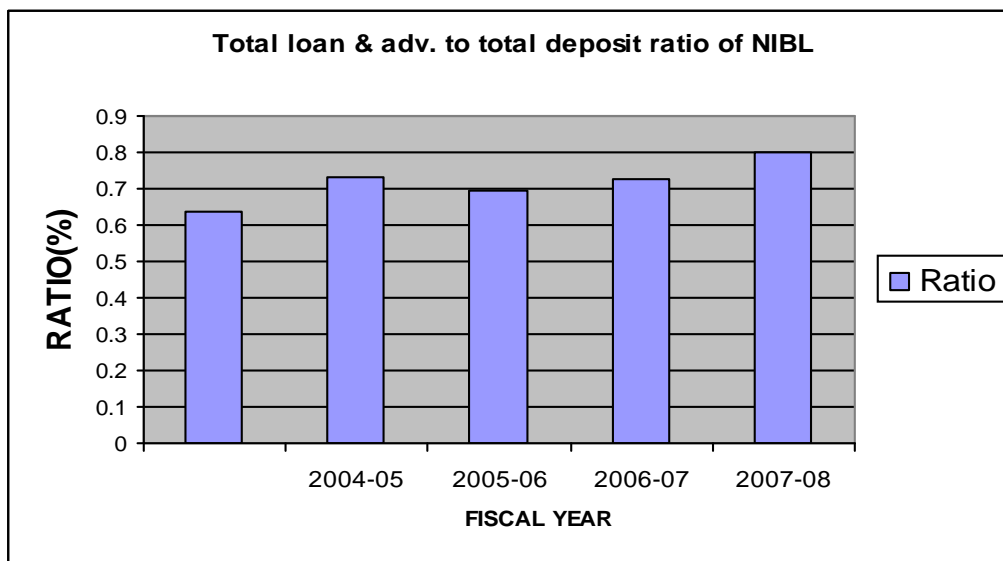
FY	Total Loan (in million)	Total Deposit (in million)	Ratio
2003-04	7339	11525	0.63679
2004-05	10453	14255	0.733287
2005-06	13178	18927	0.696254
2006-07	17769	24489	0.725591
2007-08	27530	34452	0.799083
			3.591004
AVE			0.718201

(Source: Major Indicators of respective bank)

Table 4.4.1 shows the total loan & advances to total deposit ratio of NIBL. The ratios were 63.67% in the fiscal year 2003/04, 73.32 in the fiscal year 2004/05, 69.62% in the fiscal year 2005/06, 72.55% in the fiscal year 2006/07 and 79.90% in the fiscal year 2007/08. In an average, the ratio remains at 71.82% during the five-year study period. The ratio is in a decreasing trend except in the fiscal year 2005/06 and 2006/07. The ratio has fluctuated more because the growth rate of total loan & advances and total deposit was not in same proportion.

The bank has higher average total loan & advances to total deposit ratio during the five Years study period. It indicated that bank has more liberal lending policy and able to utilize the collected funds. These are shown in the following diagrams.

Figure: 4.4.1



4.4.2 Non-performing assets to total loan & advances ratio

NRB has directed all the commercial banks create loan loss provision against the doubtful and bad debts. Non-performing assets to total loan & advances ratio shows the actual figure of NPA over the total lending of bank. It is the base ratio to measure efficiency of lending department. Here, lower ratio reflects higher efficiency to provide good lending and vice versa. The ratio is calculated by using following formula:

$$\text{Non-performing assets to total loan \& advances ratio} = \frac{\text{Non - performing assets}}{\text{Total loan \& advances}}$$

Table 4. 4.2 Non-performing assets to total loan & advances ratio

FY	Ratio times
2003-04	2.47%
2004-05	2.69%
2005-06	2.07%
2006-07	2.37%
2007-08	1.12%
Ave	2.14%

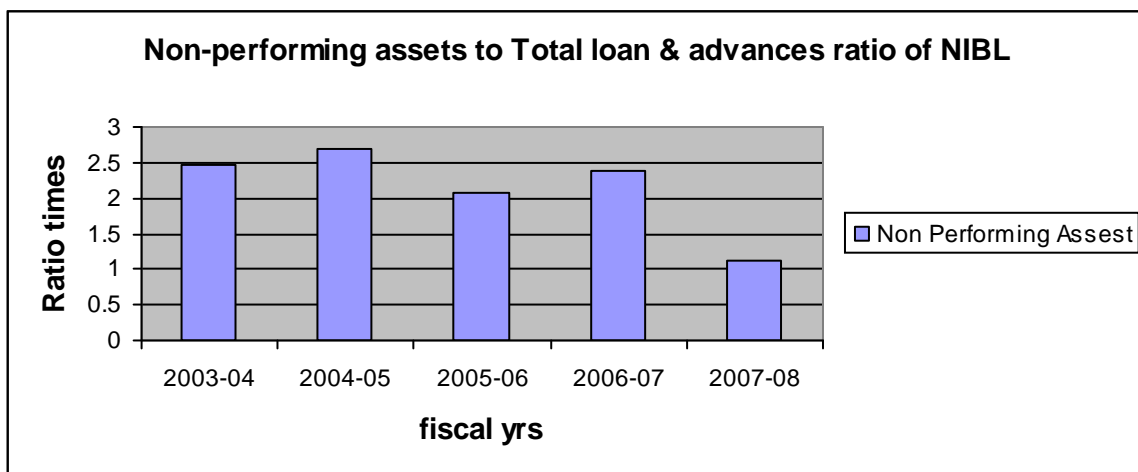
(Source: Major indicators of respective bank)

Table 4.4.2 shows the non-performing assets to total loan & advances ratio of bank. This ratio shows the bad credit and doubtful credit of bank over the total credit granted. The non-performing assets to total loan & advances ratio of bank were 2.47% in the fiscal year 2003/04, 2.69% in the fiscal year 2004/05, 2.07% in the fiscal year 2005/06, 2.37% in the fiscal year 2006/07 and 1.12% in the fiscal year 2007/08. The average ratio remains at 2.14% during the five-year study period. The ratio is in a decreasing trend

except in the fiscal year 2004/05 and 2006/07.

The bank has higher average ratio of non-performing assets to total loan & advances rather it was in decreasing trend in the following years of study period. It indicated that bank has not efficient credit management team and strict policy even it was satisfactory. These are shown in the following diagram:

Figure: 4.4.2



4.4.3 Interest income to total loan & advances ratio

It tells the income as interest from total loan & advances. It is useful to know the fact that Whether the loan has given good return or not. We can increase interest income by taking good issuing and recovery credit policy. High return shows the soundness of credit policy.

