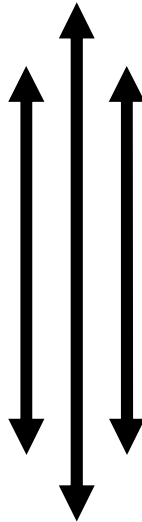


**AN ANALYTICAL STUDY ON PROFIT PLANNING OF  
COMMERCIAL BANK**  
(With Special Reference to Bank of Kathmandu Ltd. and Himalayan Bank Ltd.)

**A THESIS**

**Submitted By:  
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**A Thesis Submitted to:  
Office of the Dean  
Faculty of Management  
Tribhuvan University**



***In Partial fulfillment of the requirements for the  
Degree of  
Master of Business Studies (M.B.S.)  
December, 2013***

# RECOMMENDATION

This is to certify that the thesis

Submitted by:

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Entitled:

## **A ANALYTICAL STUDY ON PROFIT PLANNING OF COMMERCIAL BANK**

**(With Special Reference to Bank of Kathmandu Ltd. and Himalayan Bank Ltd.)**

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**(With Special Reference to Bank of Kathmandu Ltd. and Himalayan Bank Ltd.)**

*And found the thesis to be the original work of the student and written according to the prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirement of Masters Degree of Business Studies (M.B.S.)*

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## DECLARATION

I hereby declare that the work reported in the thesis entitled “***A ANALYTICAL STUDY ON PROFIT PLANNING OF COMMERCIAL BANK (With Special Reference to Bank of Kathmandu Ltd. and Himalayan Bank Ltd.)***” submitted to Office of Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement of the Degree of Master of Business Studies (M.B.S.) under the guidance and supervision of Mr Hari Shankar Pant, Shree Siddhanath Multiple Campus.

Date:December, 2013

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I have tried to cover all the possible matters that I felt, important to sum up the “An Analytical Study on Profit Planning on Commercial Bank, With Special Reference to Bank of Kathmandu and Himalayan Bank Limited.” I am hopeful that this task will be helpful to the students of business studies & to those who want to make further researchers under this topic.

Mr.Deepak Sethi  
Siddhanath Multiple Campus  
Mahendranagar,Kanchanpur.

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## ABBREVIATION

ABBS	Any Branch Banking System
A/C	Accountancy
Amt.	Amount
ATM	Automatic Teller Machine
BOD	Board of Director
BOKL	Bank of Kathmandu Limited
B.S	Bikram Sambat
Co.	Company
COD	Cost of Deposit
CRR	Cash Reserve Ratio
Etc.	Etceetra
FCY	Foreign Currency
F/Y	Financial Year
GDP	Gross Domestic Product
HBL	Himalayan Bank Limited
ICC	International Chamber of Commerce
LABP	Loan Advance & Bills Purchased
LC	Letter of Credit
LDO	Loan Discount and Overdraft
LOAB	Loan Advance and Bill Purchased
Ltd.	Limited
NBBL	Nepal Bangladesh Bank
NGO	Non Government Organization
NRB	Nepal Rastra Bank
N.Rs	Nepales Rupee
O/S	Out Standing
PE	Probable Error
PPC	Profit Planning and Control
RMOD	Resource Other than Customer Deposit
ROA	Return on Assets
ROE	Return on Equity
SCB	Standard Chartered Bank
SCB	SIAM Commercial Bank
SD	Standard Deviation
TB	Treasury bill
YOE	Yield of Equity
YOF	Yield on Fund

# CHAPTER ONE

## INTRODUCTION

### 1.1 Focus of the study:

A profit plan has an immense value in management; it helps in planning and coordinating, if used appropriately, but not a replacement for management. Profit planning is a comprehensive and coordinated plan expressed in financial terms for the operations and resources of an enterprise for some specific period in the future. Profit planning is a comprehensive statement of intentions expressed in financial terms for the operation of both short and long period. It is a plan of the firm's expectation and is used as a basis for measuring actual performance of managers and their units.

“Profit planning is predetermined detailed plan of action developed and distributed as a guide to current operations and as partial basis for the subsequent evaluation of performance. Thus it can say that profit planning is a tool which may be used by the management in planning the future course of actions and controlling the actual performance” (Gupta, 1997; 141)

Every company or institution is established based on the definite goals and objectives. According to the objectives, the company performance is tasks. Mainly two types of institutions such as profit oriented and service oriented instructions are established, but most of them are profit oriented because profit is the lifeblood of the business which not only keeps it alive but also assures the future and makes it sound. Profit planning is an important tool of the firm to achieve the objectives. “Profit do not just happened profits are managed” (Lynch, 1989; 30) so to manage the profit. The management should follow various processes for profit planning because the management process and profit planning and control are related each other.

A profit plan is an advance decision of expected achievement based on the most efficient operating standards in effect or prospect of time it is established against which actual accomplishment is regularly compared.

Profit maximization is the basis objectives of a firm and to make it render reliable service to its customers. Profit is a device to measure efficiency of a firm.

The term comprehensive profit planning and control it defined as a systematic and formalized approach for performing significant phase of the management planning and control function. Especially it involves:

- 1 The development and application of broad and long range objectives for the enterprises.
- 2 The specification of enterprises goals.
- 3 The development of strategic long rang profit plan in broad terms.
- 4 The specification of tactical short range profit plan detailed by assigned responsibility (division, products, projects).
- 5 The establishment of a system of periodic performance reports detailed by assigned responsibility and follow up procedures

In many of the better-managed companies, comprehensive PPC has been identified as a way of managing. It focuses directly up on a rational and systematic approach to management by objectives and realistic flexibility in performing the management process.

Present Issues of PPC directly related with the banking industries:

1. Commercial banks are facing the problem of secured collateral.
2. PPC is affected by intervention of NRB, rules and regulation.
3. Low income, saving and deposit tendency of Nepalese people.
4. Organizational goal, structure and business environment is affected to PPC.

## **Profile of Himalayan Bank and Bank of Katmandu Ltd.**

### **Himalayan Bank Ltd.**

Himalayan Bank was established in 2049 B.S. by a few distinguished business personalities of Nepali in partnership with Employees Provident Fund and Habib Bank Limited, one of the largest commercial bank of Pakistan. It is the first bank of Nepal whose maximum shares are held by the Nepalese private sector. Besides commercial banking services, the bank also offers industrial and merchant banking services. Bank was established with authorized capital Rs. 1 million, issued capital Rs. 77.22 million and paid up capital Rs. 77.22 million. In which, Nepali founder invested 51% share, Habib Bank of Pakistan invested 20% share, employee provident fund invested 14% share and remaining 15% share issued for public. Its Head office lies at Karmachari Sanchayakosh Bhawan, Tridevimarg, and Thamel.

It has some branch, at present there are five branches inside the Kathmandu valley NewRoad, Thamel, Pulchowk, Maharajgunj, and Suryabinayak (moved from Nagerkot). Beside this, it has ten branches outside Kathmandu valley they are in Biratnagar, Banepa, Birgunj Hetauda, Dharan, Pokhara, Tandi, Bharatpur, Butwal and Bhairahawa. The Bank also operates a counter in the premises of the Royal Palace. The bank will be aggressively opening new

branches at different parts of the kingdom to serve its customers better.

HBL has always been committed to providing a quality service to its valued customers, with a personal touch. All customers are treated with utmost courtesy as valued clients. The Bank, wherever possible, offers tailor made facilities to its clients, based on the unique needs and requirements of different clients. To further extend the reliable and efficient services to its valued customers, HBL has adopted the latest banking technology. This has not only helped the bank to constantly improve its service level but has also prepared the bank for future adaptation to new technology. The Bank already offers unique services such as SMS Banking and interest banking to customers and will be introducing more servicing like these in the near future.

HBL is committed to be Bank where **“The Power to Lead”**

Mission of the HBL is to become the preferred provider of quality financial service in the country. Vision of the bank is become a leading bank of the country by providing premium product and service and then ensuring attractive and substantial return for the stakeholders. An objective of the bank is to become the bank of first choice.

#### **Products and Services Provided by HBL:**

Himalayan Bank Ltd has been the innovator in introducing many products. To illustrate, the bank has implemented up till the following products now.

1. Credit Card
2. Tele Banking
3. Any Branch Banking System (ABBS)
4. Automatic Teller Machine
5. PSA Deposit

#### **Bank of Kathmandu Ltd.**

BOK is a Culmination of a comprehensive vision of the promoters to trade the Nepalese economy to never real in the global market. The promoters' comprehensive vision and the government's overwhelming support gave birth to BOK as one of the private sectors banks of the country in 1993 which commenced its commercial business in March, 1995.

BOK was established by a group of distinguished civil servants and renowned businessmen in collaboration with SIAM commercial public co. limited (SCB) a leading bank of Thailand. The collaboration with SCB supported BOK to bring in the technical and managerial

expertise in the Nepalese banking sector.

Upon establishing BOK as one of the reputed banks in a short period, the Nepalese promoters decided to conclude the technical service agreement with SCB and BOK to be arranged by the Nepalese professionals as it could further enhance its business performance years ahead under the Nepalese management. With the well-acclaimed capabilities of the Nepalese management team, BOK has successfully enhanced its capital structure profitability; reach to the customers and image in the market. It has created a position in the industry in a shortest possible span of time.

BOK is proud to be the banker of the leading business houses, Ingo's diplomatic agencies and foreign projects and to be the lead bank in several consortiums financing in the country.

### **Core Objectives of BOK: -**

BOK was established with the objective of stimulating the Nepalese economy and taking it to newer heights. We further aim to facilitate the nation's economy and become more competitive globally. To achieve these, BOK has been focusing on its set objectives right from the beginning, which are the following:

- 1 To contribute to the sustainable development of the nation by mobilizing domestic savings and channeling them to productive area
- 2 To use the latest banking technology to provide better, reliable and efficient services at a reasonable cost
- 3 To facilitate trade by making financial transaction easier, faster and more reliable through relationship with foreign banks and money transfer agencies
- 4 To contribute to the overall social development of Nepal.

### **Present Capital Structure of BOK.**

Share Capital & Reserves:	NPRS. In million
Authorized Capital	1000.00
Issued Capital	500.00
Paid-up Capital	463.58

*Share holding pattern* *percent*

1. Nepalese promoters	43.37%
2. General Public	56.63%
Total	100.00%

(Source: Annual Report of BOK)

BOK, in terms of public participation on equity, is the number one bank in Nepal, In its share holding structure, the general public owns more than 56.63% of its equity and the reaming only by its promoters. Even among the promoter shareholders, no single individual or family holds a substantial proportion. The total shares are widely spread to more than 20000 individual shareholders. It is in the real sense of public limited bank.

BOK, including normal functions, provides the following activities and services:

- Deposit account service
- Credit facilities.
- International trade center.
- Foreign exchange center.
- Inwards/ outwards remittance cheque.
- Gift cheque.
- Business advice.
- Safe deposit locker
- ATM
- Other services.

Since, BOK is established with the objectives of providing prompt and quality services staffs have been increasing. Therefore, it has become successful commercial banks in Nepal.

## **1.2 Statement of the problem: -**

Profit planning is the vital tool, which directs the organization achieving profit. Profit is the very basic primary short term and long-term objective of every business organization. Even increasing ratio of profit is a good symbol of organization. By nature profit is a yardstick judging of managerial efficiency in term of a means of measurement for the success. “Profit is the primary measure of success of the business enterprises.” (Goel & Dean, 1992:37),The profit-planning tool is a newly developed concept as a crucial way in the business organization .By proper profit planning a business can be managed more effectively and efficiently.

Every financial Institutions as a commercial bank must make profit out of its operations for

its survival and fulfillment of the responsibilities assigned major activities of a commercial bank comprises mobilization of resources, which involves cost and profitable deployment of those resources, which generates income. The different interest income over the interest cost, which is popularly called as interest margin, can be considered as the contribution margin in the profit of the bank. The bank attempts to compensate the other operational expenses by generating other income out of non-found based business activities of the bank.

The present studies have to analyzed and examine the application of PPC tool in the commercial banks taking a case of Himalayan Bank and Bank of Katmandu ltd. The study is focused on to seek the answer of the following questions:

1. To what extent, the comprehensive profit planning has been applying in Commercial banks?
2. Do the banks deploy the resources generalization satisfactory?
3. Do the banks mobilize the deposit and other resources?
4. How does the profit plan affect the actual performance of Himalayan Bank & Bank of Kathmandu?

### **1.3 Objectives of the Study**

The primary objective of this study is to appraise HBL and BOK Ltd. appropriately for the application of comprehensive PPC system. The specific objectives of this study are as follows:

1. To analyze the variance of budgeted and actual achievements of deposit collection.
2. To study the growth of the business of the Banks over the period.
3. To analyse the profitability of the banks.
4. To analyse the trend of total deposit, loan & advances and net profit.

### **1.4 Significance of the study**

The researcher study is connected with the profit planning in commercial Banks with a case study of BOK and HBL with the major objectives of examining the proper applicability of profit planning system in the Bank

Profit planning process significantly contributes to improve the profitability as well as the overall financial performance of an organization by the best utilization of resources.

Accomplishment of objective in every organization depends on the application of scarce resources most effectively. Also the functional performance of an organization depends

purely on the use of its resources. Budgeting is the key, to productive functional planning. So all the organization running under commercial principles has to give regards these most important single tools while managing their physical and financial targets. If the planning process of an organization is effective and result oriented, the place of development naturally steps forwards.

Profit planning is the heart of management. It tells us profit is the most important indicator for judging managerial efficiency and do not fast happened for this every organization has to manage its profits. Various functional budgets are the basic tools for proper planning of profit control over them.

Other research study may be useful for those who want to know PPC in BOK and HBL. It may also helpful for future researchers as a reference material.

### **1.5 Limitations of the study:**

In this dynamic world nothing existing is free from information. This study also is not an exception. The researcher has however tried to eliminate the limitation to the best possible extent, yet it suffers from the following limitations.

1. Only the profit planning aspect of the Bank has been analyzed, leaving other area uncovered.
2. The study covers the related data of the Banks from 2005/006 to 2011/012.
3. The data are primary as well as secondary but mostly secondary data has been used.
4. The study only analyse the variance between budgeted and actual deposit collection.

### **1.6 Organization of the Study:**

The study divides into following chapters.

**Chapter I:** First chapter deals with the background of the study, statement of problem, objective of the study, significance of the study, research hypothesis, limitation of the study, and scheme of the study.

**Chapter II:** Second chapter deals with available literature review. It's include conceptual framework, review of the published and unpublished books, journals, articles, previous unpublished masters' degree thesis etc.

**Chapter III:** Third chapter explains the research methodology used in the study, which

includes research design, sources of data, population and samples, data analysis tools etc.

**Chapter IV:** Fourth chapter is the heart of the study. This chapter includes presentation and analysis of data using different financial and statistical tools.

**Chapter V:** Last chapter revolves with suggestion, which includes the summary of the main findings conclusion of the study and recommendations.

Bibliography & appendixes have been included at the end of the study.

## **CHAPTER TWO**

### **REVIEW OF LITERATURE**

#### **2.1 Introduction:**

Review of the literature is supported to revise the eminent literature relating to the past study, which is the base for preparing it. No repetition is made with previous study and proper gap of data is maintained in the study. Some philosophers, writers or researchers have given the contribution on it since many years. There are two parts in the review of literature. They are:-

- 1 Conceptual frame work
- 2 Review of related study

#### **2.1.1 Conceptual Framework:-**

In this chapter, the researcher aims to shed light on the relevant theoretical background of the study being under taken. It comprises the conceptual framework about the commercial banks, its activities, profit-planning concepts, and review of books, previous study. So far this study is concerned with reviewing the profit planning of these two commercial banks. In this connection, the researcher has reviewed various literature in the form of books, newspapers, journals, browsing materials from the concerned websites, previous dissertations in the relevant subject matters etc.

#### **2.1.2 Commercial Bank**

Bank is the financial or business institution, which was established by law. It deals with money bank takes deposit from general people, Joint Stock Company, government, corporation etc. Similarly it takes interest and appropriate mortgage. Commercial banks are organized on a joint stock company system, primarily for the purpose of earning profit. Commercial banks attract deposits of all kinds' current, saving and fixed account. Bank is a moneylender which is different in the sense that the former lends the money which is principally collected from their depositors while later does so from its own resources.

According to shorter Oxford English dictionary "a bank is an establishment for the custody of money its essential duty is to pay their draft on it, its profit arises from its use of the money left unemployed by them." (2005; 107)

“The random house dictionary of the English language defines the bank as an institution for receiving money and in some cases, issuing notes and transacting other financial business”(Stein and Urdang 1985:16).

Banks refer to an institution, which perform the activities related with money and credit. Banks have been traditionally regarded as merely the purveyor of money. But today they are not merely purveyor of money but creator of manufacturer of money in the system.

Theory of credit’ has defined the bank not only as an institution, that borrows and lend money but also the institution for creating credit.

“I believe in that fact the banks are not merely purveyors of money but also in an important sense, manufactures of money.” (Sayers : 1975; 255)

The commercial bank act 2031, under which commercial banks in neap are established and operated, has defined commercial bank as a bank which exchanged money, accepts deposit, advances loans and performs other commercial transactions and which is not specially established with the objectives of co-operative, agricultural, industrial or any other of such kind of specified purpose.