It is calculated by using the following formula:

Interest Income

Interest income to total loan & advances ratio = **Total loan & advances**

Table 4.4.3 Interest income to total loan & advances ratio

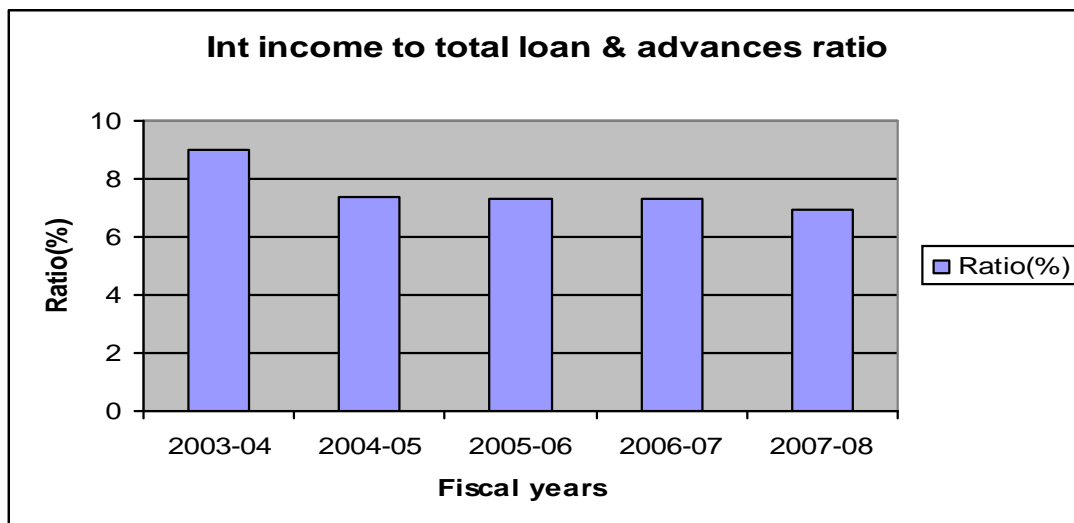
Fiscal year	Ratio(%)
2003-04	9.03
2004-05	7.36
2005-06	7.32
2006-07	7.33
2007-08	6.93
Average	7.59

(Source: Major Indicators of respective bank)

Table 4.4.3 shows the interest income to total loan & advances ratio of bank. The ratios were 9.03% in the fiscal year 2003/04, 7.36% in the fiscal year 2004/05, 7.32% in the fiscal year 2005/06, 7.33% in the fiscal year 2006/07 and 6.93% in the fiscal year 2007/08. The average ratio remains at 7.59% during the five-years study period. The ratio is in a decreasing trend except in yr 2006/07 because growth rate of total loan & advances

is more than the growth rate of total income over the study period. In an aggregate, the ratio is in a increasing trend. It is a good symptom of bank that it can earn form interest to paid for the depositors of bank. These are shown in the following diagram:

Figure: 4.4.3



4.4.4 Net profit to total loan & advances ratio

This ratio measures the earning capacity of commercial banks through its fund mobilizations loan advances. If signaling effect did not existed, there is always direct relationship between total loan & advances and net profits. It means, if one variable out of them is increased, that absolutely increased another variable and vice-versa. Higher ratio indicated greater success to mobilize fund as loan and advances and vice versa. Mostly loan and advances include cash, credit, over-draft, bills purchased and discounted.

$$\text{Net profit total loan \& advances ratio} = \frac{\text{Net Profit}}{\text{Total Loan \& advances}}$$

Table 4.4.4 *Net profit to total loan & advances ratio*

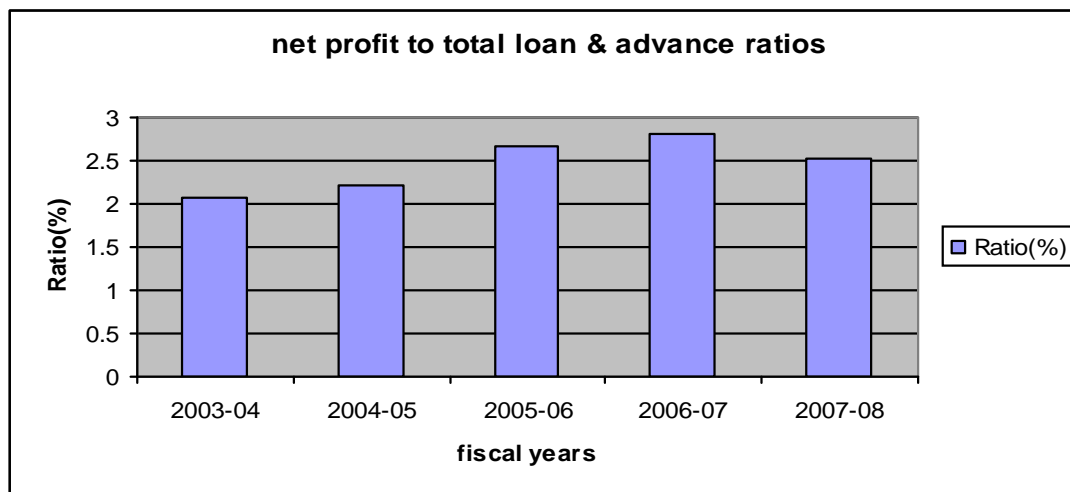
Fiscal Years	Ratio(%)
2003-04	2.08
2004-05	2.22
2005-06	2.66
2006-07	2.82
2007-08	2.53
Average	2.46

(Source: Major Indicators of respective bank)

Table 4.4.4 shows the net profit to total loan & adv of bank. The ratios were 2.08 in fiscal year 2003-04, 2.22 % in fiscal yr 2004-05, 2.66% in fiscal yr 2005-06, 2.82% in fiscal yr 2006-07, and 2.53% in 2007-08. In an average, the ratio remains at 2.46%. during the five-years study period. The ratio is in continuously increasing trend except in the fiscal yr 2007-08.

Both profit and loan & advances are in increasing trend. It is due to productive investment and profit generating investment. In this reason we can say management of bank is having good lending policy as well as they are investing in those sectors, which have high return with low risk. Interest spread rate is also a crucial factor for determination of net profit. In 2007-08 the profit ratio is in a decrease trend because the bank concentrates more in increasing its braches. These can be shown in the following diagram:

Figure: 4.4.4



4.5 Analysis of Import L/C

The importer (applicant) imported different products from out side of the country. In this Condition, the importer or applicant opened import L/C for safe payment. The bank has record of the data like the no. of L/C opened in different currency in particular month and their equivalent amt in NPR and from that no. of L/C of particulars month are accumulated to make it total L/C of Fiscal yr. So here the total amount of L/C and number of L/C issued are taken as two variables for comparison.

4.5.1 Import L/C in Nepali currency

Table: 4.5.1 Import L/C in Nepali currency

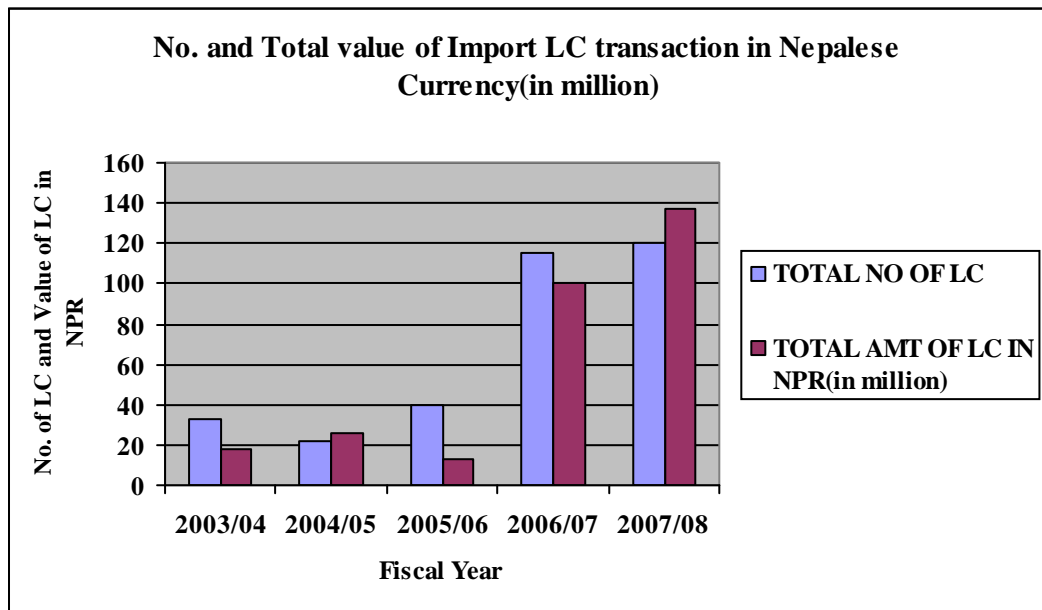
Fiscal Yr.	Total No. of L/C	TOTAL AMT IN NPR
2003/04	33	177,165,278.48
2004/05	22	260,917,020.77
2005/06	40	132,631,892.47
2006/07	115	1,004,683,467.66
2007/08	120	1,368,691,793.70

(Source: Nepal Investment Bank Limited)

Above table 4.5.1 represented the total number of import L/C opened in Nepalese currency and total transaction value of import L/C in Nepalese currency from fiscal year 2003/04/ to 2007/08. Total number of import L/C opened in Nepalese currency was in increasing trend over the five years of study period except in year 2004/05. They were 33, 22, 40, 115 and 120 in fiscal year 2003/04, 2004/05, 2005/06, 2006/07 and 2007/08 respectively. Similarly, total transaction value of import L/C in Nepalese currency was in increasing trend except in yr 2005/06. Though the no. of L/C has been increased but the NPR amt is decreased ,it is due to discount in commission given to the corporate clients. But then after, transaction value of import L/C in Nepalese currency was continuously in increasing trend until to the last year of study period. They were, 17.71 million in the fiscal year 2003/04, 26.09 million in the fiscal year 2004/05, 13.26 million in the fiscal year 2005/06, 100.47 million in the fiscal year 2006/07 and 136.87 million in the fiscal year 2007/08 respectively.

In fiscal year 204/05, both, total transaction value of import L/C as well as total number of import L/C opened in Nepalese currency has been declined as compared to previous fiscal years due to inconsistency situation of the country. Following figure more clarify about it:

Figure 4.5.1



4.5.2 Import of L/C in INR Currency

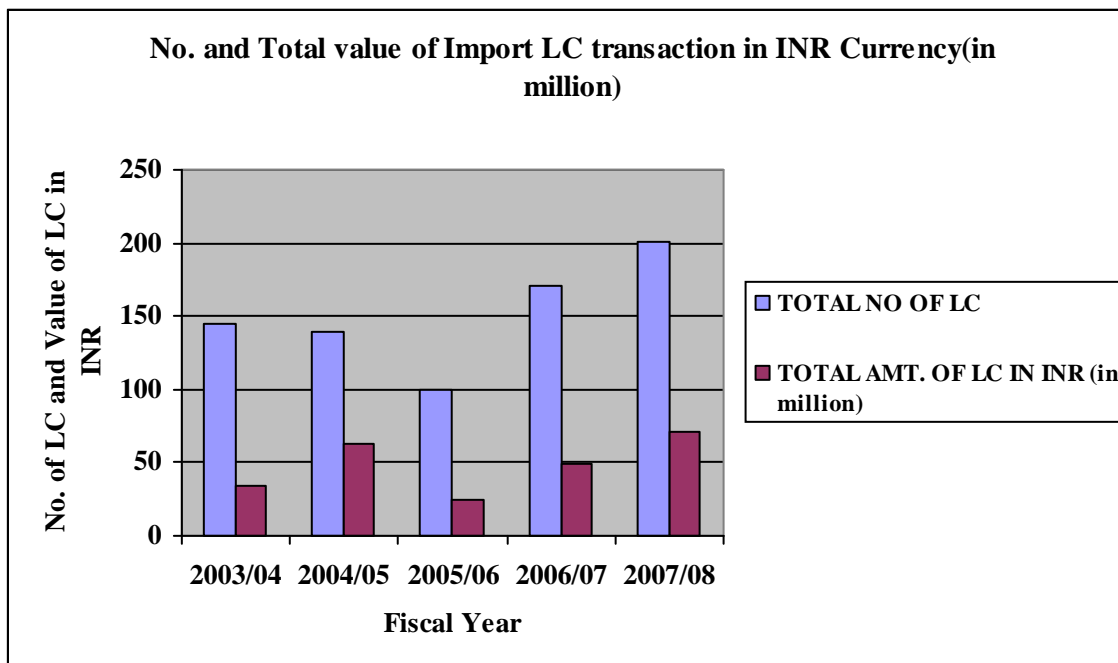
Table 4.5.2 Import of L/C in INR Currency

FISCAL YEARS	TOTAL NO OF L/C	TOTAL AMT. OF L/C IN INR CURR. (in million)	TOTAL AMT IN NPR (in million)
2003/04	145	34.22	55.25
2004/05	140	63.28	1,01.28
2005/06	100	24.97	39.93
2006/07	171	48.87	78.29
2007/08	201	71.60	1,14.67

(Source: Nepal Investment Bank Limited)

Above table 4.5.2 represented the total number of import L/C opened in Indian currency and total transaction value of import L/C in Indian currency from fiscal year 2003/04 to 2007/08. Total number of import L/C opened in INR currency was first in a decreasing trend and then in a increasing trend over the five years of study period .They were 145,140,100,171 and 201 in fiscal year 2003/04,2004/05,2005/06,2006/07 and 2007/08 respectively. Similarly, total transaction value of import L/C in INR currency was in a increasing trend except in yr 2005/06. They were, 34.22 million in the fiscal year 2003/04, 63.27 million in the fiscal year 2004/05, 24.97 million in the fiscal year 2005/06, 48.87 million in the fiscal year 2006/07 and 71.60 million in the fiscal year 2007/08 respectively. Following figure more clarify about it:

Figure 4.5.2



4.5.3 Import of L/C in US dollar

Table 4.5.3 Import of L/C in US dollar

FISCAL YEARS	TOTAL NO OF L/C	Total Amt of L/C in USD (in million)
2003/04	1287	7.90
2004/05	1165	9.65
2005/06	842	8.57
2006/07	1057	11.20
2007/08	1071	11.02

(Source: Nepal Investment Bank Limited)