The Act has defined the commercial bank on the basis of its objectives and activities. Referring to the act, a commercial bank:

- 1 Should be established with a specified objective of co-operative, agricultural, industrial of any of such of specific purpose.
- 2 Should accept customer deposit
- 3 Should advance loans and make investments.
- 4 Perform commercial transactions.

“The same act has provided for the modalities of establishing a commercial bank , as per which a commercial bank can be established under the company act as a limited liability company only with the recommendations of Nepal Rastra Bank, the central bank of Nepal” (Commercial Bank Act 2031).

About various definitions of scholars we come to know that bank is a financial or business institution, which accepts deposit, payment of cheque, granting loan, remittance, bank guarantee, and miscellaneous services to people.

### **2.1.3 Evolution of commercial Bank:**

The origination of the term 'Bank' is under dispute among the economist. According to some authorities, the word 'Bank' is derived from the word 'Banco', or 'Banque' all meaning to a

bench. This refers to the fact that early bankers transacted their money lending activities on benches in the market place exhibiting the coins of different countries in different denominations for the purpose of changing and or lending money. Some writers are of the opinion that the word 'Bank' came from the German word 'Banc' meaning joint stock fund.

In its native form, banking is as old as the authentic history and origins of the modern commercial banking are traceable in ancient times. In ancient Greece, around 2000 B.C. the famous temples of Ephesus, Delphi and Olympia were used as depositories for people's surplus fund and these temples were the centers for money lending transactions. The priest of these temples acted as financial agents until public confidence was destroyed by the spread of disbelief in the religion. Later, however for a few centuries, banking as an organized system of money lending receded because of the religious belief that the charging of interest was immoral, however, the banking as we know today, made its first beginning around the middle of 12<sup>th</sup> century in Italy. "The Bank of Venice, founded in 1157 A.D. was the first public banking institution. Following this, in 14<sup>th</sup> century, the Bank of Barcelona and Bank of Genoa were established in 1401 A.D. and 1407 A.D respectively". (Vaish, 1996; 287)

In England, start of Banking can be accounted for as far back as the reign of Edward III. Those days, the Royal Exchanger used to exchange the various coins into British money and also used to supply foreign money to the British men going out of the country. The bankers of Lombardy were famous in medieval Europe as the credit of planting the seed of modern banking in England goes to them when they settled in London in the locality now famous as the Lombard Street.

The goldsmiths there can be considered as the initial Bankers in England as they used to keep strong rooms with watchmen employed. People entrusted their cash to them. The goldsmiths used to issue duly signed receipt of the deposits with the undertaking helped in gaining a further confidence of the public therefore the money were kept with them for longer periods. They were thereby encouraged to lend some part of these funds, which became profitable business to them. Therefore they started offering interest on the deposits to attract more funds. In the course of time independent banking concerns were set up. "The Bank of England was established in 1694, under a special Royal Charter. Further in 1833 legislative sanction was granted for establishment of joint stock banks in London, which served as a big impetus to the development of joint stock banking" (Vaish, 1996; 293). These banks took the initiative of extending current account facilities of withdrawals through cheque.

In India, the ancient Hindu scriptures refer to the money lending activities in the Vedic period. During the Ramayana and Mahabharata eras, banking had become a full fledged

business activity and during the smriti period (after the Vedic period), the business of Banking was carried on by the members of Vaish community. Manu, the great law giver of the time speaks of the earning of interest as the business of Vishyas. “The bankers in the smriti period performed most of those functions which the bank in modern times performs such as the accepting of deposits, granting loans, acting as the treasurer, granting loans to the king in times of grave crises and banker to the state and issuing and managing the currency of the country”. (Vaish, 1996; 287)

“In Nepal, although the monetary history dates back to 1<sup>st</sup> century (Lichhavi Dynasty), the Banking history is comparatively very short. The development of organized banking has started in Nepal only from around the starting of 20<sup>th</sup> century of Bikram Sambat. Nepal Bank Limited, established in B.S.1994 with an authorized capital of Rs. 1 crore and paid up capital of Rs 8 lakh 42 thousand is the first organized bank established in Nepal”.(NRB, 2045)

“Although during the Prime Minister-ship of Ran Prime Minister Ranodwip Singh, an office called 'Tejarath Adda' was established for granting loans to government officials and also to the general public against the security of gold, silver and other valuables, it could not be considered as Bank in real sense as it did not collect deposit. Later after establishment of Nepal Bank, the functions of 'Tejarath Adda' were limited up[to providing loans to government officials only”. (NRB, 2045)

Banking development in Nepal found another break through after establishment of Nepal Rastra Bank, the central Bank of Nepal in 2013 B.S. This has helped organizing the monetary system in the country before which the dual currency system (Indian and Nepalese Currency) were prevailing in the system. Larger sector of economy was none monetized.

In the course of organized development of banking sector, second commercial bank, Rastriya Banijya Bank was established in 2022 B.S. at the state ownership.” Later on, in FY 2039/040, the policy for allowing establishment of foreign joint venture banks was taken with an aim of having fair competition and skill development in banking sector, which had added a new dimension in development of banking in Nepal. Accordingly, Nepal Arab Bank Ltd. (presently renamed as Nabil Bank) has been established as the first joint venture bank in Nepal in 2041 B.S”. ( NRB, 2045).

Similarly, in the year 2042 B.S. second joint venture bank, Nepal Indosuez Bank and in the year 2043 B.S. third joint venture bank, Nepal Grindlays Bank ( currently known as Standard Chartered Bank Nepal) were established .

Afterward, more and more commercial banks were opened in foreign joint venture and

private sectors in Nepal which had contributed a lot to bring the commercial banking at present day position. Bank of Kathmandu & Himalayan Bank Limited established.

#### **2.1.4 Activities of Commercial Bank: -**

Traditionally the primary of banks is essentially accepting deposits and making loans and advances. Commercial Banks are found to be having been defined by their activities.

As per the Commercial Banking act 2031, 'Bank' is a commercial bank established under this act and 'banking transactions' are the activities of accepting deposits from the others for the purpose of lending or investing, repayable on demand or after some stipulated time period by means of generally accepted procedure.

"A banker is one who in the ordinary course of his business honors cheque drawn upon him by person from and for whom he receives money in his current account". (Vaish-1996; 297)

"The functions of receiving money from his customers and repaying it by honoring their cheque as and when required is the function, above all function, which distinguish a banking business from any other kind of business." (Gulshan & Gulshan1996; 275)

"No person or body corporate or otherwise, can be a banker who does not; (a) take deposit accounts (b) take current accounts (c) issue and pay cheque drawn on himself and (d) collect cheque for his customer." (Gulshan & Gulshan, 1994; 282)

From above points, it is clear that a commercial bank's primary activities are two fold viz. one that of accepting depositing deposit from public, which is the major sources of the resources of the bank and another making loans and investments which is basically creating income yielding asset of the bank for fulfillment of its commercial objectives.

The primary activities of a commercial bank have been categorized in two folds as below:

- i Mobilization of Resources &
- ii Deployment of Resources

#### **2.1.5 Mobilization of Resources**

Resources of a commercial bank constitutes, as like in other business institutions,

- (a) The owners' fund.
- (b) The borrowed fund.

##### **A. Owners fund or capital fund**

Owner fund of the bank is the Capital fund, which includes paid up capital, reserves,

reserves, retained earning share premium, non –redeemable preference share. Apart from those mentioned above other reserves and provision items allocated out of profit of the bank are also considered as the supplementary capital fund. Owners' fund is the most dependable source of bank's liquidity.

As per central Bank (NRB)'s guideline, a commercial bank must have paid up capital of Rs1000 million in orders to be established as a national level commercial bank. Further the NRB has also prescribed the capital adequacy norms (the ration of capital fund to the risk assets as per varying weighted assets) to be of at least 12% by the end of Fiscal year 2062/63. Similarly, the commercial banking act 2031 has made a mandatory provision for every commercial bank to build the general reserve out of the allocation of at least 20% of net profit amount each year until the amount becomes double the paid up capital.

The Borrowed fund of a bank constitutes the resources apart from the owners' fund. In a bank, it is mostly contributed by customer's deposit, and some part by the short-term fund borrowed from other banks and central bank.

## **B. Customer Deposits**

Customer deposits are the chief source of commercial bank's resources. It is so much important for a bank for its liquidity supply that banks are often engaged in keen competition for deposit mobilization because the capacity of a bank to grant credit to it's borrowers depends upon it's capacity to mobilize deposits in the banks are accepted from their customers in various types of account opened in the banks by the depositors.

The total deposit of a bank is composed of demand and time deposits. The demand deposits are most volatile and can be withdrawn at any time by their depositors subject to the general rules of the banks governing these deposits. Generally no interests are paid into those accounts.

Demand deposits are usually accepted in current accounts. A current account is running and active account which may be operated upon any number of times during a working day. As per commercial banking act of Nepal, a current account is the bank account having money, which is subject to repayable whenever demanded. These accounts are suitable for businessmen, joint stock companies, institutions, public authorities etc.

The time deposits consisting fixed deposit and partly of saving deposit are called so because these can be withdrawn only after the expiry of the stipulated period for which these have

been made. Banks offer interest on these accounts varying the duration of deposit maturities time deposits are kept generally by individuals, educational institutions, charitable trusts and others having surplus fund for future saving and earning some regular return on it.

The saving deposits are accepted on saving accounts, “the bank account having money which is deposited for the purpose of saving.”(Commercial Bank Act-2031), Banks generally impose certain restrictions on withdrawal from such accounts.

The bank in the name of the depositors keeping fixed deposits opens fixed deposit accounts. Amount in such accounts are called time liabilities of the bank because the money is payable on the expiry of a fixed period of time which the depositors chooses s per his convenience.

The commercial Banking act 2031 defined fixed deposit account as the “bank account, which is having money in it for a specific period of time.”

### **C. Other liabilities**

Resources other than the capital fund and customer deposits are the other liabilities of the bank. It includes short-term borrowed fund from other banks locally or foreign and Central Bank. Such borrowings are called inter bank borrowings which are normally obtained for a very short period and those are meant for meeting temporary liquidity crunch in the bank. The rates of interest on such borrowing depends on the prevailing inter bank interest rate. Other liabilities also include the payables in the account of the bank, which has been arisen during the regular operation of the bank.

#### **2.1.6 Deployment of resources**

Deployment of resources of the bank means utilization of the bank’s fund in such a way that it ensures liquidity as well as gives some earnings for meeting its operating expenses and optimum return on the shareholder’s investment. Thus it is setting up of the best possible assets portfolio, which meets above requirement in the best way. In fact the efficiency of a banker is reflected by this activity.

Every bank strives to maximize its earning by employing its surplus cash by lending it to the prudent borrowers in a manner which in no way impairs its capacity to pay on demand the acquired funds to their owners.

Thus for a banker, deployment of the available resources is a challenging job, because the liquidity and profitability are the opposing consideration to each other. “The secret of successful banking consists in allocating the resources between various forms of competing assets in such a way that a proper balance is stuck between the opposing consideration of

liquidity and profitability. The sound balance will be achieved when the bank has sufficient (and no more than sufficient )cash in hand to meet every claim that is or is likely to be made by its depositors on it and at the same time it earns enough income to pave its way and earns profit for its shareholders. (Vaish-1996; 297)

Therefore the deployment of resources or assets portfolio building of a bank should be guided by major two consideration viz. the liquidity, and the profitability.

#### **A. Assets portfolio for liquidity**

Liquidity in a bank means its capacity to convert its deposit liabilities into cash. As major portion of a bank's resources constitute customer deposit which are subject to repayable on demand or after some time as the case may be, a banker can not afford to neglect his cash position so as to be always capable to meet withdrawal of the deposit. Therefore bank keeps adequate amount of liquid asset in the form of cash in their vault and balance at their account in Central Bank (NRB). As said earlier, Maintenance of excess liquid assets that required is detrimental to the profitability objective of the bank as the idle cash gives no return rather it involves the cost of carrying (insurance cost, guarding cast etc). (Vaish 1996; 300)

The Central Bank fixes the mandatory cash reserve ratio (CRR) from time to time. Current CRR fixed by NRB for commercial Banks is as below:

- i. Balance to be maintained at NRB Account: At least 7% of current and saving deposits amount and 4.5% of fixed deposit amount.
- ii. Balance to be kept in Bank's vault: at least 3% of total deposit liability (NRB Circular 2005/2006)

(Source: Directives of Nepal Rastra Bank, Banking Operation Department, 2005)

#### **B. Investments**

Investment includes the fund invested for buying government and other stock exchange security, treasury bills, fund placement at call account with other bank etc. Such investments can easily be liquidated if required thus has a feature of liquid assets as well as giving some yield out of it also. Therefore it is in second line in terms of liquidity apart from cash and balance at NRB.

### **C. Loans, Overdrafts and Discounts (LDO)**

Banking business essentially involves lending. In fact the deposits are accepted for lending or investment. This is the most profitable activity of a commercial Bank. Banks being a business proposition, it must declare handsome dividends to its shareholders. “Unless the profit outlook of a bank is bright, new funds will be difficult to obtain.” ( Vaish, 1996; 302).

“Commercial Banks generally lend for short-term commercial purpose to finance the need of trade and commerce. As the fund available for lending with the banks, are mostly the fund mobilized from the depositor, a commercial bank should carefully consider the safety margin before granting the loan. The banker should be extra careful in selecting the borrowers. Generally banks lending is guided by their lending policies. General principles of a sound lending policy of a bank are as follows.” (Gulshan & Gulshan: 1994; 278).

**A. Safety:** Bank’s lending should be secured by way of tangible securities and/or personal security (guarantee) of the borrower.

**B Liquidity:** As the bulk of fund in the bank are short-term fund received as deposits, it is prudent to confine into short-term advances, which can be repaid quickly.

**C. Profitability:** The major income of a bank comes from the difference in interest earned from the borrower and interest paid to the depositors, which is termed as ‘Spread’. The interest rate of lending depends upon the purpose of advance and the risk involved. Greater the risk involved higher will be the rate of interest charged.

**D. Risk Diversifications:** The famous saying “don’t put all the eggs in one basket” is the fundamental base of the principle of risk diversification. As there is risk in every advance, bank should spread the risk by lending to larger number of borrowers.

Generally banks make their advances in the forms of loans, overdrafts, Cash credits and Bills discounting.

In a loan account, the entire amount is disbursed to the borrower, which is repayable in installments or in lump sum on the expiry of loans. Interest is charged on the entire loan disbursed to the borrower. The types of loans may be pledge loan, demand loan, Hire purchase, import fiancé (transit loan), Export finance (packing credit), loan against fixed deposits, against government securities, against shares etc.

Overdrafts are granted in current account of a customer. It is the permission given to

overdraw from the account up to a certain limit allowed to the person on revolving basis. Interest is charged on daily outstanding overdrawn amount only. Normally such facility is given against the security of collaterals, fixed deposits, government securities, shares, life insurance policies etc.

Cash Credits are similar to overdraft in terms of operation but it is provided to the borrower as working capital finance, normally to traders, industrialists, framers etc. in cash credit facility, unlike in loans, the borrower shall enjoy the flexibility of drawing the amount up to the sanctioned limit anytime they require fund during the validity of limit. As the interest is charged only to the actually utilized amount on daily basis, the borrower can repay instantly upon receipt of proceed in order to minimize their interest liability. Generally such facilities are availed against security of pledge or hypothecation of stocks of trade commodities along with collaterals.

Discounting of Bills by a bank actually is buying the bills of borrower, which are self-liquidating nature. By means of endorsement on the documents, the title on the payment upon liquidity is transferred in favor of the bank that discounts it. Bill may be clean or documentary. If it is a clean negotiable cheque, drafts, bills of exchange payable at sight or after certain tenor, then it is called clean Bill and if the instrument is accompanied with other trade documents (commercial invoices, transport documents etc.) it becomes the documentary Bill. Bills discounting is short-term credit availed by the bank in which bank gives the value of the bill (called negotiation) deducting some amount (usually the interest until the period of its possible realization) from the face value.

### **Concept of Spread**

Deposit mobilization activity of banks is a costly affair. The bank has to incur expenses toward payment of interest on the interest bearing deposits accepted by the bank. Such expense is called interest Expense. For a better profitability, a business concern should be careful in minimization its cost by marketing low cost deposits and building optimum portion of interest free deposits in his deposit mix.

Deployment of resources in income generating assets (loans and investments) is the income yielding activities of the Banks. Higher the proportion of loan and advances in the asset portfolio, higher will be the yield on fund. As the interest income is the major contributor of income of a Bank, the banker should be careful in realization of interest and enhance the profitability. The difference of interest earned from lending and interest expenses incurred in

deposit is called the spread. In other words spread is the net income of the bank from which banks have to meet their other operational costs and give out the dividends to the shareholders. Therefore Bankers attempt to increase their spread in order to improve their profitability. A banker can attempt to maintain higher spread by minimizing the average cost of deposit and maximizing the average yield on fund. But as per the current regulatory provision of NRB, the interest spread of a Bank can be maximum 5% only.