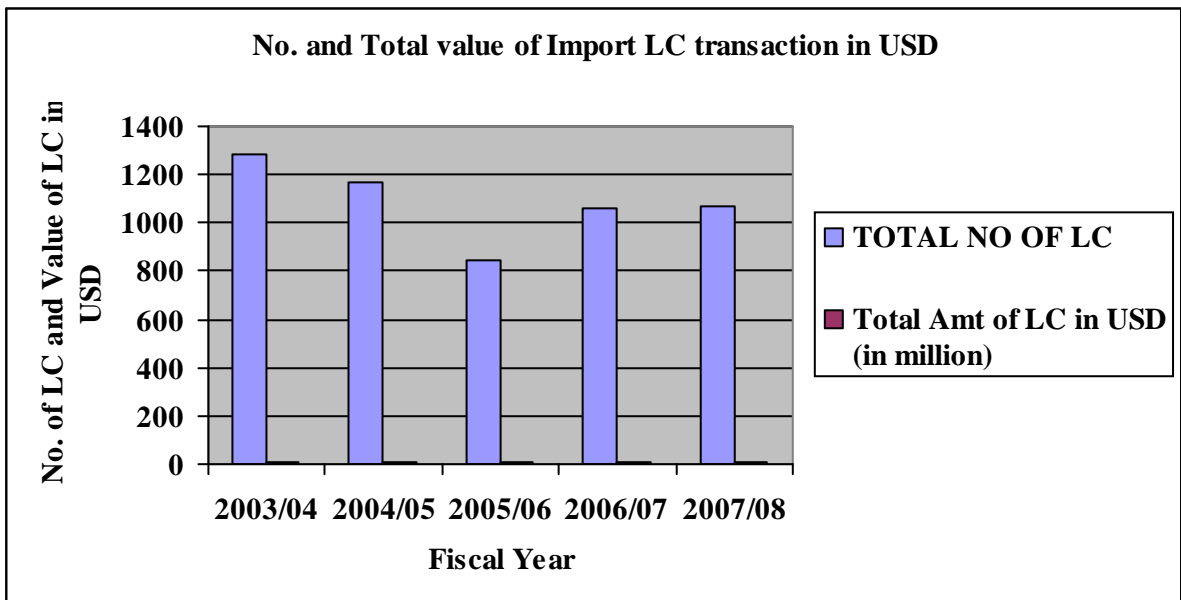
Above table 4.5.3 represented the total number of import L/C opened in US dollar and

total transaction value of import L/C in US dollar from fiscal year 2003/04 to 2007/08. Total number of import L/C opened in US dollar was in fluctuating trend over the five years of study period. They were, 1287, 1165, 842, 1057 and 1071 in the fiscal year 2003/04/, 2004/05, 2005/06, 2006/ 07 and 2007/08 respectively.

Likewise, total transaction value of import L/C in US dollar was also in fluctuating trend, i.e. first decreased, then again increased trend over the study period. They were, 7.90 million in the fiscal year 2003/04, 9.65 million in the fiscal year 2004/05, 8.57 million in the fiscal year 2005/06, 11.20 million in the fiscal year 2006/07 and 11.02 million in the fiscal year 2007/08 respectively.

Here, total number of import L/C opened in US dollar and total transaction value of import L/C in US dollar was fluctuating by trend as compared to previous fiscal years. Following Figure more clarify about it:

Figure 4.5.3



4.5.4 Import of L/C in EURO

Table 4.5.4 Import of L/C in EURO

FISCAL YEAR	TOTAL NO. OF L/C	TOTAL AMT. OF L/C IN EURO CURR.(in million)
2003/04	85	1.10
2004/05	65	1.56
2005/06	51	1.62
2006/07	57	5.14
2007/08	63	2.38

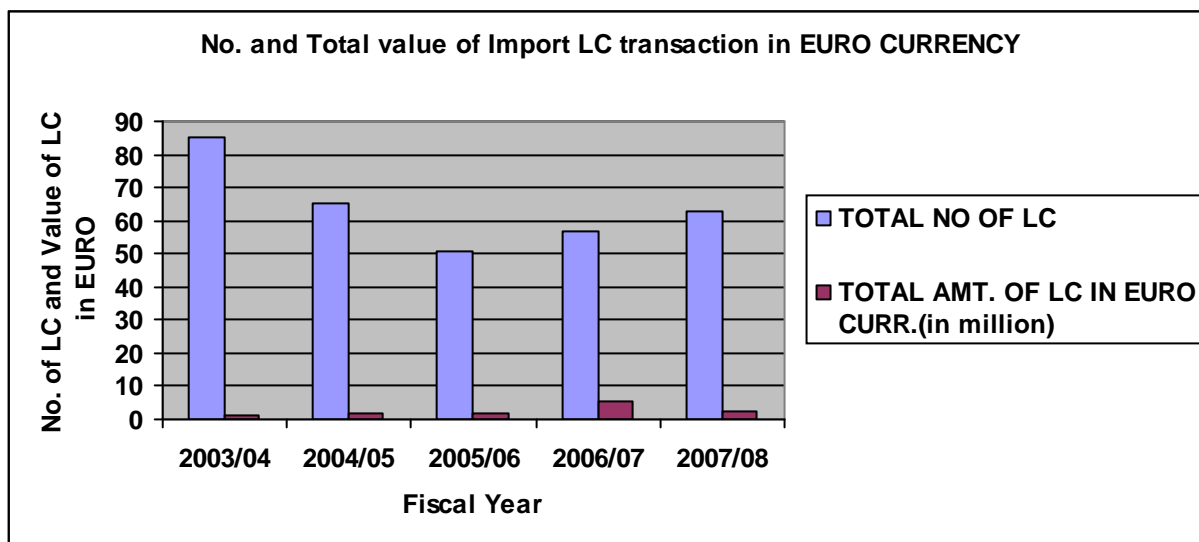
(Source: Nepal Investment Bank Limited)

Above table 4.5.4 represented the total number of import L/C opened in EURO and total transaction value of import L/C in EURO from fiscal year 2003/04 to 2007/08. Total number of import L/C opened in EURO was in fluctuating trend over the five years of study period. They were 85, 65, 51, 57 and 63 in the fiscal year 2003/04/, 2004/05, 2005/06, 2006, 07 and 2007/08 respectively.

Likewise, total transaction value of import L/C in EURO was also first in increasing trend and in last it is in deceasing trend over the study period. They were, 1.10 million in the fiscal year 2003/04, 1.56 million in the fiscal year 2004/05, 1.62 million in the fiscal year 2005/06, 5.14 million in the fiscal year 2006/07 and 2.38 million in the fiscal year 2007/08 respectively.

Here, total number of import L/C opened in EURO and total transaction value of import L/C in EURO was fluctuating by trend as compared to previous fiscal years. Following Figure more clarify about it:

Figure 4.5.4



4.5.5 Import of L/C in GBP Currency

Table 4.5.5 Import of L/C in GBP Currency

FISCAL YEAR	TOTAL NO. OF L/C	TOTAL AMT OF L/C IN GBP CURR. (in million)
2003/04	11	0.46
2004/05	15	0.61
2005/06	7	0.49
2006/07	4	0.33
2007/08	13	0.52

(Source: Nepal Investment Bank Limited)

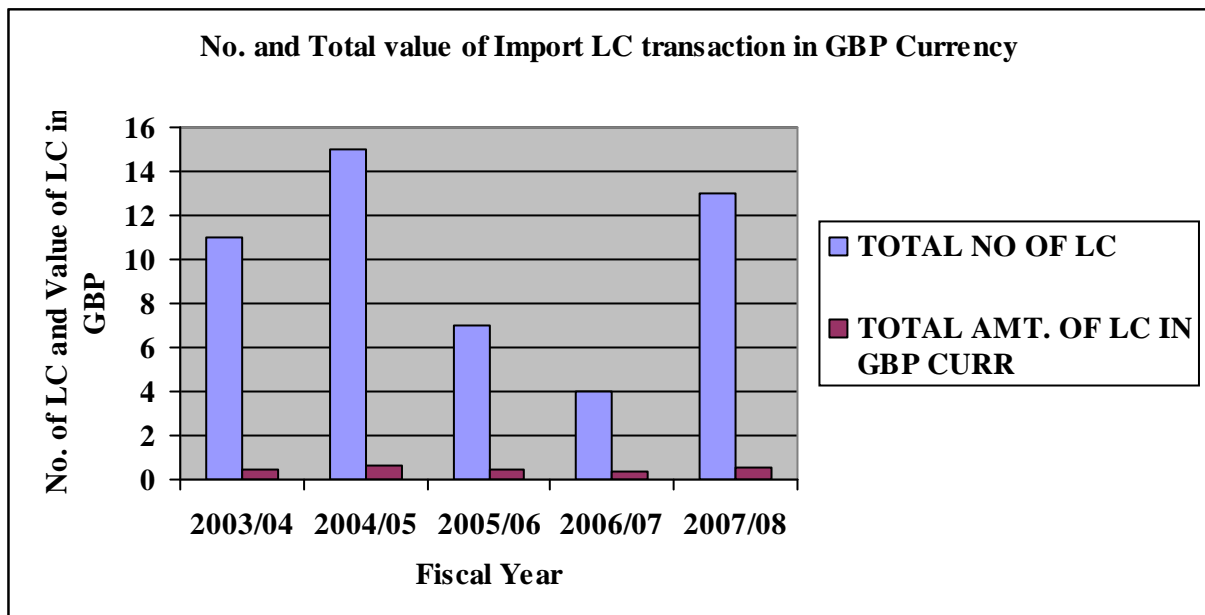
Above table 4.5.5 represented the total number of import L/C opened in GBP and total

transaction value of import L/C in GBP from fiscal year 2003/04 to 2007/08. Total number of import L/C opened in GBP was in fluctuating trend over the five years of study period. They were, 11, 15, 7, 4 and 13 in the fiscal year 2003/04/, 2004/05, 2005/06, 2006/07 and 2007/08 respectively.

Likewise, total transaction value of import L/C in GBP was also in fluctuating trend, i.e. first increased, then after decreasing and then increasing trend over the study period. They were, .46 million in the fiscal year 2003/04, .61 million in the fiscal year 2004/05, .49 million in the fiscal year 2005/06, .33 million in the fiscal year 2006/07 and .52 million in the fiscal year 2007/08 respectively.

Here, total number of import L/C opened in GBP and total transaction value of import L/C in GBP was fluctuating by trend as compared to previous fiscal years. Following Figure more clarify about it:

Figure 4.5.6



4.5.6 Import of L/C in JPY

Table 4.5.6 Import of L/C in JPY

FISCAL YEAR	TOTAL NO. OF L/C	TOTAL AMT. OF L/C IN JPY(in million)
2003/04	32	14.61
2004/05	29	14.33
2005/06	36	13.43
2006/07	50	34.32
2007/08	138	56.07

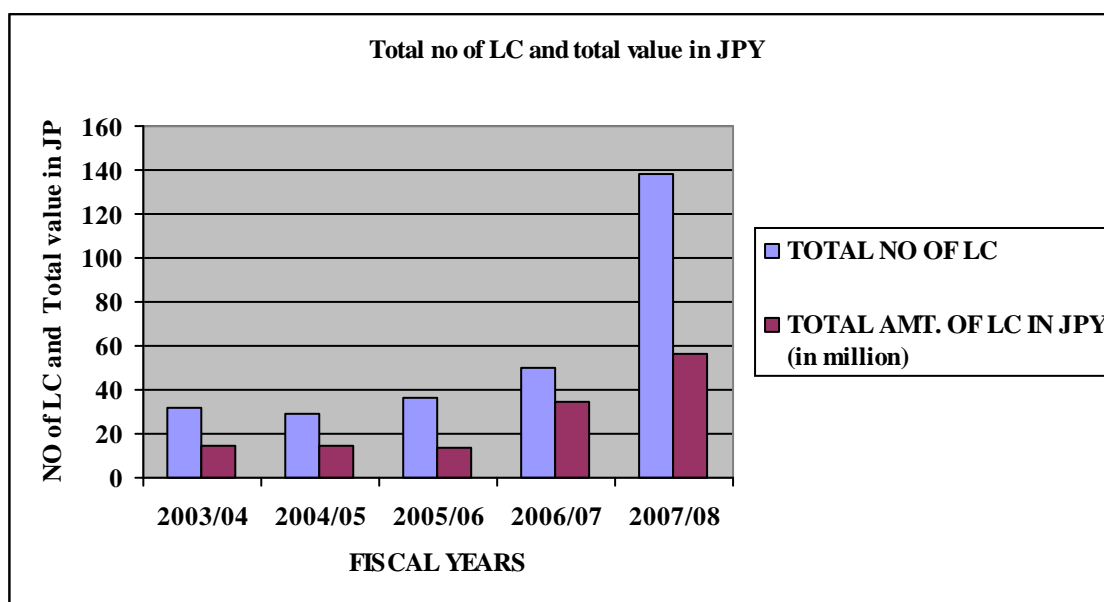
(Source: Nepal Investment Bank Limited)

Above table 4.5.6 represented the total number of import L/C opened in JPY and total transaction value of import L/C in JPY from fiscal year 2003/04 to 2007/08. Total number of import L/C opened in JPY was in fluctuating trend over the five years of study period. They were, 32,29,36,50 and 138 in the fiscal year 2003/04/, 2004/05, 2005/06, 2006/07 and 2007/08 respectively.

Likewise, total transaction value of import L/C in GBP was also in fluctuating trend, i.e. first decreased then in increasing trend over the study period. They were, 14.61 million in the fiscal year 2003/04, 14.33 million in the fiscal year 2004/05, 13.43 million in the fiscal year 2005/06, 34.32 million in the fiscal year 2006/07 and 56.07 million in the fiscal year 2007/08 respectively.

Here, total number of import L/C opened in JPY and total transaction value of import L/C in JPY was fluctuating by trend as compared to previous fiscal years. Following Figure more clarify about it:

Figure 4.5.6



4.6 Analysis of Export L/C

In the present globalization market, the exporter (beneficiary) exported different products from own (inside) country to foreign (outside) country. In this circumstance, the beneficiary concern with advising bank for export L/C. That mean, export L/C is opened by the exporter in his/her own country for safe payment.