### **Loan Loss Provisions**

The Central Bank (NRB) has made a mandatory provision for the entire bank to classify their outstanding LDO on the basis of aging into four grades viz. pass loan, Substandard, doubtful and Loss (BOD, NRB, 2001). The loans falling under the respective grades are identified on the basis of the overdue position from the date of maturity of the loan and the amounts shall have to be allocated from net income in order to provided for against the loan loss at various rates (from 1% to 100% if loan amount depending on the grade in which a particular loan account falls). Such allocated amount is called Loan Loss Provision amount and is treated as the expenses items. Therefore, in order to improve the profitability, the banker should be more attentive toward timely realization of dues so that the amount of loan loss provision may be maintained at the least possible extent.

### **Other income generating activities of the Bank**

Banks do some other kind of business, besides deployment of funds, which are popularly, bank guarantee transactions, issuing Letter of Credit, cheque/drafts collection, remittances, etc. in such activities banks do not have to involve their fund and yet they are charging some fee as commission for such services provided. These transactions are called non-funded transaction. While issuing a Bank guarantee, the banker is issuing a guarantee letter on behalf of his client guaranteeing the performance of the client and assuring the employer of paying him the amount of guarantee in case the client fail to perform. Bank guarantee liabilities are the contingent liabilities of bank, which shall become actual liability only when the client fails to perform as per the contract with the employer.

Letter of Credit (L/C) is the instrument widely used in export import transactions. Banks issue L/C assuring the seller for making payment of the good (up to the value and currency of the L/C), provided the terms and conditions mentioned in the L/C are fully complied with. By means of this facility provided by the bank, the international trade has been made possible in

the country. UCPDC (Uniform Custom and Practices of documentary Credit) published by ICC (International Chamber of commerce) is the literature, which provides the uniformity in the L/C transactions worldwide. Besides this, the directives issued by Nepal Rastra Bank, Foreign Exchange Department, largely guide the L/C transactions of commercial Banks. Letter of credit issuance is also a contingent liability for a bank. Banks earn income in the form of commission while issuing L/C. Further, in case if foreign currency L/C, if the client does not have his own source of foreign currency for making payment under L/C, it has to buy the same from commercial banks, on which banks may earn profit on sale of Foreign Currency (FCY). Generally the Banks have to maintain sufficient balance of convertible FCY in order to meet their L/C payment in the currency stipulated. When the exchange rate is in upward trend, banks gain by revaluation on FCY reserves.

### **Concept of Burden**

During the establishments and operation of a bank, it has to incur various kinds of expenses besides the expenses incurred for interest payments. Such expenses are employee's expenses, administrative expenses, depreciation on fixed assets, other operating expenses, and expense for loan loss provision, interest suspense expenses. Employ bonus expenses, expenses for income tax provisions etc. all such expenses other than interest expenses cumulatively form a burden in order to break even. However the other income (income other than interest income) earned by the bank from their other activities besides fund lending contributes to lowering the burden thereby increasing the profitability of the bank. Therefore the net burden (other expenses less other income) has been termed as Burden.

### **2.1.7 Role of Commercial Banks in the development of the economy**

Commercial Banks play an important role in directing the affairs the economy in various ways. The operations of commercial Banks record the economic pulse of the country, the size and composition of their transaction reflect the economic happening in the country Commercial Banks have played a vital role in giving the direction in economic growth over the time by financing the requirement of industries and trade in the country .By encouraging thrift among the people, banks have fostered the process of capital formation in the country. In the context of deposit mobilization, Commercial banks induce the savers to hold their savings in the form of bank deposits thus help bringing the scattered resources into the organized banking sector which can be allocated to the different economic activities. In this

way they help in country's capital assets formation. Through their advances, Banks also help the creation of income out of the economy. "In a planned economy, banks make the entire planned productive process possible by providing funds to the public sector, joint sector or private sector for any type of organization. All employment, income distribution and other objectives of the plan as far as possible subsumed into the production plan which banks finance." (Vaish, 1996; 282)

The importance of commercial banks in directing the economic activities in the system is immense. Not only in the highly developed economies where the commercial and industrial activities are paralyzed in the absence of banks, even in the developing countries' economy are most of the economic activities particularly of organized sectors bank based. Therefore, in a nutshell it can be said that the growth of the economy is tied up with the growth of the commercial banks in the economy.

## **2.2 Profit Planning as a concept**

Profit planning involves selection of defined periods of time for the strategic and tactical profit plans (often five years and one year, respectively) in other words profit planning is a comprehensive statement of intentions expressed in financial terms for the operation of both short and long period. It is a plan of the firm's expectation and is used as a basis for measuring the actual performance of managers and their units. A profit plan has a immense value in management, it helps in planning and co-coordinating if used appropriate, but not a replacement for management. Profit planning is a comprehensive and co-coordinated plan expressed in financial terms, for the operations and resource of an enterprise for some specific period in the future. "A profit plan or budget is the formal expression of the enterprises plans and objectives stated in financial terms for a specified future period of time." (Fremgen, 1973; 144)

"Profit planning is a predetermined detailed plan of action developed and distributed as a guide to current operations and as a partial basis for the subsequent is a tool which may be used by the management in planning the future course of actions and controlling the actual performance."(Gupta, 1992; 521)

Profit plan is estimation and predetermination of revenues and expenses that estimates how much income will be generated and how it should be spent in order to meet investment and profit requirements. In the case of institutional operations it presents a plan for spending income in a manner that does not result in a loss

The term comprehensive profit planning and control is defined as a systematic and formalized approach for performing significant phase of the management planning and control functions specially it involves:

- 1 The development and application of broad and long range objectives of the enterprise.
- 2 The development of strategic long range profit plan in broad terms.
- 3 The specification of enterprises goals.
- 4 The specification of tactical short range profit plan detailed by assigned responsibility (Division, Products, projects).
- 5 The establishment of a system of periodic performance reports detailed by assigned responsibility and follow up procedures.

In many of the better-managed companies comprehensive PPC has been identified as a way of managing it focuses directly up on a rational and systematic approach to management by objectives and realistic flexibility in performing the management process.

A profit planning and control program can be one of the more effective communications network is in an enterprise. Communication for effective planning and control requires that both the executive and the subordinate have the same understanding of responsibilities, ensures a degree of understanding not otherwise possible. Full and open reporting in performance reports that, focus on assigned responsibilities likewise enhance the degree of communication essential to sound management.

“Profit planning is an example of short range planning. This planning focuses on improving the profit especially from a particular product over a relatively short period of time. Therefore as used here, it is not the same as corporate planning of a cost reduction program” (Terry, 1968:2).

Profit planning involves streamlining activities in order to get employees profit minded and to secure maximum benefit from minimum effort and expenditure. Best results seem to be obtained by assigning a profit planner to investigate all the factors affecting the profit obtained from a single production the planner is given the right to probe the economics, the organization. The mode of operations, the pricing, the marketing or any fact of making and selling the product that in his judgment affects profit accruing from that product. The concentration of profit efforts upon one product and the right of the planner to cross traditional functional boundaries of the enterprise of translate needs from one group of another and to obtain concurred profit building efforts among those who can affect profits are

the fundamental factors that contribute to the success of profit planning.

A profit plan is an advance decision of expected achievement based on the most efficient operating standards in effect or and prospect of time it is established against which actual accomplishment is regularly compared.

Profit Planning through volume of cost analysis, however, is a modern concept of management planning tools designated primarily for industrial enterprises. It involves a study of what a business cost and expenses should be and will be at different level of operations and it include a study of the resultant effect up to due to this hanging relationships between volume and cost.

### **2.2.1 Profit**

#### **Meaning and Concept of profit: -**

Profit is as important to a firm as water to the fish. Profits are the excess of income over cost of production and services. Profit is the amount available for ownership or equity after payments are made to all other factors used by the firm. "Profit is the basic elements of profit plan so that the concept of profit planning may not be complete idea of profit. According to oxford dictionary profit means a) financial gain b) amount of money gained in business especially spent. Advantage or benefits gained from something." (Hornby- 1992; 5.67)

According to F.B Hawley, profit is the reward for risk taking in business. If the entrepreneur dies not receive the reward, he will not be prepared to undertake the risks involved in the business. This profit of the entrepreneur exceeds the ordinary return on capital. Entrepreneur would not be ready to undertake the risks.

According to Schumpeter, profit is the reward for innovations. The objective of innovation is to reduce cost of production and cause gap between existing price of the commodity and its new cost. The innovation may come in many forms, such as introduction of new production technique, or a new machine, or plan, a change in internal organizational structure of the firm.

Profits around which all enterprises activities directly or indirectly revolve play the significant role for judging the managerial efficiency. In absence of profit nobody can think about the long-term survivability of the enterprises.

### **2.2.2 Planning: -**

Planning is the process of developing enterprises objectives and selecting a future course of action to accomplishment them. It includes developing premises about the environment in which they are to be accomplished. Planning is the basic foundation of PPC. We should be clear in the concept of planning. “According to oxford Dictionary”, “Planning means:

- 1 (To do something) arrangement for doing or using something, considered or workout in advanced.
- 2 Why of arrangement something especially when shown on a drawing scheme.
- 3 Go according to plan” (Hornby, 1992; 5.45).

“Planning is deciding in advance what is to be done in future.” (Bhusan, 1976; 362)

A planning process includes setting goals, evaluating resources forecasting by different methods and formulating a master plan. Planning depend upon the organized objectives. For the planning purpose a firm’s objectives can distinguish mainly three, the first is prime, the second is instrumental objectives are aims for accomplishment of more basis aim. For this purpose the company has established divisional departmental and individual job objectives. Specific objectives are those objectives that have been specified as to tome and magnitude which is known as goals. As a result of specifying a time period and a target amount, this goal is capable of giving specific guidance to various senses of management planning .Objective setting of a firm of very difficult. Unfortunately, most top management fails to develop a clear and operational statement of company objectives. More carefulness is necessary for this tedious job. Carefully stated firm’s objectives would yield at least the following benefits.

- 1 Company objectives provide the ultimate criteria for resolving difficult company decisions and
- 2 Company objectives are the basis for long-range profit planning.

Planning is the process of developing enterprises objectives and selecting future course of action to accomplish them. It includes.

- 1 Establishing enterprises objectives,
- 2 Developing premises about the environment in which they are to be accomplished,
- 3 Decision-making.
- 4 Identifying activities necessary to translate plans in to action, and
- 5 Current re-planning to current deficiencies.

The planning processes both short and long term is the most crucial component of the whole system. It is both foundation and the bond for the other elements because it is through the planning process that we determine what we are going to do. How we are going to do it and who is going to do it and who is going to do it. It operates as the brain centre of an organization and like the brain it both reason and communicate.

“Planning is the conscious recognition of the futurity of present decision. Planning is the feed forward process to reduce uncertainty about the future. The planning process is based on the conviction that management can plan its activities and condition that state of the enterprise that determines its density”. (Pandey, 1991; 554)

Planning could be taken as the tools of achieving organizational goals efficiently and effectively from the selection of various alternatives with in an acceptable time frame. Planning consists in setting goal for the firm both immediate and long- range considering the various means by which such goals may be achieved and deciding which of any variables alternatives means would be best suited to the condition express prevail.

The essence of planning is:

1. To accomplish goals
2. To reduce uncertainty
3. To provide direction by determining the course of action in advance.

Planning is determined course of action for achieving organizational goals or objectives effectively and efficiently at a fluid environment with a certain time frame through the selection of various alternatives. On the other hand it holds accountability and responsibility about result to individual. A full appreciation of the firm task requires distinguishing among three types of company’s activities, which we call strategic planning, management control and operational control. The strategic planning is a important function of top management. Planning requires the management to setting a future state toward which effort will be directed i.e. objective, assessing the organization’s resources, i.e. what the organization is going to work with, assessing the current and lately’ determine how and when to allocate resource accomplish the objective. Planning on the other hand is selecting objective and determining a course of action including allocation resources in order to achieve those objectives in a specific time period. Planning states what, when, and how things will be accomplished. An adequate planning is necessary for control of operations.

### **2.2.3 Types of planning**

#### **i Corporate planning**

Corporate planning means the systematic process of setting corporate objectives and making strategic decisions and developing the plans necessary to achieve these objectives.

Corporate planning is one part of profit plan. It was first started in the USA in 1950, and it is however being used in one form or another in many companies there.

“Corporate planning is to determine the long-term goals of a company as a whole and then to generate plan designated to achieve these goals bearing in mind probable change in its environment. He pointed out the premises of the corporate planning are:

- 1 Before drawing up a plan, which is designed to do something, decide what you want it to do.
- 2 In these days of rapid change it is necessary to look ahead as far a possible to anticipate these changes.
- 3 Instead of treating a company as a collection of department, treat it as a corporate whole.
- 4 Take full account of the company’s environment before doing up any up any plan.”(Robertson,1968; 535)

Long term planning is included in corporate planning. Corporate planning often is considered synonymous with long-term planning. The main objectives of corporate planning are as follows.

- 1 Achieving objectives.
- 2 Embodiment of goals and objectives in the Enterprises.
- 3 Formulating realistic and attainable objectives.
- 4 Clarity and adequacy of goals and objectives.
- 5 Communication of goals and objectives.
- 6 Involvement of personnel in developing the goals of the enterprises.

#### **ii. Strategic long range planning: -**

Strategic plan is a road map for the future of the organization. It is a long range plan for five years and more. Top management prepares it. It is the means for implementing corporate strategy. It provides broad direction to take the organization where it wants to be in the long run. Its thrust is to search sustainable competitive advantage for the organization.

Strategic plan establishes overall mission, objectives and strategic for an organization. It

makes strategic choice about future courses of action from among the relevant strategies. Policies for acquisition and deployment of resources are also specified.

- 1 Mission is the reason for the existence of an organization. It identifies product, customer and competitive advantage.
- 2 Objectives are desired outcomes in terms of results to be achieved strategies are broad plans to achieve objectives.

“Strategic planning is the careful, deliberate, systematic taking of decisions which affect or are intended to affect the organization as a whole over long period of time.” (Steiner & Miner: 1972; 5.15) Strategic planning is the formalized long range planning process used to define and achieve organizational goals

Basically the long range planning is more important for broad and long living enterprises. A long-range planning is closely concerned with the concept of the corporation as a long living institution the planner must include the following factors in his plan from the analysis of available information.

- a) Probable future opportunity.
- b) Uncertainty and
- c) Challengers.

Strategic planning is a decision making process such decision should be related about

- Determination of goals, objectives and strategies.
- The level and direction of capital expenditure.
- The accession of new sources of funds
- Organization design and structure etc.

### **iii. Tactical short term planning: -**

Tactical plan is a short-range plan. It is developed for a short period of time usually a year, initially by quarters and by months for the first quarter. A tactical planning is done at all level and involves directing the organizations activities to achieve overall its strategic objectives consistent with the organization’s mission and policies. Standing plans provides consistency by and efficiency for non-going operations, and single use plans are developed for unique situation. Projects are short-term plans designed to achieve objective within large-scale programs. Short-term plans cover about a year, and are less formal and detailed than long-range plans, which usually cover more than three months. The short range planning is

selected to conform to fiscal quarter for years. Because of the practical needed for conforming plans to accounting periods and the some. What arbitrary limitation of the long range to three to five years is usually based as has been indicated on the prevailing belief that the degree of uncertainty over a long period makes planning of questionable value.

#### **2.2.4 The Role of Forecasting in Planning**

The forecasting is to take future decision at present from the analysis of relevant factors of past and present situation. It is an integral part of decision-making activities of management.

An organization established goals and objectives seeks to predict the environmental factors that selects action all that is hopes will result in attainment of goals and objectives. The need for forecasting is increasing as management attempts to decrease its dependence on change and become more scientific in dealing with its environment. Since each area of organization is related to all others. A good or bad forecast can effect the entire organization.

“It should be realized that building is not merely forecasting although forecasting is form of he basis of budgeting. Forecasting is estimate of the future environment with in which the company will operate. Budgeting or planning on the other hand involves the determination of what should be done, how the goals may be reached and what individual units are to be assumed responsible and be held accountable. Budget provides orderly way to attain goals and also provides a time schedule for future action to produce. Measure result” (Pandey; 1991; 576)

Forecasting is indispensable in planning. Forecasts are statement of expected future conditions definite statements of what will actually happen are partially impossible. Expectations depend upon the assumptions made. If the assumptions are possible the forecast has a better chance of being useful forecasting assumptions and techniques vary with the kind of planning needed.

The short-term forecasting is needed in budget making. A budget set for the following year will be much useful. It is regarded to sales levels, which will eventuate rather than nearly to current sales level. As budget distributed according to current sales may establish policy as to lines of emphasis, but will obviously required successive adjustment if sales levels changes.