The actual amount of export L/C may deviate because the final amount varies according to quantity of goods actually exported by the exporter because of the clauses in L/C like "partial shipment allowed". Since bank has not kept the record of actual amount of goods exported finally by the exporter or beneficiary and there is not more data regarding the export of L/C in other currency .This analysis is based on the record of document value maintained by bank only of NPR and USD. Even though the total amount of L/C and the number of L/C opened are not exactly dependent variables to each other, both of these variables are presented on the same chart for comparison.

4.6.1 Export of L/C in Nepali currency

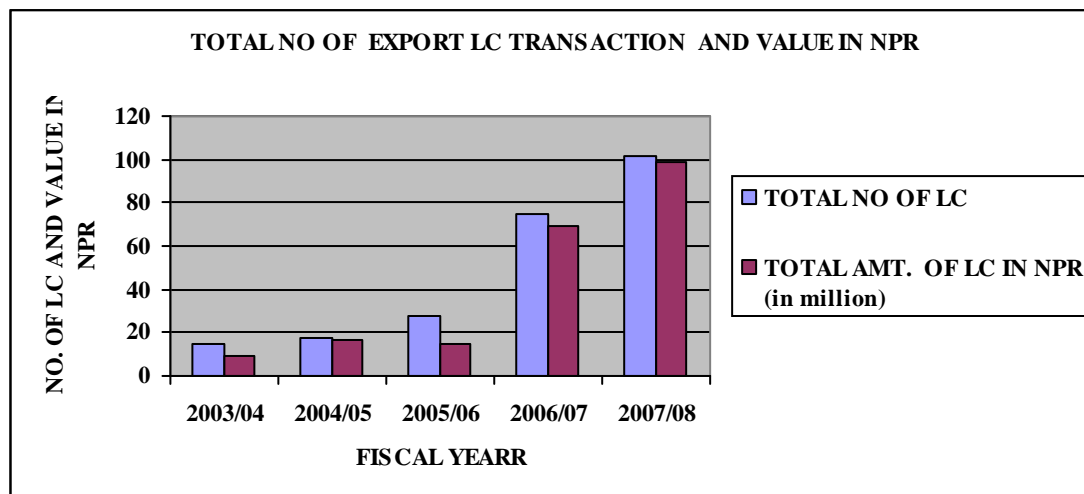
Table 4.6.1 Export of L/C in Nepali Currency

FISCA L YEAR	TOTAL NO. OF L/C	TOTAL AMT. OF L/C IN NPR(in million)
2003/04	15	9.26
2004/05	18	16.23
2005/06	28	14.57
2006/07	75	69.39
2007/08	102	98.31

(Source: Nepal Investment Bank Limited)

Table 4.6.1 depicted the total number of export L/C opened and total transaction value of export L/C in Nepalese currency from fiscal year 2003/04 to 2007/08. Total number of export L/C opened in Nepalese currency was in increasing trend. They were, 15,18,28,75,102 in the fiscal year 2003/04, 2004/05/, 2005/06, 2006/07, and 2007/08 respectively. Similarly, total transaction value of export L/C in Nepalese currency was also in continuously increasing trend over the last year of study except in Fis yr 2005/06 period. They were, 9.26 million in fiscal Y r 2003/04, 16.23 million in the fiscal yr 2004/05, 14.57 million in the fiscal yr 2005/06, 69.39 million in the fiscal yr 2006/07 and 98.31 million in the fis yr 2007/08 respectively. In fis yr 2005/06 total transaction value of export L/C in Nepalese has been decreased , but the no. of export L/C opened in Nepalese currency has been increase as compared to previous fiscal yr it is due to inconsistency situation of the country as well as in industrial sector. This can be clarify by following diagram:

Figure 4.6.1



4.6.2 Export of L/C in USD

Table 4.6.2 Export of L/C in USD

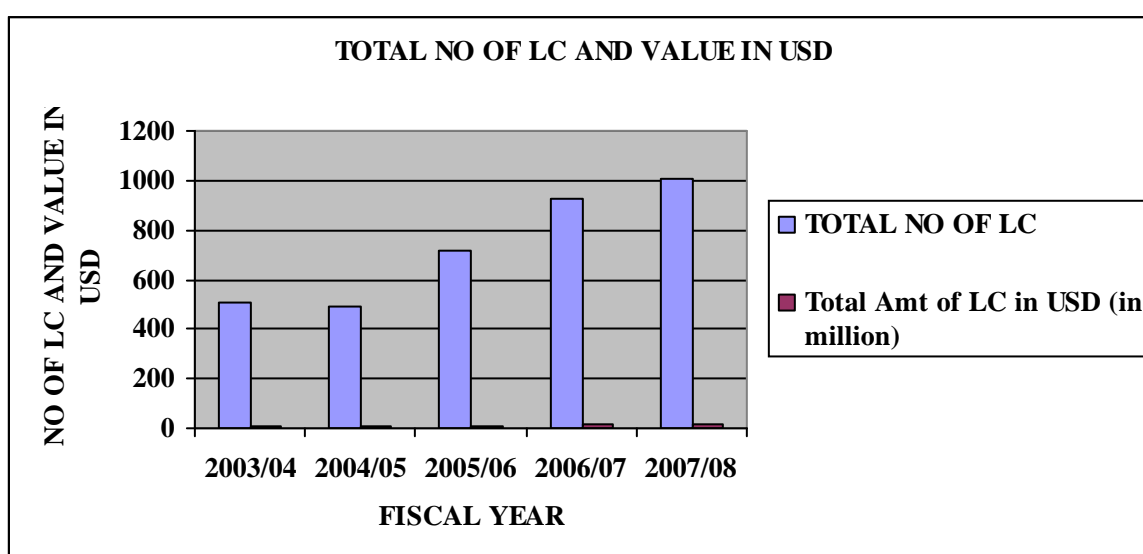
FISCAL YEAR	TOTAL NO. OF L/C	TOTAL AMT. OF L/C IN USD (in million)
2003/04	505	6.75
2004/05	489	7.12
2005/06	713	10.32
2006/07	929	12.31
2007/08	1004	12.89

(Source: Nepal Investment Bank Limited)

Table 4.6.2 depicted the total number of export L/C opened and total transaction value of export L/C in USD from fiscal year 2003/04 to 2007/08. Total number of export L/C opened in USD was in increasing trend except in fiscal yr 2004/05 .They were 505,489,713,929 and 1004 in the fiscal year 2003/04,2004/05/,2005/06,2006/07, and

2007/08 respectively. Similarly, total transaction value of export L/C in Nepalese currency was in continuously increasing trend over the last year of study period. They were, 6.75 million in fiscal Y r 2003/04, 7.12 million in the fiscal yr 2004/05, 10.32 million in the fiscal yr 2005/06, 69.39 million in the fiscal yr 2005/06, 12.32 million in the fiscal yr 2006/07 and 12.89 million in the fis yr 2007/08 respectively. This can be clarify by following diagram:

Figure 4.6.2



4.7 Total Commission earned on L/C in NPR

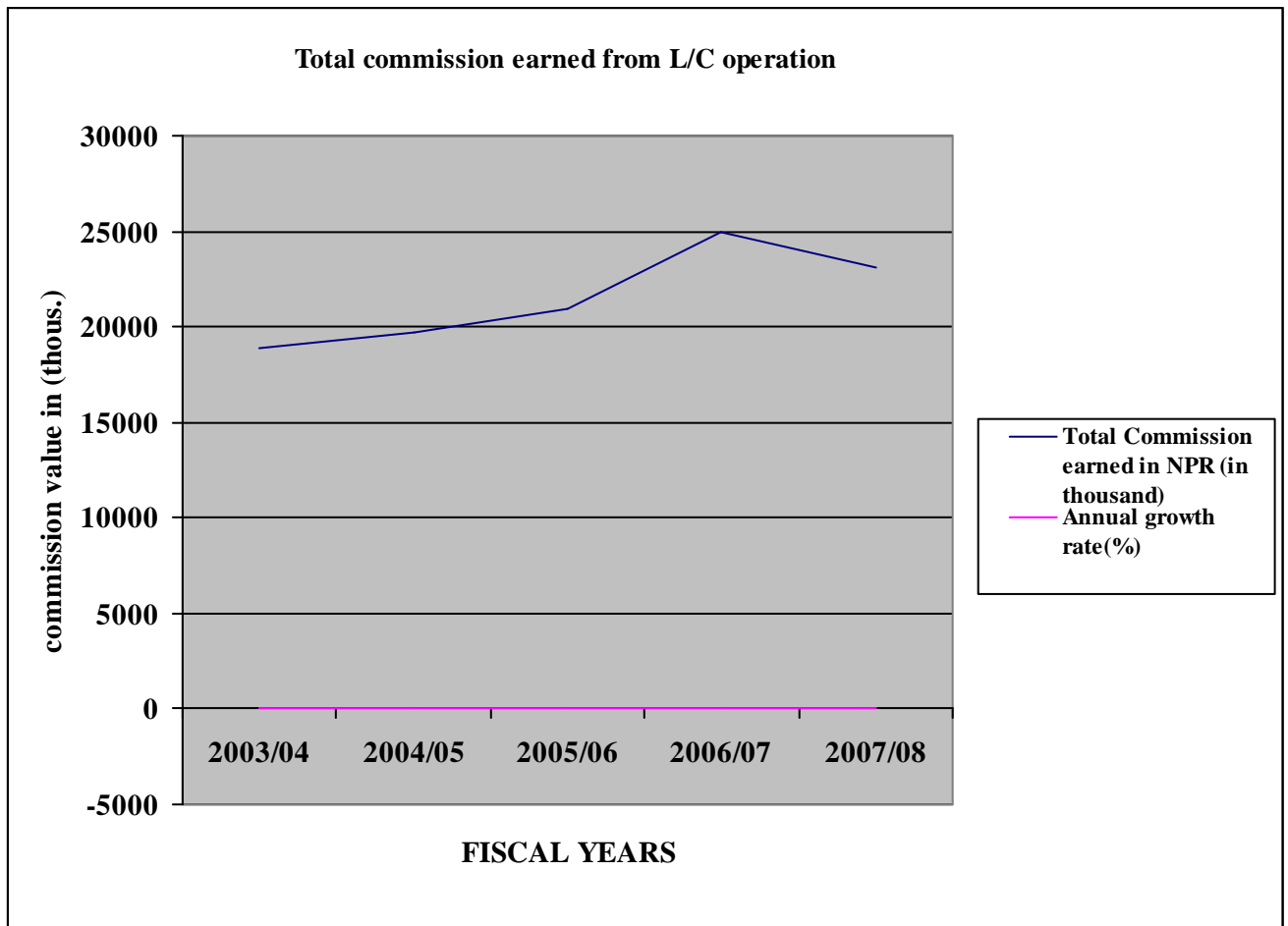
Table 4.7 Total Commission earned on L/C in NPR

FISCAL YEAR	Total Commission earned in NPR (in thousand)	Total Commission earned in NPR	Annual growth rate(%)
2003/04	18,879	18,879,342.71	0
2004/05	19,739	19,739,871.29	4.61
2005/06	20,908	20,908,704.52	5.88
2006/07	24,955	24,955,374.27	19.37
2007/08	23,140	23,140,571.10	-7.25

(Source: Nepal Investment Bank Limited)

Table 4.7 represented the total commission earned by bank from its L/C operation over the five years of study period, i.e. from 2003/04 to 2007/08. The bank is able to earn Rs. 18,879 thousands in 2003/04, Rs. 19,739 thousand in 2004/05, Rs. 20,908 thousand in 2005/06, Rs. 24,955 thousand in 2006/07 and Rs. 23,140 thousand in 2007/08 as commission charge from L/C transaction. Except in the last fiscal year, i.e. in 2007/08, remaining fiscal year has significant growth rate in commission earned by bank over the five years of study period. The decline in fiscal yr 2007/08 is due to the commission discounted to the corporate client .The following figure more clarify about it:

Figure 4.7



4.8 Correlation Coefficient (r):

The purpose of regression analysis is to identify a relationship. Correlation may be defined as the degree of linear relationship existing between two or more variables. These variables are said to be correlated when change in the value of one results change in another variable. Correlation is of three types. They are Simple, Partial and Multiple correlations. Correlation may be positive, negative or zero. Correlation can be classified as linear or non-linear. Here, we study simple correlation only. In simple correlation the effect of others is not included rather these are taken as constant considering them to have no serious effect on the dependent variable (*Shrestha, 2051: 31*).

It is calculated as:

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

Where,

r = Correlation coefficient between X and Y

$\sum XY$ = Number of product observation and sum of product X and Y

$\sum X \sum Y$ = Sum of product X and sum of product Y

Probable Error:

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

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

Where,

r = Correlation coefficient

N = Number of pairs of observations

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

Here, researcher has been calculating the correlation coefficient between total transactions value of import L/C in NPR and total transaction value of export L/C in NPR as well as total transaction value of import L/C in US dollar and total transaction value of export L/C in US dollar to know the relationship of these variables. This relationship result helps the management for policy formulation in the coming days.

4.8.1 Computation of correlation coefficient between total transaction value of import L/C in Nepalese currency (X) and total transaction value of export L/C in Nepalese currency (Y) of bank .

Table 4.8.1 Correlation coefficient between Import (X) and Export (Y) L/C of Nepalese currency (Rs. in million)

Fis Yr.	X	Y	X²	Y²	XY
2003/04	17.72	9.26	314.00	85.7476	164.0872
2004/05	26.09	16.23	680.69	263.4129	423.4407
2005/06	13.26	14.57	175.83	212.2849	193.1982
2006/07	100.47	69.39	10,094.22	4814.9721	6971.6133
2007/08	136.87	98.31	18,733.40	9664.8561	13455.6897
	294.41	207.76	29,998.13	15041.2736	21208.0291
	$x=294.41$	$y=207.76$	$x^2=29998.13$	$y^2=15041.27$	$xy=21208.03$

Where,

X = Value of Import L/C in Nepalese currency, Y = Value of Export L/C in Nepalese currency, X = 294.41, Y = 207.76, $\sum x^2 = 29998.13$, $\sum y^2 = 15041.27$, $\sum XY = 21208.03$ and N = 5.