#### **2.2.5 Forecasting Vs planning: -**

Planning and forecasting often are confusing of being the same. But forecast is not a plan, rather is it a statement and for a quantified assessment of future conditions about a particular

subject based on one or more explicit assumptions, planning on the other hand, involves the use of forecast to help to make good decisions about most attractive alternatives for the organization. Thus a forecast seeks to describe what will happen, where as a plan is based on the notion that by taking certain action how the decision maker can affect subsequent events in a given situation and thus influence the final results, in the direction desired. Generally speaking, forecasting and forecasts are inputs to the planning purpose.

### **2.3 Purpose of Profit Planning: -**

A comprehensive profit planning is a systematic and formularized approach for stating and communicating the firm's expectation and accomplishing management in such a way to maximize the use of a profit plan and to achieve the maximum benefit from the resources available to an organization over a particular span of time. The maximum objective of profit planning is to assist in systematic planning and controlling the operations of the enterprise.

The purposes for the application of profit planning are:

- 1 To state the firm's expectation (goal) in formal terms clearly to avoid confusion and facilities their attainment.
- 2 To communicate expectation to all concerned with the management to the firm so that they understood, supported and implemented.
- 3 To provide a detailed plan of action for reducing uncertainty and for its proper direction of individual and group efforts to achieve goals.
- 4 To coordinated the activities and efforts in such a way that the use of resources in maximized.
- 5 To provide a means of measuring and controlling the performance of individuals and units and to supply information based on which the corrective action can be taken.

#### **2.3.1 Long range and short range profit plan**

Two types of plans are developed; one strategic (long-range) and another tactical short range. The former profit plan takes a time horizon of 5to 20 years and the later for short period. The long range planning is a picture of more summary data. A part of this plan is more or less informal as presented by tentative commitments made by the executive committee in the organizational planning season. The formal portion of long-rang profit plan includes the following component detailed by each year.

- 1 Income statement

- 2 Balance sheet
- 3 Capital Expenditure plan
- 4 Personal Requirements
- 5 Research plan and
- 6 Long Rang Market Penetration plan

Thus the long rang profit plan covers all the area of anticipated activity; sales expenses, research and development, capital expenditure, cash, profit and return on investment.

The short-range tactical profit plan shows the primarily annual results, the detail by months, responsibility and products; in an organization these annual summaries should be prepared.

To provide a general understanding of the profit plan and to provide an overall view of the comprehensive short-range profit plan.

According to Galenn and other, it is possible for the firms to develop these two profit plans for all aspects of the operations. Assuming participatory planning and receipt of the executive instruments, the manager of each responsibility center will immediately initiate activities within his or her responsibility center to develop strategic profit plan and tactical profit plan. Certain format and normally the financial function should establish the, general format, amount of detail, and other relevant procedural and format requirements essentially for aggregation of the plan. All these activities must be coordinating among the centers in conformity with the organization structure.

The preparation of long-rang profit planning in addition to short range profit planning is also viewed as a total planning concept of business. Long range planning is essential to maintain the annual profit at improving level. The ultimate measure of the success of a business in generally based on growth in the volume of sales, increasing return on capital investment, efficient organization and these are all long-term consideration.

## **2.4 Budgetary Control**

### **2.4.1 Meaning of Budgeting and Budget:-**

A budget is a detailed plan outlining the acquisition and use of financial and other resources over a given period of time. It represents the plan for the future expressed informal quantities terms. The act of preparing a budget is called budgeting. The uses of a budget to control a firm's activities are known as budgetary control.

“A budget is a detailed plan expressed in quantitative terms that specifies how resources will be acquired and used during a specified period of time. The procedures used to develop a

budget constitute a budgeting system”. (Hilton, 2005; 404)

According to fremgen, a budget is the quantitative expression of a proposed plan of action by management for a future time period and is an aid to the coordination and implementation of the plan. Budget is defined as a comprehensive and coordinated plan, expressed in financial terms for the operations and resources of enterprises for some specified period in the future.

According to his definition the essential elements of a budget are:

- 1 Plan
- 2 Operation and resources
- 3 Financial terms
- 4 Specified future period
- 5 Cooperation

Therefore, we can say that budget is a quantitative expression of a plan of action and an aid coordination and control. Basically, budgets are forecasted financial statement formal expressions of managerial plans.

### **Budgeting: As a Device of Profit Plan**

Budgeting, as a tool of planning, is closely related to the broader system of planning in an organization. It serves basically as a device for management, control; it is rather pivot of any effective scheme of control. “Budgeting is the principle tool of planning and control offered to management by accounting function.”(Welsch, 2005; 632) The prime objective of budgeting is to assist in systematic planning and in controlling the operations of the enterprises. In fact budgeting is best sources of communication and an important tool in the hands of management. Since, budgeting deals with fundamental polices and objectives, it is prepared by top management. A formal budget by itself will not ensure that a firm’s operations will be automatically geared to the achievement of the goals set in the budget. For this to happen, the top-level managers and lower level employees have to understand the goals and support them and coordinate their efforts to attain them.

A budget is comprehensive in that all the activities and operations of an organization are included in it. It covers the organization as a whole and not only some segments. The budgets are prepared for each segment of an organization. These are integrated into an overall budget for the entire organization. The overall budget is referred to as the master budget. Budgeting is a device of a planning and control that serves as a guide to conduct operation and a basis for evaluating actual results.

The main and objectives of budgeting are:

- I. Explicit statement of expectations

II. Communication

III. Coordination

IV. Expectations as a framework for judging performance

### **2.4.2 Essentials of an Effective Budgeting**

An effective budgeting system should have some essential to ensure best results. The following are the chief characteristics of an effective budgeting.

- a) Sound forecasting
- b) An Adequate and planned Accounting System
- c) Efficient Organization with Definite lines of Responsibility
- d) Formation of budget committee
- e) Clearly defined business policies
- f) Availability of statistical information
- g) Support of top management
- h) Good reporting systems
- i) Motivational approach

(Source: Goet, Bhattarai & Gautam 2063)

#### **A. Sound forecasting**

Forecasts are the foundation of budgets, these forecasts are discussed by the executives and when most profitable combinations of forecasts are selected they become budgets. The sounder are the forecasts better results would out of the budgeting system.

#### **B An Adequate and Planned Accounting System**

There should be proper flow of accurate and timely information in the enterprise, which is, must for the preparation of budgets. Only having an adequate and planned accounting system in the firm can ensure this.

#### **C. Efficient Organization with Definite Lines of Responsibility**

An efficient adequate and best organization is imperative for budget preparation and its operation. Thus a budgeting system should always be supported by a sound organization structure demarcating clearly the lines of Authority and responsibility Not only this, there should be a true delegation of authority from top to low levels of management. This will provide adequate opportunity to all executives to make decisions and also to participate in the function of budget preparation. Thus, an efficient organization helps not only in budget co-

ordination but also plays important role in budget co-ordination and operation.

#### **D. Formation of Budget Committee**

As mentioned earlier, Budget committee receives the forecasts and targets of each department as well as periodic reports and finalizes. And also approves the departmental budget. Thus in order to make a budgeting system more and more effective, a budget committee should always be set up.

#### **E. Clearly Defined Business Policies**

Every budget reflects the business policies formulated by the top management. In other words budgets should always prepared taking in to account the policies set for particular department or functions. But for this purpose, policies should be precise and clearly defined as well s free from any ambiguity.

#### **F. Availability of Statistical Information**

Since budgets are always prepared and expressed in quantitative terms. It is necessary that sufficient and accurate relevant that should be made available to each department. Such date may not be available from accounting system alone and therefore they may be processed through statistical techniques. These data should be as far as possible, reliable accurate and adequate.

#### **G. Support of Top Management**

If a budget program is to be made successful, the sympathy of each member of the management team towards it should starts preferably from top i.e. chairman. The enthusiasm for budget operation as well as direction for it should initiate and come from top.

#### **H. Good Reporting Systems**

An effective budgeting system also requires the presence of a proper feedback system. As work proceeds in the budget period, actual performance should not only be recorded but it should also be compared with budgeted performance. The variations should be reported promptly and clearly to the appropriate levels of management.

## **I. Motivational Approach**

All the employees or staff other than executives should be strongly a properly motivated towards budgeting system. In an organization it is needed to make each staff member feel too much involved in the budgeting system. To meet this end, motivational approach towards budgeting should be followed.

### **2.5 Fundamental Concepts of Profit Planning**

The fundamental concepts of PPC include the underlying activities or tasks must generally be carried out to attain maximum usefulness from PPC. These fundamentals have never been fully codified. An outline of the fundamental concepts of profit planning and control are:

1. Managerial involvement and commitment
2. Organizational adaptation
3. Responsibility accounting
4. Full communication
5. Realistic expectation
6. Flexible application
7. Timeless
8. Individual and group recognition
9. Zero base budgeting
10. Activity costing
11. Behavioral view point
12. Management control using PPC
13. Follow up (Goet, Bhattarai & Gautam 2063;1.3)

Each of these fundamentals is discussed briefly in the following paragraphs. And it's tried to proof to what extent they are playing the role to make PPC a meaning full and a comprehensive approach.

#### **Managerial involvement and commitment: -**

Managerial involvement entails managerial support, confidence, and participation and performance orientation. All levels of management especially top level management should consider following points in order to make PPC program successful. Managerial support, confidence, participations and performance orientations include managerial involvement. All

level of management especially top level management should consider following points in order to make PPC program successful.

- 1 Understand the nature and characteristics of profit planning and control.
- 2 Be convinced that this particular approach to manage is preferable for their situation.
- 3 Be willing to devote the effort required to make it operative.
- 4 Support the program in all its ramifications.
- 5 View the results of the planning process as performance commitments.

“For the comprehensive profit planning and control (PPC) program to be successful it must have the full support of each a members of management, starting with the president the impetus and direction most come from the very top.”(Goet, Bhattarai & Gautam 2063;1.4)

### **Organizational adaptation**

A profit planning and control programmed must rest upon sound organizational structure for the enterprise and a clear-cut designation of lines of authorities and responsibilities. The purpose of organizational structure and the assignment of authority is to establish a frame work with in which enterprise objectives may be attained in a co-ordinate and effective way on a continuing basis. The responsibility for the obligation of each departmental manager should be well clarified. Whatever may be the nature and sense of organizational structure, one should always bear in mind the fact that no organizational structure can be taken as ends itself but it should always be treated as means or tools to attain the goal. “In conclusion the organizational involvement includes.

- 1 Delegation of authority and responsibility to each functional sub. Units.
- 2 Sub-divide the whole organization into different functional subunits
- 3 Each subunits should prepare its own annual or periodic plan
- 4 Based upon plan prepared by subunits a master plan is to be prepared by higher management.”(Goet, Bhattarai & Gautam, 2063; 1.4)

### **Responsibility Accounting**

In order to set up profit planning and control on a sound basis, there must be a responsibility accounting system that is one tailored first and foremost to the organizational responsibilities. A responsibility accounting system can be designed and implemented on a relevant basis regardless of the accounting system standard cost system, direct costing systems, and so on.

Therefore PPC requires responsibility accounting system.

### **Full communication: -**

Communication can be defined as an interchange of thought or information to bring about a mutual understanding between two or more parties.

Communication can be either of dialogue messages or understanding from working together. Although most of the management gives least importance on communication but it is the most important thing for any organization observation and control. Most of the organization faces lot of problem due to bad communication system.

For profit planning and control; effective communication means development of well defined objectives specification of goals, development of profit plans and reporting and follow up activities related to performance evaluation for each responsibility center. Communication for effective planning and control requires same understanding of responsibilities and goals in both the executives and subordinates.

### **Realistic Expectation: -**

Perfection on setting goal or objectives of the future sales, production levels, costs, capital expenditures, cash flow and so on determines the success of profit planning and control programmed. So, for profit planning and control purpose, a realistic approach with time dimension and external and internal environment that will prevail during the time span should be considered. This is called realistic expectation.

### **Timeliness: -**

‘Time and Tide wait for none’. Whether an individual or an entity remains idle or busy, time passes at the same rate. The problem of the manager in one hand is to accomplish the planned activities in a given time and on the other hand is to prepare the plan itself phasing of the planning is of two types:

- 1 Timing of planning horizons and
- 2 Timing of planning activities.

“Planning horizons refers to the period of time into the future for which management should plan. Decision made to the organizations obviously can affect only the future. No present decisions can effects or change the past, since all managerial decisions are futuristic each management is faced with the basic question of time dimension. The effective

implementation of PPC concepts requires that the management of ES establish a definite time dimension for certain types of decision. And timing of planning activities suggests that there should be a definite management time schedule established for initiating and completing certain phases of the planning process.” (Goet, Bhattarai & Gautam 2063; 1.5)

### **Flexible Application**

This stress that a PPC programmed must not dominate the business and that flexibility in applying the plan must be forthright management policy. So that strait jackets are not imposed and all favorable opportunities are seized even through “They are not covered by the budget. Rigidity in practicability will be the harmful boundary in an association in an occasion for the enterprises. So, such boundary should be avoided which mean there should be flexibility in PPC so that the unseen golden opportunity should be grasped in future for the betterment of that organization.” (Goet, Bhattarai & Gautam 2063; 1.5)

### **Zero Base Budgeting: -**

Zero Base Budgeting is a method of budgeting in which managers are required to start from zero level every year and to justify all costs as if the programs involved were being initiated for the first time. Under zero-base budgeting, every budget is constructed on the premise that every activity in the budget must be justified. It starts with the basic premise that the budget for next year is zero and that every expenditure, old and new, must be justified on the basis of its cost and benefit.

### **Activity Costing: -**

“Responsibility accounting system generally accumulates costs by department and product costing systems associate costs with units of product or service organization also frequently finds it useful to associate costs with activities. By decomposing an organizations production process into discrete set of activities, and then associating costs with each of those activities. Moreover, by systematically identifying the activities through out the organizations managers can identify redundant activities.”(Welsch, 2005; 42)

### **Individual and Group Recognition: -**

Behavioral aspects of human being are of the field of study of the psychologist, educators and businessman, and finding was that there could be so many unknown misconception and speculations, which has to be considered for an efficient management. A good and dynamic

leadership can resolve this problem by integrating all the group efforts for betterment of the organization.

### **Management control Using PPC**

The primary purpose of control is to ensure attainment of the objective, goals and standards of the enterprises. Control has many facets such as direct observation, oral express, policies and procedures, reports of actual results and performance reports. “PPC focuses on performance reporting and evaluation of performance to determine the causes of both high and low performance. The essential characteristics of a PPC performance reports are as follows.” (Welsch-2005; 40)

- 1 Performance is classified by assigned responsibilities
- 2 Controllable and non controllable items are designated
- 3 Timely reports are issued.

Emphasis is given to a comparison of actual results and planned results should be designated the responsible manager and show actual results.

### **Behavioral viewpoint**

An ounce of behavior is better than a quintal of the theorem so ever be the theory and theorem, the organization only when it improves its behavior, is best or in another way Welsch has suggested that the motivation of human resources through dynamic leadership central to effective management. “It is found by many psychologist and educators and businessmen that, there are many known and unknown, misconception and speculations concerning the responses of the individual and the group in the varying situation so the PPC programs bring many of these behavior problems in the sharp and focus and trying to resolve.”(Welsch, 2005; 53)

### **Management by Exception**

A comprehensive profit planning and control program facilities in many ways, underlying these is the measurement of actual performance against planned objectives goals, and standards and the reporting if that measurement in performance reports. This measurement and reporting extends to all areas of operations and to all responsibility centers in the enterprises. It involves reporting

- a) Actual result

- b) Budgeted or planned results and
- c) The differences between the two

This type of reporting represents an effective application of the well- recognized management exception principle. “The exception principle holds that the manager should concentrate primarily on the exceptional or unusual items that appear in daily, weekly and monthly reports, thereby leaving sufficient managerial time for overall policy and planning considerations. It is the ‘out of line’ items that need immediate managerial attention to determine causes and to take corrective action. The items that are not out of line need not utilize extensive management time, however; they should trigger “rewards” in appropriate ways. To implement the exception principle, techniques, Procedures must be adopted to call the manager attention to the ‘out of control’ items. Performance reports because they include a comparison of actual results with plans by areas of responsibility, emphasize in a relevant ways performance variation. The out of line items stand out. It is with respect to these items that the busy executive should investigate, determine the causes and take corrective action.” (Welsh-2005; 45)

## **Follow Up**

This fundamentals holds that both good and substandard performance should be carefully investigated the purpose being three fold.

- 1 In the case of substandard performance, to lead in a constructive manner to immediate corrective action.
- 2 In the case of outstanding performance, to recognize it and perhaps provide for a transfer of knowledge to similar operation and
- 3 To provide a basis for better planning and control in the future.

### **2.5.1 Profit Planning and Control Process: -**

Profit planning and control process is necessarily integrates the planning, leading and control function of management. A PPC program includes more than the traditional idea of a periodic or master budget. Rather, it encompasses the application of a number of related management concepts through a variety of approaches, techniques and sequential steps. These steps are outlined in this study in the following manner.

#### **2.5.1.1 Identification and Evaluation of External Variables**

It is discussed the distinction between external and internal variables for an enterprises. These

variables exert major influences on an enterprise. The variable identification phase of the PPC process focuses on a) identifying and b) evaluating the effects of the external variables. Management planning must focus on how to manipulate the controllable variables. Variables, which have a direct and significant impact on the enterprises, are called relevant variables. Variables may have their different relevancy according to the market nature. “For the enterprises purpose the external relevant variables are population, G.N.P. competitive activities product line, and industry sales. And so far internal variables are concerned employees, capital, research productivity, pricing operating costs, advertisements etc. a particularly significant phase of this analysis includes an evaluation of the present strength and weakness of the enterprises the comprehensive PPC approach is based on the expectation that these significant aspects of operations will be critically analyzed and evaluated periodically and in an orderly manner.” (Welsh-2005; 74)

### **2.5.1.2 Development of the Broad Objectives of the Enterprises**

Development of the broad objectives of the enterprises is a responsibility of executive management. Based on a realistic evaluation of the relevant variables and an assessment of the strength and weakness of the organization, executive management, can specify or restate this phase of the PPC process.

“The statement of broad objectives should express the mission, vision and ethical character of the enterprise. Its purpose is to provide enterprise identify continuity of purpose is to provide and definition. One research study listed the purpose of the statement essentially as follows.

1. To define of the purpose of the co.
2. To clarify the philosophy character of the Co.
3. To create particular climate with in the business.
4. To set down a guide for managers so that the decisions they make will reflect the best interest of the business with fairness and justice to those concerned.”(Welsh, 2005; 75)

### **2.5.1.3 Development of Specific Goals for the Enterprises**

This component of a comprehensive PPC process is to bring the statement of broad objectives into sharper focus and to move from the realm of general information to more specific planning information. It provides both narrative and quantitative goals that are definite and measurable. These are specific goals that relate to the enterprises as a whole and to the major

responsibility centers.

“Executive management as the second component of the substantive plan for the upcoming budget year should develop these goals. Executive management should exercise leadership in this planning phase so that there will be a realistic and clearly articulated framework with in which operations will be conducted toward common goals.”(Welsh, 2005; 77)

#### **2.5.1.4 Development and Evaluation of Company Strategy**

Company strategies are the basic thrusts ways and tactics that will be used to attain planned objectives and goals. “A particular strategy may be short-term or long-term. Here are some actual examples of basic strategies:

- 1 Increase long-term market penetration by using technology to develop new products and innovation the product.
- 2 Emphasize product quality and price for the top market.
- 3 Expand market the company will not enter foreign markets in the foreseeable future.
- 4 Market with low price to expand value.
- 5 Use both institutional and local advertisement program to build market share.
- 6 Improve employee morale and productivity by initiating behavior management program.

Among probable alternatives, the best should be chosen which would tackle to the objectives and goals of the organization. Strategies focus and ‘how’ so that they outline a plan of action for the enterprises.” (Welsh, 2005; 78)

#### **2.5.1.5 Executive Management Planning Instruction**

This phase involves communication of the substantive, plan to middle and lower management levels. It explains the broad objective, enterprise goals enterprise strategies, and any other executive management instruction, needed to develop the strategic and tactical profit plans. It also is called the statement of planning premises or the statement planning guidelines. Executive management explicitly establishes a planning foundation that is a condition precedent to the movement in the planning process. “On the basis of this planning foundation the statement of planning guidelines is set as executive management instructions and is disseminated in order to initiate a sophisticated and potent move from broad corporate planning to the development of profit plans by each major responsibility center in the enterprises. It is simply a communication steps from executive management to the lower

levels of management and it should adopt the fundamentals of full communication.” (Welsh, 2005; 79)

### **2.5.1.6 Preparation and Evaluation of Project Plans**

Project plans encompass variable time horizons because each project has a unique time dimension. Project plans encompass such items as plans for improvement of present products, new and expanded physical facilities, entrance into new industries, exit from products and industries, new technology, and other major activities that can be separately identified for planning purposes. The nature of projects is such that they must be planned as separate units.

“Consistent with this approach during the formal planning cycle, Management must periodically evaluate and decide upon the plan status of each project in process and select any new projects to be initiated during the time dimension covered by the upcoming strategies and tactical profit plans.” (Welsh, 2005; 79)

### **2.5.1.7 Development of strategies and tactical profit plan**

When the managers of the various responsibility centers in the enterprises receive the executive management planning instruction and the projects plans, they can begin intensive activities to develop their respective strategic or tactical profit plans. The strategic and tactical profit plans are usually developed concurrently. Certain format and procedural instructions should be provided by a centralized source, normally the financial functions, to establish the general format, amount of detail and other relevant procedural and format requirements essential for aggregation of the plans of the responsibility centers, into the overall profit plans. All of this activity must be coordinated among the centers in conformity with the organization structure.

“When the two plans for the overall enterprises are completed, executive management should subject the entire planning package to a careful analysis and evaluation to determine whether overall plans are the most realistic set that can be developed under the circumstances. When this point is reached the two profit plans should be formally approved by the top executive and distributed to the appropriate managers.” (Welsh, 2005; 80)

### **2.5.1.8 Implementation of profit plan**

Implementation of management plans that have been developed and approved in the planning process involves the management function of leading subordinates in attaining enterprises

objectives and goals. Thus effective management at all levels requires that enterprises objectives, goals, strategies, and policy to be communicated and understood by subordinates. “There are many facets involved in management leadership. However the comprehensive PPC program may aid substantially in performing this function, plan, strategies and policies foundation for effective communication. The plan should have been developed with the managerial conviction that they are going to be met or exceeded in all major respects. If these principles are effective in the development process, the various effective and supervisor will have a velar understanding of their responsibilities and the expected level of performance.” (Welsh, 2005; 80)

### **2.5.1.9 Use of periodical Performance reports**

“The accounting department on a monthly basis prepares performance reports. Also some special performance reports are prepared more often on an “as needed” basis. The performance reports a) compare actual performance with planned performance and b) show each difference as a favorable or unfavorable performance variation.” (Welsh, 2005; 85)

### **2.5.1.10 Follow up**

Follow up is an important part of effective control because performance reports are based on assigned responsibilities; they are the basis for effective follow up actions. “It is important to distinguish between cause and effect. The performance variations are effects, the management must determine the under lying causes. The identification of causes is primarily as responsibility of line management.” (Welsh, 2004; 88)

Finally, there should be a special follow up of the prior follow up actions. This step should be designed to

- 1 Determine the effectiveness of prior corrective actions and
- 2 Provide a basis for improving future planning and control procedures.

## **2.6 Advantages and disadvantages of PPC**

The usefulness of comprehensive PPC may offer more benefits, which may be summarized as below.

1. It forces early consideration of basic policies.
2. It requires adequate and sound organization structure; that is there must be a definite assignment of responsibility for each function of the enterprise.
3. It compels all members of management, from the top down, to participate in the establishment of goals and plans.

4. It compels departmental managers to make plans in harmony with the plan of other departments and of the entire enterprise.
5. It requires that management put down in figures what is necessary for satisfactory performance.
6. It requires adequate and appropriate historical accounting data.
7. It compels management to plan for the most economical use of labor material and capital.
8. It instills at all levels of management the habit of timely, careful and adequate consideration of the relevant factors before reaching important decision.
9. It reduces cost by increasing the span of control because fewer supervisors are needed.
10. It frees executives from many day-to-day internal problems through predetermined policies and clear- cut authority relationships. It thereby provides more executive time for planning and creative thinking.
11. It tends to remove the cloud of uncertainty that exists in many organizations, especially among, lower levels of management, relative to basic policies and enterprise objectives.
12. It pinpoints efficiency and in efficiency.
13. It promotes understanding among members of management of their co-workers problems.
14. It forces management to give adequate attention to the effect of general business condition.
15. It forces a periodic self-analysis of a company.
16. It aids in obtaining bank credit, banks commonly requires a projection of future operation and cash flows to support large loans.
17. It checks progress or lack of progress towards the objectives of enterprises.
18. It forces reorganization and corrective action (including rewards)
19. It rewards high performance and seek to correct unfavorable performance.
20. It forces management to consider expected future trends and condition.

(Shresth, Lalitman; 2007; 35 'Thesis')

PPC model should not be assumed that the concept is full proof or that it is free of problem. The following main arguments are usually given against PPC

1. It is difficult, if not impossible, to estimate revenues and expenses on our company realistically.

2. Our management has no interest in all the estimate and schedules. Our strictly informal system is better and works well.
3. It is not realistic to out and distribute our goals policies and guidelines to all the supervisors
4. Budgeting places to great a demands
5. It takes awat management flexibility
6. It creates all kinds of behavioral problems.
7. It places the management in a straitjacket.
8. It adds a level of complexity that is not needed.
9. It is too costly asides from management time.
10. The managers, supervisors and other employees hate budgets.

Whatever exists in the world has both advantages and disadvantages; and it is clear that we use or apply it only in that case if it has many advantages. A PPC model also has more advantages than disadvantages. Thus, now a days PPC system (model) is especially familiar to organizations and widely used in this world of management.

## **2.7 Basic Assumption and Limitations Profit Plan**

Profit planning system is more common in large companies, to serve the management. Still, the usefulness of budgeting to very small business could have been circumvented by an early attempt to qualify the dreams of headstrong. But, there are so many assumptions of using profit-planning program.

The basic assumptions prior to the start of the profit planning system are:

- 1 Profit plans are based on estimates and reality hardly coincides to the estimate. Therefore a profit planning and control program must be continually adapted to fit changing circumstances.
- 2 Profit plans are just plans and the execution of a profit plan will not occur automatically. It requires smart and sincere human effort.
3. Profit planning should not limit the manager's thinking.

However, each tool suffers some limitation and its use is fruitful within these limits. Profit planning and control is also not a limitless tool; so it is essential that the user of profit planning and control must be having a full knowledge of its limitations. The limitations of profit planning are as under:

- 1 Based on estimates: profit planning is not an exact science. Its sources depend upon precision of estimates.
- 2 Danger of Rigidity: profit planning is not an estimation and quantitative expression of all relevant data. So, there can be the tendency to attach some sort of rigidity or finality to them:
- 3 Application for long period
- 4 Execution is not automatic
- 5 Not a substitute for management
- 6 Costly affairs
- 7 Proper evaluation
- 8 Lower morale and productivity

“The profit plan should be regarded not as a master but as a servant. It is one of the best tools yet devised for advancing the affairs of a company and the individuals in their various spheres of managerial activity. It is not assumed that any profit plan is perfect. The most important consideration is to make sure, by intelligent use of profit plans that all possible attainable benefits are derived from the plans as rendered and to re-plan when there are compelling business reasons.” (Goet, Bhattarai & Gautam, 2063; 1.6)

### **2.7.1 Development of Profit Plan**

Development of profit plan in commercial Bank begins with the preparation of various functional budgets. Those functional budgets are in fact the picture of various activities of the Bank to be performed during a particular period of time. Therefore the functional budgets of a Bank are activity based such as budget for deposit collection, budget for lending and investments, budget for non-fund based business, budgets for expenditures and revenues. The development of profit plans process that involves managerial decisions and ideally a high level of management participation. The following are the budgets, which are developed in a bank while making a profit plan.

### **2.7.2 Resources Mobilization Plan or Budget**

The planning for resources mobilization is the foundation for planning in a bank. The all other planning is based on it. The major and the sustainable resource of a Bank is the customer deposit. Therefore, the plan for resources mobilization has a primary focus on the

customer deposit mobilization. The lending and investment activities are depended on the deposit mobilized by the Bank. So the deposit mobilization or collection plan is the starting point in preparing the other different plan.

Deposit mobilization is the primary function of banks, which has major contribution in the total resources of the bank. In terms of the cost for the bank, customer's deposits are of two kinds, viz. (a) Interest free deposits i.e. current deposits, margin deposits etc. and (b) interest bearing deposits i.e. saving deposits, fixed deposits of various tenure are called deposits. The interest free deposits are cost free but are generally volatile in nature. Those can be withdrawn without restriction from the bank, thus cannot be invested into higher income yielding assets.

Further, interest –bearing deposits involve cost of deposit but their retention ratio with the bank are much better so they can be put to high income yielding assets having longer tenure.

Therefore a proper mix of cost free and costly deposits corresponding to short term and longer term deposits are to be maintained by the bank in its deposit mix in order to minimize its average cost of deposit at the same time having comfortable mix of income yield assets.

The cost of deposit of banks is also affected by the prevailing deposit interest rate of other banks in the market.

Budgeted targets for deposit mobilization during a particular year is set in advance with the view of optimizing the cost of deposit and the same are allocated to the different branches of the banks. Such allocation may be regarded as the tactical plan for deposit mobilization the banks.

Banks resources other than customer deposits are the borrowing from other banks and the capital fund. Generally banks borrows from other banks to meet temporary requirement of liquidity which may occur sometimes during the course of banking operation caused due to unexpected withdrawals of deposit or deferment in loan repayment by the borrower by some reason or other. Such activities are managed from the Head Office with the least possible cost.

Among the capital fund, the equity capital is formed generally one time during opening of the bank. The central bank (NRB) may from time instruct the bank to enhance the paid up capital to improve the capital adequacy of the bank. General Reserve, the other item of capital fund, has to be raised every year by at least 20% of the net profit earned by the bank until the amount gets double the paid up capital. This is the mandatory provision made by Commercial Banking Act 2031.

Further, the bankers may choose by themselves whether or not to increase the owner's capital

by raising the other item included in capital funds besides paid up capital by raising the other item included in capital funds besides paid up capital and general reserves. It is always better to have a higher capital fund base of a bank because, creation of bank's assets, and the size of lending to any particular borrower are tied up with the capital adequacy requirement by the central Bank. As per NRB directives, banks shall have to build their capital base at least of 12% by the end of F/Y 20662/063. And a bank can take the size of exposure per borrower equivalent to maximum of 25% of its core capital in fund based, and 50% of that in non-fund based exposure. (NRB Directives, 2005)

### **2.7.3 Resources Deployment Plan or Budget**

The planning for deployment of resources starts from assessment of nature of resources to be mobilized. That is the assets are allocated on the basis of the nature of resources. This approach of deployment of resources is called asset allocation approach. As M.C. Vaish writes in his book 'money Banking Trade and Public Finance', "The fundamental criterion which must be followed in allocating funds for acquiring different types of assets is that the velocity turnover rate of different sources of supply of fund determines the appropriate maturity of the assets acquired through fund utilization, for instance while relatively stable fund, like saving deposits, fixed deposits and paid up capital could be used to buy long dated high yielding securities, demand deposit which are more volatile, could be used to acquire relatively liquid asset like cash or money at call and short notice on which little or no return is made by the bank." (Vaish, 1996; 304)

Therefore the budgeted deposit mix is the major determining factor of the planning of assets portfolio.

A Bank should make the planning for deployment of its resources in such a way that it ensures required liquidity as well optimize the yield on the fund of bank. Therefore banks resources deployment process involves following:

- 1 Deployment in liquid assets
- 2 Deployment in lower income yielding assets
- 3 Deployment in higher income yielding assets.

Funds kept as cash in vault and as balance with NRB and other banks in current account are the most liquid assets of the bank. Normally banks have to maintain certain fixed percentage of their deposit liability in this form as directed by the Central Bank from time to time. There is no yield in the fund deployed as liquid assets.

Deployment for lower income yield assets are generally placing the funds in short term securities, treasury bills etc. which provides reasonable liquidity to the bank as well as yield some return although they are at very low rate.

Major portion the income of the Bank comes as interest income from the resources deployed to loans advances and Bill discounting (LDO). As the most part of the resources are for LDO, Banks make its lending budgets in advance as per their lending policies. Lending targets are fixed at various sector of economy for various kinds of trades and commercial activities and to various borrowers ensuring well diversification of the assets. The targets allocated to the branches, which are generally operated as separate profit centers.

## **2.8 Planning for non funded Business Activities**

The other activities of commercial banks where it does not have to involve its fund yet it can generate other income are called non-funded business activities of the Bank. They are usually letter of credit and Bank guarantee issuance business of the bank where the bank undertakes payment liabilities, which are contingent in nature and the banks charges certain percentage of commission on such transaction to their client who are availing these facilities from the bank.

The bank fixes annual target for such business and those are allocated to the branches of the bank.

### **2.8.1 Expenditure Planning**

The expenses planning and controlling are very necessary for supporting the objectives and planned programs of the firm. An expense is related with profit. It is real fact, that the minimization of cost is maximization profit. So the expenses must be planned carefully for developing a profit plan. In a Bank there are generally following types of expenses:

- a. Interest Expenses
- b. Personnel Expenses
- c. Office Operating Expenses
- d. Expenses Meeting the loss in Exchange fluctuation
- e. Non operative expenses
- f. Expenses for provision for loan loss
- g. Expenses for provision for staff bonus

#### h. Expenses for provision of income tax

The interest expenses are incurred while paying for the deposit mobilized by the bank and include the expenses incurred for interest payment in all kinds of interest bearing deposit as per the agreed rate between the bank and the borrower. In the total expenses of a bank, the portion of interest expense is quite higher. Therefore, the expenses are categorized into interest expenses and other expenses while the later includes other expenses as mention above except the interest expense.