Now,

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

i.e

$$r = 0.515$$

Similarly,

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

$$= 0.2216$$

$$\text{6 times P.E.} = 6 \times 0.2216 = 1.33$$

	SUMMERIZATION TABLE			
COEFFICIENT CORRELATION (r)	OF RELATIONSHIP	PROBABLE ERROR (P.E)	6 TIMES P.E	SIGNIFICANT or INSIGNIFICANT
0.515	POSITIVE CORRELATION	0.23	1.33	significant

The above calculation of correlation coefficient between total transaction value of import L/C in Nepalese currency and total transaction value of export L/C in Nepalese currency

of bank is “0.51”. That means there is positive correlation between these two variables. And the computation of probable error shows that there is significant relationship between these two variables. It means the two variables x and y move in the same direction.

4.8.2 Computation of correlation coefficient between total transaction value of Import L/C in USD (X) and total transaction value of Export L/C in USD (Y) of bank.

Table 4.8.2 Correlation coefficient between Import (X) and Export (Y) L/C of US dollar (Rs. in million)

Fis Yr	x	y	X ²	Y ²	xy
2003/04	7.90	6.75	62.41	45.5625	53.325
2004/05	9.65	7.12	93.12	50.6944	68.708
2005/06	8.57	10.32	73.44	106.5024	88.4424
2006/07	11.20	12.31	125.44	151.5361	137.872
2007/08	11.02	12.89	121.44	166.1521	142.0478
	48.34	49.39	475.86	520.4475	490.3952
	x=48.34	y=49.39	x ² =475.86	y ² =520.45	xy=490.39

Where,

X = Value of import L/C in USD, Y = Value of export L/C in USD

currency, X = 48.34, Y = 49.39, x² = 475.86, y² = 520.45, XY = 490.39

and N = 5.

Now,

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

i.e

$$r = 0.7745$$

Similarly,

$$P = 0.6745 \times \frac{1-r^2}{N}$$

$$= 1.14$$

$$6 \text{ Times P.E} = 6.84$$

	SUMMERIZATION TABLE			
COEFFICIENT OF CORRELATION (r)	RELATIONSHIP	PROBABLE ERROR (P.E)	6 TIMES P.E	SIGNIFICANT or INSIGNIFICANT
0.7745	POSITIVE CORRELATION	1.14	6.84	INSIGNIFICANT

The above table of correlation coefficient between total transaction value of import L/C in US dollar and total transaction value of export L/C in US dollar of bank is '0.77'. That means there is highly positive correlation between these two variables. And the computation of probable error shows that there is insignificant relationship between these two variables. It means if one variable is increased that obviously decreased another variable in terms of 0.7745% and vice versa but not significant at all time.

CHAPTER 5

SUMMARY, FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Nepal is economically a backward country. Govt. of Nepal has taken many measures for raising the economy of the country. Thus the govt. took the liberalization of foreign exchange system and the present International trade system came into existence in Nepal. In most of the developing countries in one way or other exchange control system/measure exists. In any country where exchange control measures are applicable, generally L/C is beneficial for overseas trade.

In the modern days the role of commercial bank is very significant as it helps trade and commerce of the country as well as International trade. The bank acts as middleman between buyer and seller. It gives a form of security to both the buyer and the seller, as the bank upon compliance of the stated terms and conditions handles payment. It brings an element of confidence for the payment once the goods have been dispatched and the seller also gets the money as soon as required documents are shown after the shipment of the goods. It is a widely accepted method for settling international financial trade transaction.

Nepal being a landlocked country required to use CaL/Cutta port for transit purpose. Therefore, if Letter of Credit is not established, there is no way that Indian Authorities in CaL/Cutta port can verify that the goods when declared as destined for Nepal really belongs to Nepalese Importer. So, if these goods are imported under L/C system, then documentary evidence can be provided to them for its genuine destination.

The whole report is based on the Letter of Credit business of NIBL. The report focuses more on the operational part so as to aware people about the L/C and to provide

general idea of operation of L/C business, which is one of the most important financial tools concerned to International Trade and Finance.

Nepal Investment Bank Ltd. is one of the growing commercial bank in Nepal, previously named as Nepal Indosuez Bank Ltd., which was established with the joint venture between Nepalese and French partners Credit Agricole Indosuez. NIBL has been serving its customers since 1986 and has contributed in the development of the country. Being a member of SWIFT (Society of Worldwide Inter bank Financial Telecommunication), which facilitates efficient and speedy fund transfer and messaging towards its valued customers. NIBL plays developing role not only in urban area but also in rural areas. This shows that the bank is genuinely interested in overall development of the country.

Major Findings:

- Letter of Credit is a most widely used financial tool in today's International Trade and Finance.
- NIBL has contributed a lot in the International Trade and Finance by way of providing Letter of Credit facility, apart from other regular banking facilities.
- Businessmen prefer to make payment through L/C while importing goods from abroad than any other instrument (Telex, Draft, Swift etc) because it is the safest mean of payment and it also gives guarantee that the goods (as per the requirement or agreement) will be received.
- From the study of Letter of Credit Business of NIBL, we see that its import transaction is far greater than export. Hence we can say that the import to Nepal, as a whole, is also in increasing trend than export.

5.2 Conclusion

The report has drawn out the operation of Letter of Credit including the Bank, Its origin, evolution, banking history in Nepal and it's working style. L/C acts as an agent between importer and exporter. It provides means of settlement of foreign trade transaction.

NIBL is playing bigger role for the development of international trade. Letter of Credit service provided by the bank contributes in the development of the nation. Usually the procedure of opening L/C is similar to all the banks but some variation can be found in terms and conditions, which differ from bank to bank. It is necessary that all the banks of Nepal follow the directives of the Nepal Rastra Bank and ICC guidelines before opening Letter of Credit.

Nevertheless, NIBL is one of the leading banks in Nepal, which is helping people and the nation as a whole by providing different services and facilities. Its objective is not only to make profit to its shareholders but also to contribute in the development of the Nation.

5.3 Recommendations

With an intense competition at all the area of every sector, NIBL needs to provide services that are prompt, consumer friendly and are less expensive to customers. Letter Of Credit documentation and overall process should be executed within shortest possible time frame. However, in doing so the bank needs to be cautious, as it demands a thorough verification of customer details and documents.

In order to survive in the cut- throat competition decreasing the margin level, that bank takes from its customer and quicker service will not guarantee a good L/C unless detail analysis are done. In order to differentiate services from other banks a unique

approach to consumer service needs to be facilitated such that it includes not only a satisfied customer but further ensure customer delight. Things to be considered are:

- Bringing more promptness in the workflow procedure.
- Adopting efficient marketing strategy to encourage more of the customers to benefit from this facility provided by NIBL.
- Rules laid down by NRB regarding L/C transactions are inconsistent with the international practice. This has caused difficulty to business people for international trade and decreased in the earning of the Banks. Hence it is recommended that the bank focus on coordinating approach for the change of such policy.
- From the figures, tables and pictures presented in this report, it is obvious that NIBL, since the management is taken over by Nepalese, has been going on aggressively to capture more and more of market share, which is good but it is recommended that the creditworthiness of the customer be checked before providing any credit facility.

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