Interest expenses in a bank depend on the average cost of deposit (COD) mobilized by the bank. Lower the COD lower the interest expenses and thus higher the profitability. Therefore from profitability point of view banks plan their COD at lowest possible level. The nature of interest expense is that of a variable expense. The net earning from interest income of a bank deducting the interest expense for the deposit mobilized is called 'Spread' which is similar to the 'Contribution Margin' in sales of commodities by a manufacturing units.

Other expenses are the administrative expenses those are generally incurred by the bank during the course of its operation. Higher the volume of business transaction of a bank, higher will be the amount of its other expenses. Therefore, the expenses should be related with the business activities, which ultimately should yield in income for the bank. Such other expenses form burden to the profitability as it consume the spread earned. Therefore budgets are prepared with an aim of reducing the burden as far as possible. The expenses budgets are formulated in co relation with the activities of the bank and the targets are allocated to different branches.

### **2.8.2 Revenue Plan**

Revenue of a bank is generated from the income yielding activities of the bank. Therefore while preparing the resources deployment plan and non-funded business activities plan. The banks make the estimation of the revenue in advance during the period for which the plan is developed.

Revenues of a bank are generated in the following forms:

- 1 Interest Income
- 2 Commissions and Discounts
- 3 Dividend
- 4 Other Income
- 5 Foreign Exchange Income

## 6 Non operating Income

Generally the interest income of a commercial bank holds a major portion in total revenues of the bank and it provides the major source of earning of a bank. Therefore total income of a bank is categorized in two type viz. interest income and other income, while the later including other income items as listed above accepting the interest income.

The interest income is earned by charging interest on the fund deployed in interest earning assets such as loan and advances, overdrafts, investments in government securities, debentures etc. for this study, the income from Bills discounting has also been treated as interest income, as we consider Loans overdraft and Bill Discounting together as a single asset portfolio as LDO.

As the average rate of interest on LDO are comparatively higher than any other kind of income yielding assets, from the profitability point of view, higher asset allocation into LDO, higher will be the income.

The other income are generated from other activities of the bank such as issuance of L/C, Bank Guarantees, from remittance charges, cheque collection fee, locker charges, service charges, commitment charges, trading gain on foreign exchange, revaluation gain on foreign exchange reserves etc. the amount of other income earned by the bank, lower will be the net burden amount and thus better will be the profitability of the bank.

Income of a bank is essentially activity based i.e. the volume of business. Higher the income generating activities of a bank, higher will be the amount of its revenue. Therefore the bank develops its plans for various activities in such a way that it optimizes its revenue.

## 2.9 Implementation of the profit plan

### 2.9.1 Completion of the Annual Profit Plan

The development of an annual profit plan ends with the planned income statement, the planned balance sheet, and the planned statement of cash flows. These three statements summarize and integrate the detailed plans developed by management for the planning period. They also report the primary impact of detailed plans on the financial characteristics of the firm. In profit planning, the budget director has an important responsibility for designing and improving the overall system. "Other essential sub budgets are the following.

- 1 Planned statement of cost of goods manufactured.
- 2 Planned statement of cost of goods sold.
- 3 Planned income statement.

4 Planned statement of cash flows.

5 Planned balance sheet.

The profit plan completion date is important. Issuances of a profit plan after the beginning of the budget period is one sure way of destroying much of the budget potential.” (Welsch, 2005; 466)

### **2.9.2 Implementing the profit plan**

Profit plan should represent potentially attainable goals, yet the goals should present a challenge to the enterprise. The plan should be developed with the conviction that the enterprise is going to meet or exceed all major objectives. Participation enhances communication (both down ward and upward). If this principle is to be effective, the various executives should have a clear understanding of their implementation responsibilities.

The final test of whether the efforts and cost in developing a profit plan are worthwhile is its usefulness to management. The plan should be developed with the conviction that the enterprises are going to meet or exceed al major objectives; participation enhances communication. If this principle is to be effective, the various executives and supervisors should have a clear understanding of their responsibilities. The copies of the complete profit plan be prepared and distributed to the member of executive management. The guiding principle in establishing the distributed policy might be to provide one copy to each member of the management team according to his/her overall responsibilities, while taking in to account the problem of security. After distribution of the profit plan a series of profit plan conferences should be held. The top executives discuss comprehensively the plans expectations and steps in implementation. At this top level meeting the importance of action, flexibility and continuous control may well be emphasized. In essence, each manager has to realize that the budget is a tool for his or her use. Conferences should be held so as to convey the profit plan to each level of management.

The manager of each responsibility center obtains an approved profit plan for his center and it becomes the basis for current operations and excerpts considerable coordinating and controlling effects.

Performance must be measured and reported to management. Execution of the plan is assured through control procedure must be established so that accomplishment, or failure is immediately known. On this basis action can be taken to correct or minimize and undesirable effects. Short term performance reporting is essential.

“A budget programs viewed and administrated in a sophisticated way does hamper or restrict

management, instead, it provide definite goals around which day today and mouth to mouth decisions are made. Flexibility in the use and application of both the profit plan and variable budgets also should be considered in detail. Flexibility in budget application is essential and it increases the probabilities of achieving or bettering the objectives.” (Welsch- 2005; 472)

### **2.9.3 Performance Reports**

Performance reporting is an important part of a comprehensive PPC system. Its phase of a comprehensive PPC program significantly influences the extent to which the organization’s planned goals and objectives are attained. Performance reports deal with control aspect of PPC. The control function of management defined as The action necessary to assure the objectives, plans, policies and standards are being attend. Performance reports are one of the vital tools of management to exercise its controls function effectively.

Special external reports, reports to owner & internal reports are specially presented in the organization. Performance reports include in internal reports groups. It is usually prepared on a monthly basis and follows a standardized format. Such reports are designed to facilitate internal control by management. Fundamentally actual result of reports is compared with goals & budget plans. Frequently they identify problems that require special attention since these reports are prepared to pinpoint both efficient & inefficient performance.

#### **1 Features of performance reports**

In comprehensive PPC, performance report is very important. The main objective of performance reports is the communication of performance measurement, actual results and the related variances. Performance reports offer management essential insights in to all the facts of operational efficiencies. Performance reports should be:

1. Tailored to the organizational structure and focus of controllability (that is by responsibility centers).
1. Designed to implement the management by exception principle.
2. Repetitive to implement the management by exception principle.
3. Adapted to the requirement of the primary users.
4. Simple understandable & reports only essential information.
5. Accurate and designed to pinpoint significant distinctions.
6. Prepared and presently promptly.
7. Constructive in tone.

## )] Aspects of Performance Reports

To extent to which the various managers use their performance reports depends on many factors, some behavioral and some technical. One important factor is the extent to which the performance reports serves the management and decisions making needs of the users. Top management needs reports that give a complete and readily comprehensive summary of the overall aspects of operations and identification of major events. Middle management needs summary data as well as detailed data on day-to-day operation. Similarly lower level management needs reports that must be detailed, simple understandable & limited to items having a direct bearing on the supervisor's operational responsibilities.

In the design and preparation of performance reports careful attention must be given that titles and headings should be descriptive; column heading & side caption should clearly identify the data, & the technical jargon should be avoided. Reports should not be too long & complex; tabulations should be avoided. Performance reports should be standardized to a reasonable degree and if should be relevant.

Performance reports should be available on a timely basis. To attain a realistic balance between immediate reporting & the costs of detailed reporting, monthly performance reports are widely used in the organization.

### 2.10 Review of Previous Studied Work

The profit planning in the context of particularly commercial Banks seems to be a new subject of study for research and analysis. So for this researcher could find three study that has been made in this topics, Binod Kumar Sharma (April 2002), Uday Kishor Tiwari (December, 2003) & Lalit Man Shresth (June, 2006) for the purpose of partial fulfillment of the requirement for Master Degree in Business Studies. They are studies the profit planning of commercial bank with a case of, Nepal Bangladesh Bank, Standard Chartered Bank Nepal Limited and Bank Of Kathmandu & Nepal Bangladesh Bank Limited respectively.

**Mr. Sharma B.K,** (2002) submitted the thesis on the topic "*Profit Planning in Commercial Bank*" (A case study of Nepal Bangladesh Bank ltd.)

#### **Objective:**

The basic objective of this study is to appraise Nepal Bangladesh Bank, appropriately for application of comprehensive PPC system. Thus the major objectives are:

- i) To analyse the current profit planning premises adopted of the banks.
- ii) To observe NB Bank's profit planning on the basis of overall managerial Budgets

developed by the Bank.

iii) To analyze the variance of budgeted and actual achievement.

iv) To study the growth of the business of the Bank over the period.

v) To provide suggestion and recommendations for improvements of the overall profitability of the bank.

**The major findings of the study were:**

1. It is observed that the Bank is adopting a police to keep minimum number of employee as possible. But it has unnecessary long ladder at various levels with out specific job description.
2. NB Bank is currently operating with its 15 branch offices making its presence at almost all of the cities of the country. It is one of the banks, having highest branch network among the joint venture private Bank in Nepal.
3. Objectives of the Bank are expressed in literacy form, and not specified clearly; therefore there is a danger of it being misinterpreted in the ways of one's benefit by the concerned.
4. Major concentration of resources mobilization of NB Bank is at deposit mobilization. In this respect they are incurring higher cast toward deposit mobilizations.
5. Bank's resources development for non yielding liquid assets (cash and Bank Balance is increasing every year, which is detriment's to profitability objectives, but it is supportive to meeting liquidity requirements of the Bank.
6. The interest expense of the bank is found increasing each year corresponding to the increasing in deposit. The interest expenses are perfectly and positively correlated with deposit.
7. Outstanding letter of credit liability of the Bank is increasing every year however the growth is not consistent.
8. The amount of interest income is increasing every year corresponding to increase in LDO. There is a perfect and positive correlation between interest income and LDO.

**Mr.Tiwari** U.K,(2003) submitted the thesis on the topic "*A Profit Planning in Commercial Bank*" (A case study of standard chartered Bank Nepal ltd.)

**Objectives:**

The basic objective of this study is appraising Standard Chartered. Bank Nepal Ltd.

Appropriately for the application of comprehensive PPC system. Thus the major objectives are:

- i) To analyse the current profit planning premises adopted by the banks.
- ii) To analyze the variance of budgeted and actual achievements.
- iii) To study the growth of the Bank over the period.
- iv) To provide suggestion and recommendations for improvements of the overall profitability of the bank.

**The major findings of the study were:**

1. Bank management policy is very strong. It keep minimum number of employees and highly qualified for maintain the job.
2. The Bank operated with only 9 branches in Nepal.
3. Customer deposits collection is the main resources mobilization of the bank.
4. Loan allowance and bill purchasing hold the highest outlet of resources deployment.
5. Bank's actual deposit is more variable than actual outstanding LABP. Hence the coefficient of variation of actual deposit is higher than actual outstanding liability LABP.
6. The analysis of BEP shows that the bank figure is an earning trend will be encouraging if it can increase its revenue and decrease in burden.

**Shrestha L.M,** (2007) submitted the project work on the topic “*A Study of Profit Planning of Commercial Banks in Nepal*” (Comparative Study of Nepal Bangladesh Bank Ltd. and Bank of Katmandu Ltd.)

**Objective:**

In general, the objective of the study is to find out the application of profit planning in the commercial banks. The following objectives are developed for the studying the application of profit planning in the commercial banks.

- i) To analyse the system of profit planning and practices of the N.B bank and BOKL Ltd.
- ii) To observe the bank's profit planning on the basis of overall managerial budgets developed.
- iii) To examine the effectiveness of profit planning in the N.B bank and BOKL.
- iv) To examine the effectiveness of profit planning in the N.B bank and BOK Ltd.
- v) To provide suggestions and recommendations for improvements of the overall

profitability of the bank.

- vi) To check on the superiority between NB Bank and BOKL from the aspect of profit planning aspect.

**The major findings of the study were:**

- 1 Considering the overall analysis on profit planning in commercial banks, they are having high deposit mobilization. Deposits mobilized by the banks are found to be considerably growing every year in both the NBBL and BOK. Comparatively high growth rate can be seen in the MBBL and BOK.
- 2 Resources other than customer deposits (RMOD) of the banks are found considerably increasing in both the bank. Comparatively more increasing trend is in the BOK and HBL.
- 3 Bank's resources deployment for non-yielding liquid assets (cash and bank balance) is increasing every year but comparatively the BOK has been decreasing position than NBBL.
- 4 In the NBBL, LDO has found increasing trend over the year where in the BOKL has increasing trend.
- 5 The NLKO of both banks are in increasing rate over the study period.
- 6 Interest expenses ratio is the highest in the total expenses items of the banks, the interest expenses of the banks are found increasing each year corresponding to the increase in deposit on the both the banks. The cost of deposit (calculated as the ratio of total interest expenses during a year on the deposit as of the year and expressed in percent term) of both the banks is decreasing each year.
- 7 Interest income of the bank is the highest among other income items in the total revenue. The amount of interest income is increasing every year corresponding to increase in LDO in both the banks. The average yield on LDO of NBL is 12.38 percent and similarly yield on LDO of BOK is 11.53 percent.
- 8 Other income of the banks is in increasing trend in both the banks.
- 9 The interest spread or the amount of interest margin is found to be increasing every year in both the banks. The increasing trend of NBL is high volume than BOKL.
- 10 Net Burden of the banks is increasing every year, but as the average rate of growth of other income higher than that of other expenses in both the banks. It can be expected that it would not hamper much to the profitability if the same trend were continued.
- 11 Both the banks have net profit over the study period and increasing trend up to the FY

2002 but decreasing trend in the rest FY 2002 and 2004. As the rate of growth of burden result low not profit. The rate of growth of spread is higher than that of burden; the profitability of the banks is increasing.

- 12 The average current ratio of the NBL has found to be higher than standard ratio 2:1 except in the FY 2005, which shows satisfactory liquidity position and the average ratio of BOKS has found to be lower than standard which shows the solvency position of BOKL has found to be lower than standard which shows the solvency position of BOKL is no better than NBL.
- 13 Generally the equity ratios of the banks are higher because they mobilize fixed deposit much more. The average debt to equity ratio of NBBL is higher than BOKL.
- 14 The average interest coverage ratio of NBBL is 1.25 and BOKL is 1.22 times during the study period.
- 15 From the profitability ratio, it is found that, the return on assets of NBBL is more than BOKL. The average return on assets of NBBL is 1.36 and BOKL is 1.064.
- 16 Return on deposit is also more of NBBL than BOKL. The average return on deposit of NBBL is 1.57 whereas, the BOKL is 1.21.
- 17 The average return on equity of than NBBL is higher than BOKL. It seems the return on equity of NBBL is better than BOKL. The average return on equity of NBBL is 24.58 AND BOKL IS 21.39.

## **2.11 Research Gap**

The purpose of this research is to develop some expertise in one's area, to see what new contribution can be made and to receive some ideas, knowledge and suggestions in relation to profit planning of Himalayan Bank Limited and Bank of Kathmandu Limited. Thus, the previous studies can't be ignored because they provide the foundation to 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 studies. Here, it is clear that the new research cannot be found on the exact topic, i.e. profit planning "A comparative study of Himalayan Bank Limited and Bank of Kathmandu Limited". Therefore, to fulfill this gap, this research is selected. To complete this research work: many books, journals, articles and various published and unpublished dissertations are followed as guideline to make the research easier and smooth.

Previous researchers could not cover all the aspects of profit planning in Nepalese context. They analyzed the profit planning by using secondary source formation in terms of profit practices. But actually, profit planning covers many other areas such as total deposit collection, total lending, NPL level, loan loss provision and relationship between them which are very much important for profit appraisal. Present study tries to define profit planning by applying those facts. Therefore, this study is useful to the concerned banks as well as different persons: such as shareholders, investors, policy makers, stockbrokers, investors, policy makers, stockbrokers, state of government etc. Thus present study may be valuable piece of research work.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Research design:**

A research design is purely and simply the framework or plan for a study that guides the collection and analysis of data, as per Kerlinger. This study is an examination and evaluation of process in profit planning programs of BOK and HBL. Various functional budgets and other related accounting information's and statement of the bank are the materials to analyze and evaluate the profit planning system of the Bank. Descriptive as well as analytical research designs have been adopted in this research. This is a comparative study research of commercial Banks.

#### **3.2 Data Collection Procedures and Sources of Data:**

This study is mostly based on secondary data. However, primary data and information have been obtained through informal discussions with the executives and other staff of the Bank. But this study is mainly based on secondary data. The main sources of data are quarterly and annual financial reports, official records, website brochures, prospectus, and other relevant publication of HBL, BOK Banks, central bureau of statistics and relevant publications. From this sources the relevant historical data are gathered for analysis purpose.

#### **3.3 Population and Sample:**

As this study aims to analyze the profit planning aspect of the commercial bank taking the reference of HBL and BOK and data have been analyze for several years of its operation. Here, all the commercial banks are population of the study and HBL and BOK have been selected as sample for the present study.

#### **3.4 Research variables:**

Loan / advance overdrafts and Bills Discounted (LDO), customer deposits, total resources, total deployment, outstanding balance of Letter of Credit and Bank Guarantees, Interest Expenses, Interest Income, Other income etc. Bank of Kathmandu and Himalayan bank Ltd. are the research variable for this study.

## **Time Period of Profit Plan**

As per NRB, directives all the commercial banks have identically to follow the accounting year of twelve months. It starts from first shrawan to end of Asadh. Which covers the last nine months of years (B.S) to the first three month's of succeeding years (B.S) HBL and BOK prepares the profit plan for twelve months of upcoming year, which includes the business budget, expenditure and profit plan for the year.

This study covers seven years period from fiscal year 2005/006 to 2011/012 for its analysis. For the case of specific year's study the data of fiscal year 2011/012 are have to analyze.

### **3.5 Data Analysis Tools:**

This study is confined to examine the profit planning of Bank of Kathmandu and Himalayan Bank. Therefore, the data have been collected accordingly and managed, analyzed and presented in suitable tables, formats, diagrams, graphs and charts. Such presentation have been interpreted and explained wherever necessary. Financial, Accounting, Mathematical and Statistical tools are used to analyze. The presented data, which includes Ratio analysis, Percentage, Regression analysis Correlation coefficient, Mean, Standard deviation, Coefficient of Variance, and time series etc.

#### **3.5.1 Financial and Accounting Tools:**

Following financial tools have been used to analyze the data in this study: Ratio analysis: By ratio analysis, we study the arithmetical relationship of two data. In this study, we have applied liquidity ratio, capital structure ratio, activity ratio and profitability ratio of the bank.

#### **3.5.2 Statistical and Mathematical Tools:**

The data presented in this study are analyzed by applying following statistical and mathematical tools.

1. Percentage increment
2. Mean.
3. Standard deviation
4. Coefficient of variance.
5. Regression analysis.
6. Correlation of coefficient.
7. Probable error.
8. Coefficient of determination.

9. Time series

**3.5.2.1 Percentage Increment Table:**

It is a table, which shows the deposit collection of bank. Here, it indicates the percentage change in deposit collection in different year.

**3.5.2.2 Mean:**

The most popular and widely used measure of representing the entire data by one value is what most lay men call an 'average' and what the statisticians call the arithmetic mean. Its value is obtained by adding together all the times and by dividing this total by the number of items. Arithmetic mean may either be simply it can be obtained as follows:

$$\bar{X} = \frac{\sum x}{N} \qquad \bar{X} = \frac{\sum Ed}{N}$$
$$\bar{X} = \frac{\sum fx}{N} \qquad \bar{X} = \frac{\sum Efd}{N}$$

**3.5.2.3 Standard deviation:**

The standard deviation concept was introduced by Karl Pearson in 1823. It is by the most important and widely used measure of studying dispersion. Its significance lies in the fact that it is free from those defects from which the earlier methods suffer and satisfies most of the properties of a good measure of dispersion. Standard deviation is also known as root-mean square deviation. It is denoted by  $\sigma$ .

**3.5.2.4 Coefficient of variance:**

This measure developed by Karl Pervasion, is the most commonly used measure of relative variation. It is used in such problems, where we want to compare the variability of two or more than two series. That series (group) for which the coefficient of variation is greater said to be more variable or conversely less consistent, less uniform, less stable or less homogeneous. It can

be obtained as follow:  $C.V. = \frac{\sigma}{\bar{x}} \times 100$ .

### 3.5.2.5 Regression Analysis:

Regression analysis is statistical device with help of which we are in a position to estimate (predict) unknown values of one variable from known values of another variable. The variable which is used to predict the variable of interest is called the independent variable and the variable we are trying to predict is called the dependent variable/explained variable. It can be formulized in the following way:-

The equation of straight line of the form  $y = a + bx$

### 3.5.2.6 Correlation Coefficient:

Correlation is a statistical device which helps us in analyzing the co-variation of two or more variable. The problem of analyzing the relation between different series should be broken down into three steps:-

1. Determining whether a relation exists and it does measuring it.
2. Testing whether it is significant.
3. Establishing the cause and effect relation, if any.

### 3.5.2.7 Probable Error:

The probable error of the coefficient of correlation helps in interpreting its values with the help of probable error it is possible to determine the reliability the value of the coefficient in so far as it depends coefficient of correlation is obtained as follows:

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

Where, r is the coefficient of correlation and N the number of pairs of observations.

### 3.5.2.8 Time Series:

The coefficient determination ( $r^2$ ) is defined as the ratio of the explained variance to the total volume.

$$\text{Coefficient of determination} = \frac{\text{Explained Variation}}{\text{Total Variation}}$$

### 3.5.2.9 Time Series:

The term 'time series' is usually used with reference to economic data and the economists largely responsible for the development of the techniques of time series analysis. However, the term 'time series' can apply to all other phenomenon that are related to time such as the number of accident occurring in a day, the variation in the temperature of a patient during a certain period.

Symbolically, we can define it, as under:

$$Y = T \times S \times C \times I$$

Y= The result of four elements

T= Trend

S=Seasonal Component

C=Cyclical Component

I=Irregular Component

## **CHAPTER FOUR**

### **DATA PRESENTATION AND ANALYSIS**

#### **4.1 Introduction:**

This chapter deals with the systematic presentation, Analysis, and interpretation of data; as it is major part of the research work. This is key chapter as it deals with the objectives specified in the first chapter.

We analyze the corporate planning system and budgeting procedure in a commercial bank with the specific context of Himalayan Bank limited and Bank of Kathmandu Limited. To accomplish these objectives, the various functional budgets analyze and related data presents in systematic way in tabular forms and graphs charts and data are analyzed using statistical tool such as mean, standard deviation coefficient of variance, correlation of coefficient and Time series and budgetary tool such as ratio analysis.

#### **4.1.1 Deposit Collection**

Customer Deposit is the most important source of resources mobilization of the bank. As per the above data of FY 2011/2012 the contribution of customer deposit to total resources of BOKL and HBL are 86.81 percent and 87.66 percent respectively. Deposit is collected from various sectors such as the general public business entities, NGO'S, school's, Trust and other individuals and institutions, which quality to open an account in the bank.

Deposit is collected on customer's account, which is opened as per the bank policy. The customer's deposits are of two types.

1. Interest free deposit accounts.

a) Current Deposit a/c

b) Margin Deposit a/c

c) Other Deposit a/c

2. Interest bearing deposit a/c

a) Saving Deposit a/c

b) Call Deposit a/c

c) Fixed Deposit a/c

(Source: Deposit collection budget of BOKL and HBL)

Following table shows the budgeted amount of deposit collection and to the same achieved actually. Since budgeted figure for deposit collection from FY 2005/06 FY 2011/2012 could not be available, this study has assumed the budgeted amount.

**Table No 1**  
**Status of Budgeted and Actual Deposit**

(Rs million)

	BOKL			HBL		
	Budget	Actual	Growth (%)	Budget	Actual	Growth (%)
2005/06	3560	4196.41	17.18	13000	14043.1	8.02
2006/07	5150	5724.13	11.15	15600	17532.4	12.39
2007/08	5500	5723.28	4.6	16800	18619.37	10.83
2008/09	6000	6170.7	2.85	19150	21007.38	9.70
2009/10	6700	7741.64	5.55	19500	22010.33	12.87
2010/11	8000	8942.75	11.78	21500	24814.01	15.41
2011/12	9500	10485.36	10.37	23900	26490.85	10.84
Average			10.6			11.44

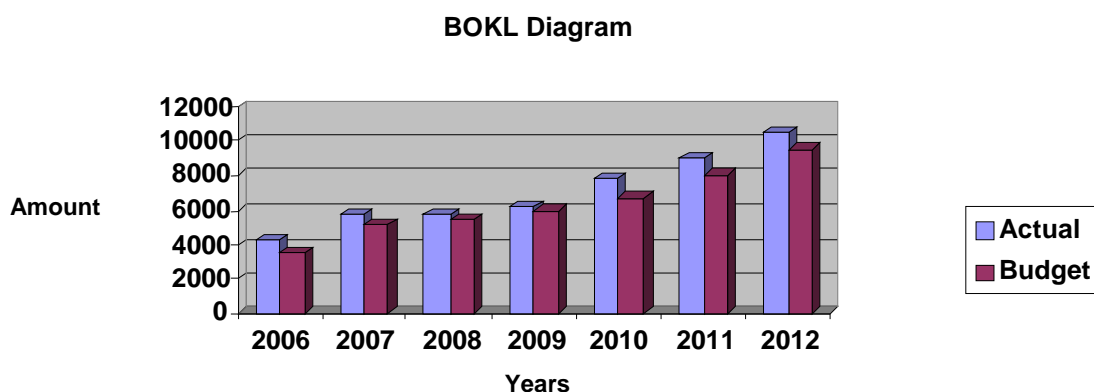
(Sources: Annual report 2005/2006 to 2011/2012)

Above table shows that the deposit collection target has been met for 100% or more than the budgeted amount of both banks. The yearly status of budgeted and actual achievements is shown in the Bar diagram and scattered.

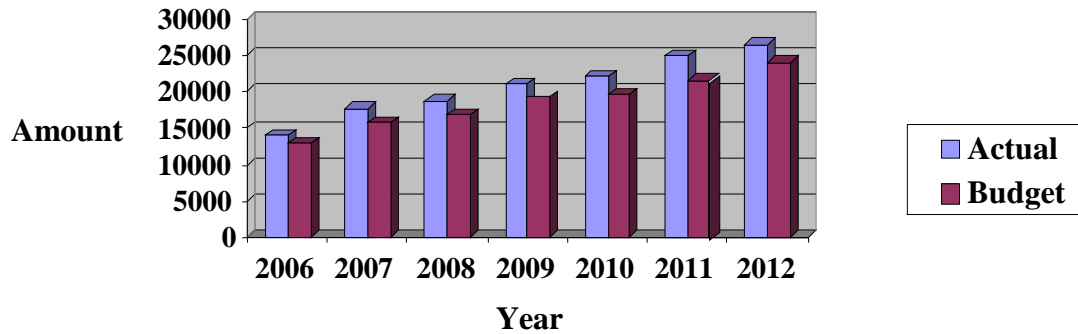
**Diagram No 1**

**Bar Diagram of Budgeted and Actual Deposit Collection of HBL & BOKL**

(Rs million)



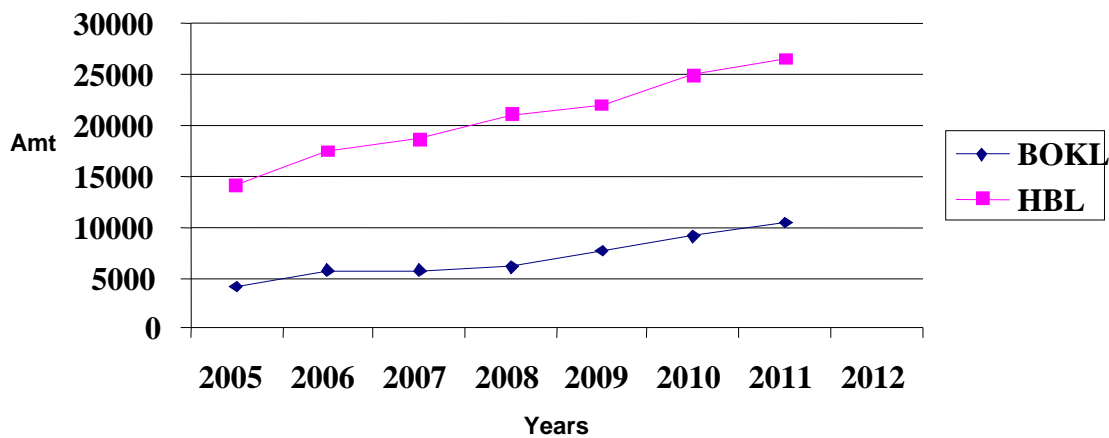
### HBL Diagram



Both bar diagram show high level of achievement made by the Banks toward deposit collection sector. The bar diagram shows the achievement level higher than the budgeted level. It shows both banks are good condition in financially.

### Diagram No 2

Actual Collection of HBL and BOKL.



Above Scatter diagram, the High achievements were made by HBL than BOKL. The entire above picture give the high level of performance of the Bank in deposit collection sector. We can find the relationship between the budgeted deposit collection with that of actual for different year by the help of statistical tools, that is arithmetic detail calculation of these, statistical tools is shows in appendix- 1. Now we are going to present summering the results from Appendix-1 we have:

**Table No 2**  
**Summary of the deposited and achievement**

(Rs million)

	BOKL		HBL	
	Budgeted X	Actual Y	Budgeted X	Actual Y
Mean	6344.29	6997.75	18492.86	20645.35
Standard deviation	1806.19	2009.89	3404.45	3980.78
C.V	0.2847	0.2872	0.1841	0.1928
Correlation (r )	0.9906		0.9957	

The above table shows that actual deposits are little more variable than budgeted deposit, since the coefficients of variation of deposits are of more variable nature. In both the banks the actual deposits is more consistent and homogeneous than budgeted deposits. A great coefficient of variation is said to be more heterogeneous. Here budgeted and Actual deposits of HBL are more homogeneous than BOKL.

We can use another statistical tool correlation coefficient to analyze the relationship between budgeted and actual deposit of both the banks. We can take the help of Karl Person's Coefficients of Correlation is denoted by (r). BY calculating 'r' we can examine whether there is positive Correlation between budgeted deposits and actual deposits or not. The actual deposit will change in the same direction, as the budgeted deposits for this purpose budgeted deposits is denoted by 'X' and assumed to be independent variable and actual deposits is denoted by 'Y' is assumed to be dependent variable upon budgeted deposit so that increase in budgeted is supported to increase in actual achievement or vice versa. Which means that there should be positive correlation between, budgeted figure and achievement figures significance of correlation of (r) is tested with probable error (PE). We have probable error of BOK is 0.00477 and PE of HBL is 0.002188.

The detail calculation of 'r' and probable error PE is presented in Appendix 1(a) and (b). From that appendix, we have calculated the value of 'r' of BOK is 0.9906 and 'r' of HBL is 0.9957. This figure of 'r' shows that is positively perfect correlation between budgeted deposit and actual deposits.

Now the coefficient of determination, which explains the change in Y variable i.e. actual deposit, can be calculated as  $r^2$  therefore, the coefficient of determination of the BOK is 0.9813 and HBL is 0.9914.

Since, r of BOK is greater than six times of probable error ( $0.9906 > 6 * 0.00477$ ) and r of HBL is also greater than six times of PE i.e.  $0.9957 > 6 * 0.002188$ . So the value of 'r' is more significant so it is no doubtful that actual deposit will go on same direction that at budgeted. Another statistical tool, regression line can also be fitted to show the degree of relationship between budgeted deposits and actual deposits and to forecast the achievement with given target. For this purpose achievement figure have been supposed to be dependent upon independent target, So that regression line of achievement 'Y' on target (X) or 'Y' on 'X' is as follows.

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

We have the following value as calculated above:

**Table No. 3**

**Summary of mean and standard deviation of budgeted and Actual**

	BOKL		HBL	
	Budgeted (X)	Actual (Y)	Budgeted (X)	Actual (Y)
Mean	6344.29	6997.75	18492.86	20645.35
Standard deviation ( $\sigma$ )	1806.19	2009.89	3404.45	3980.78
r(X;Y)	0.9906		0.9957	
	$Y - 6997.75 = 0.9906 \times \frac{2009.89}{1806.19} \times (X - 6344.29)$ $Y = 1.1023 X - 4.439 \dots \dots \dots i$		$Y - 20645.35 = 0.9957 \times \frac{3980.78}{3404.45} \times (X - 18492.86)$ $Y = 1.1643 X - 3391.19 \dots \dots \dots i$	

From the above equations (i) & (ii), it is clear that actual deposits are in increasing trend by the help of these regression equations. We ascertain the expected deposit achievement with given value of target deposits say (X) ascertain the expected deposits. Achievements for fiscal year,2011/12.

**For BOKL (Rs million)**

When X=10200

The expected deposit achievement

$$Y=1.1023 \times 10200 - 4.439$$

$$Y=11243.46 - 4.439$$

$$Y=11239.021$$

**For HBL (Rs million)**

when X=24500

the expected deposit achievement

$$Y=1.1643 \times 24500 - 3391.19$$

$$Y=28525.35 - 3391.19$$

$$Y=25134.16$$

If the relation between deposits and actual deposits remain same as previous year than the actual deposits of BOKL & HBL for the fiscal year 2011/2012 will be Rs 11239.021 and Rs 25134.16 respectively as stated by the above regression line equations.

The following table shows the data of actual deposit mobilized by the bank as of the end of each fiscal year. The table shows the amount of deposit is fluctuate.

**Resources other than Customer Deposit (RMOD)**

This is another resource of Bank which is formed with the capital fund (the net worth) and the liabilities other than customer deposits.

The following table shows the figure of RMOD resources.

**Table No 4****Status of Resources (capital fund) other than Deposit****(Rs million)**

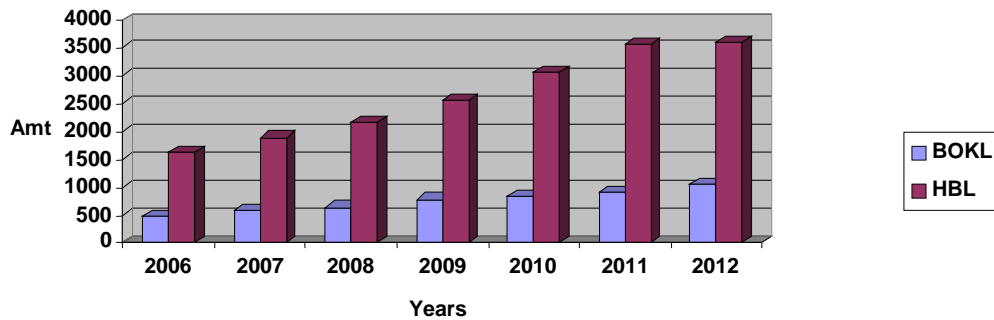
	BOKL			HBL		
	Capital fund	Growth	Percent	Capital fund	Growth	Percent
2005/06	482.55	-----	-----	1691.99	---	-----
2006/07	585.26	102.71	21.28	1888.64	268.55	15.88
2007/08	633.37	48.11	8.22	2162.46	273.82	14.50
2008/09	775.87	142.50	22.50	2544.75	382.29	17.68
2009/10	842.54	66.67	8.59	3060.45	515.7	20.26
2010/11	908.38	65.84	7.81	3551.28	490.83	16.04
2011/12	1039.78	131.4	14.46	3584.33	33.05	0.93
Average			13.81			14.215

(Sources: Annual report 2005/06 to 2011/2012)

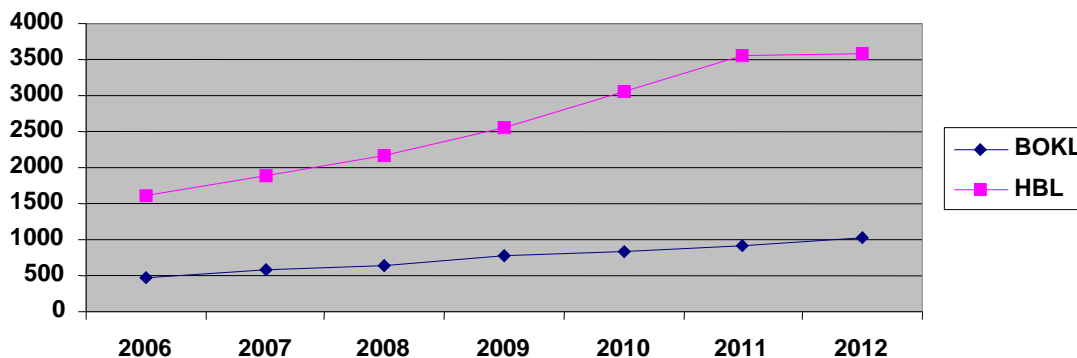
The table shows the RMOD status of HBL is greater than BOKL. The actual RMOD of HBL is increasing trend in the first fourth years but decreasing trend in last two years. Similarly in the BOKL has fluctuated trend in first four years but increasing trend in last 2 years. The

status of the resources mobilized from the source other than customer deposit is shown by the scattered and bar diagram as below.

**Diagram No 3**  
**Status of RMOD**



**Diagram No 4**  
**Status of Resources (capital fund) other than Deposit**



#### 4.1.2 Resources Deployment Plan:

Deployment of the resources refers to the reasonable allocation of the resources of the making comfortable liquidity as well as investing in income generating activities. Beside these, some investments have to be made in fixed assets and other operating assets for the bank. The deployment of available resources can be objectively categorized as below.

- i) Deployment for liquidity.
- ii) Deployment for income generating activities.
- iii) Deployment for other asset.

##### i) Deployment for liquidity:

This is made for meeting expected withdrawal and other kind of payments obligations of the

bank. The resources for this purpose are kept in liquid form such as cash in vault, cash at bank etc. Generally there is no yield on this type of deployment excepting in the cash money placed in interest bearing account. The Central Bank of Nepal (NRB) at has instructed commercial bank to mandatory maintain approximately 10% of their total customer deposit liability as liquid form (cash in vault) and at (NRB) for this study, cash and bank balance is grouped in one dependent portfolio. The following table shows the cash and Bank balance figure of the bank.

**Table No 5**  
**Status of cash and Bank balance**

**(Rs million)**

	BOKL			HBL		
	Actual	Growth	Percent	Actual	Growth	Percent
2005/06	637.79	-----	-----	901.91	-----	-----
2006/07	1134.78	496.99	77.92	1435.17	533.26	59.12
2007/08	683.65	-451.13	-39.75	1264.67	-170.5	-11.88
2008/09	692.71	9.06	1.33	1979.21	714.54	56.5
2009/10	782.88	90.17	13.02	2001.18	21.97	1.11
2010/11	740.52	-42.36	-5.41	2014.47	13.29	0.66
2011/12	728.7	-11.82	-1.60	1717.35	-297.12	-14.75

Sources: Annual report 2005/06 to 2011/2012

The cash and bank balance of HBL is increased in first year but decreased in second and fluctuate trend in next years excepting last years. At FY 2011/012, it decreased by 14.75. BOKL cash and bank balance is increased in first 2 year but decreased in FY 07/08, 010/011 & 011/012. The main causes of fluctuated in cash balance no security in Bank by political instability. So, most of the people deposited their money in foreign Bank.

**ii) Deployment for income generating activities:**

Bank deploys the major portion of the resources is deployed for income generating activities popularly called as fund based exposure. Fund based exposure are taken by the bank in following two portfolio.

- a) Loan & advance, and Bill purchased (LABP)
- b) Other Investment.

LABP includes all loans, advances, overdrafts, bills purchased/discounted, provision and other types of loans availed to the borrowers of the bank in return of which the bank earns interest income. Other investment include investment in shares, Treasury bill (TB), Placement of fund on call market etc. the following table shows the status of LABP and other investment made by banks.

**Table No 6**  
**Status of LABP and Investment**

(Rs million)

	BOKL				HBL			
	LABP	%	Investment	%	LABP	%	Investment	%
2005/06	3087.63	-----	143.43	-----	7224.73	-----	2216.42	----
2006/07	4256.28	37.85	395.22	175.55	9015.35	24.78	4083.16	84.22
2007/08	4613.7	8.4	619.45	56.73	9557.12	6.01	9157.12	124.27
2008/09	4542.7	-1.54	1778.14	187.05	10844.6	13.47	10175.43	11.12
2009/10	5646.7	24.3	2477.41	39.32	12919.63	19.13	9292.1	-8.68
2010/11	5912.58	4.71	2598.25	4.88	13451.17	4.11	11692.34	25.83
2011/12	7259.08	22.77	3374.71	29.88	15761.98	17.18	10889.03	-6.87

Sources: Annual report 2005/06 to 2011/12.

The above table shows the status of LABP and investment of both Banks. LABP and investments is the major portion of the resources deployment. The LABP and investments of BOKL has increasing in all years except FY 2008/09. Investment of BOK increasing in every year. Investment of HBL decreased in FY 2009/10 & 2011/12. The main causes of decreased in investment of HBL is National crises and political Instability.

**iii) Deployment for other assets:**

This including assets such as fixed assets, other capital expenditure. Subject to write off in future course of times income receivables, advance payments, sundry debtors etc. the following table shows the status of resources deploy by bank in other assets.

**Table No 7**  
**Status of other assets**

**(Rs million)**

	BOKL				BOKL			
	Net fixed assets	%	Other assets	%	Net fixed assets	%	Other assets	%
2005/06	53.03	----	234.25	-----	193.04	----	644.88	-----
2006/07	102.02	92.38	204.50	-12.7	201.68	4.47	707.56	9.72
2007/08	94.21	-7.66	170.24	-16.75	318.84	58.09	665.74	-5.91
2008/09	93.64	-0.61	269.26	58.16	229.87	-27.91	818.76	22.98
2009/10	83.63	-10.69	233.41	-13.32	299.64	-69.65	848.33	3.61
2010/11	95.23	13.87	181.67	-22.17	295.82	-1.28	976.46	15.1
2011/12	110.74	16.29	203.69	12.12	203.69	82.82	665.34	-31.86

Sources: Annual Reports 2005/06 to 2011/12.

The above table shows the deployment of the banks available resources into various portfolios among which the LABP holds the biggest outlet of resources deployment of HBL is higher than BOKL deployment. Hence, we have segregated the deployment into two categories in this study.

1. Deployment in LABP
2. Deployment in other sector than LABP (NLABP)

#### **4.1.2.1 LABP Budget**

The following table shows the status of LABP

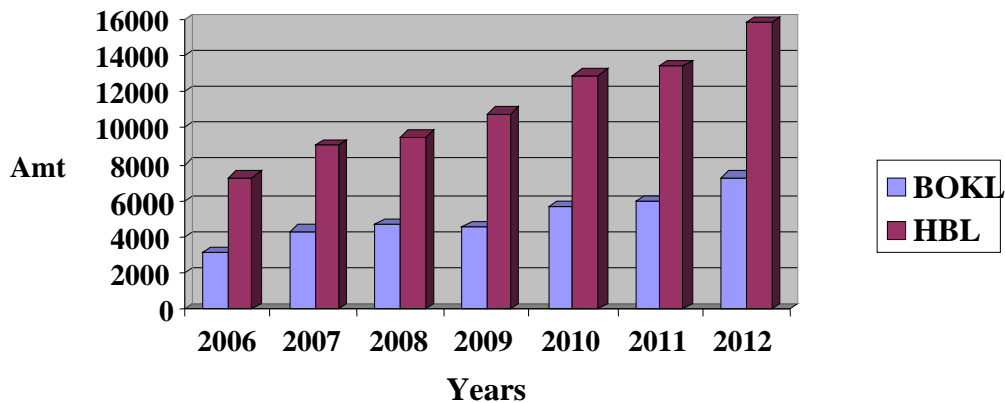
**Table No 8**  
**Status of LABP (Rs million)**

	BOKL			HBL		
	LABP	Growth	Percent	LABP	Growth	Percent
2005/06	3087.63	-----	-----	7224.73	-----	-----
2006/07	4256.28	1168.65	37.85	9015.35	1790.62	24.78
2007/08	4613.7	357.42	8.4	9557.12	541.77	6.01
2008/09	4542.7	-71	-1.54	10844.6	1287.48	13.47
2009/10	5646.7	1104	24.30	12919.63	2075.03	19.13
2010/11	5912.58	265.88	4.71	13451.17	531.54	4.11
2011/12	7259.08	1346.5	22.77	15761.98	2310.81	17.18
Average			16.08			14.11

(Sources: Annual report 2005/06 to 2011/012)

The above table shows growth rate of LABP. The growth rate of HBL has increased in first year and decreased in second year. After the second year growth is increasing up to fourth year. At the last year growth is increasing trend. Similarly the growth rate of BOKL has decreased in first three years and at the last year growth is increasing trend. From the main reason for fluctuating in LABP is investor's own security and their business security. Most of the industry and business are closed from strike. The statuses of LABP deployment are presented in the scatter diagram and bar diagram as below.

**Diagram No 5**  
**Bar Diagram of LABP Status**



From the above diagram and Table, it is clear that the LABP are increasing. The LABP of HBL is higher than BOKL. Both the Bank's LABP are increased positively but in the FY 2003/04 of BOKL has negative.

**4.1.2.2 Resources Deployments in other portfolio than LABP (NLABP)**

Deployment in other portfolio than LABP includes cash and bank, investment, fixed assets and other assets. The following table shows the status of NLABP.

**Table No 9  
Status of NLABP**

**(Rs million)**

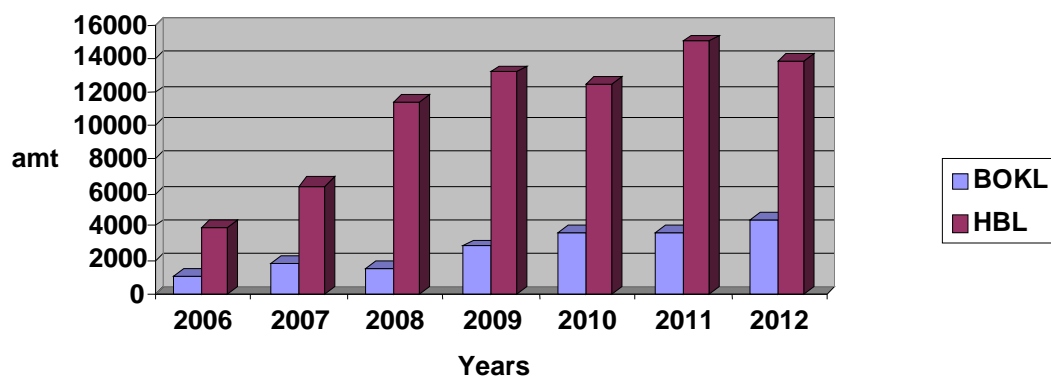
	BOKL			HBL		
	NLABP	Growth	Percent	NLABP	Growth	Percent
2005/06	1069.1	-----	-----	3956.25	-----	-----
2006/07	1836.52	767.42	71.78	6427.57	2471.32	62.47
2007/08	1567.55	-268.97	-14.64	11406.37	4978.8	77.46
2008/09	2833.75	1266.2	80.77	13203.27	1796.9	15.75
2009/10	3577.33	743.58	26.24	12441.25	-762.02	-5.77
2010/11	3615.67	38.34	1.07	14979.09	2537.84	20.40
2011/12	4417.84	802.17	22.19	13812.54	-1166.55	-7.79
Average			31.19			27.09

Sources: Annual report 2005/06 to 2011/12

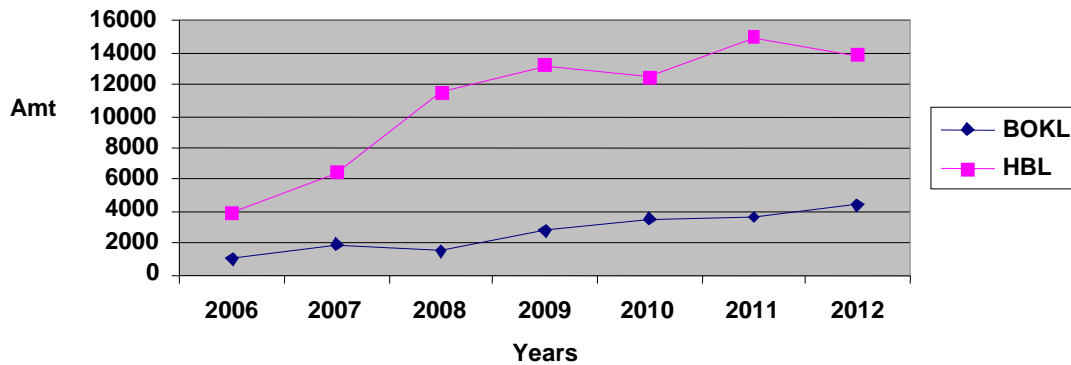
The above table shows NLABP of BOKL is gradually increasing in last 5 years to now. But HBL growth is significantly increased in first 3 year then after it is fluctuating.. BOKL average growth rate is higher than HBL.

The status of the resources deployment to other portfolio than NLABP is shown by the Bar diagram and Scattered diagram is below.

**Diagram No 6  
Bar diagram of the status of NLABP**



**Diagram No 7**  
**Scatter Diagram of the status of NLABP**



The above table and diagram show the investment in NLABP of HBL is satisfactory than BOKL because its growth rate has significantly increased but NLABP of BOKL growth rate is slowly and gradually.

**4.1.2.3 Expenditure Planning:**

Planning for expenses is most essential to achieve the objectives and planned programs of the bank. Every bank has to bear certain Expenses to operate its day today activities like staff salaries, bonus and remuneration, interest amount to the deposit holders, administrative costs, provision for possible loss, house rent, fuel for vehicles, water and electricity expenses, stationery etc. these expenses are necessary to possible has to service to gain maximum profit, the following table shows the status of expenditure incurred by the bank during the study period.

**Table No 10**  
**Status of Expenses**

**(Rs million)**

	HBL													
	2005/06		2006/07		2007/08		2008/09		2009/10		2010/11		2011/12	
Interest	594.80	57.01	734.52	56.58	578.13	50.06	554.13	44.61	491.54	39.12	561.96	38.69	648.84	39.48
Salaries, allowance	58.88	5.74	85.57	6.59	101.54	8.79	120.14	9.67	152.51	12.14	178.59	12.30	234.59	14.27
Provision for bonus	34.85	3.34	48.34	3.72	38.78	3.36	40.00	3.22	46.73	3.72	58.06	4.00	67.24	4.09
Other expenses	103.25	9.90	134.32	10.36	166.51	14.42	202.87	16.33	186.23	14.82	147.14	10.13	145.16	8.83
Depreciation	132.54	12.70	141.12	10.87	155.79	13.49	177.13	14.26	211.05	16.79	277.37	19.10	329.70	20.06
Provision for taxes	114.32	10.96	154.32	11.89	114.02	9.88	147.89	11.90	157.52	12.54	214.26	14.75	214.94	13.08
Non Operating	3.67	0.35	0	0	0	0	0	0	10.99	0.87	15.01	1.02	2.90	0.19
<b>Total</b>	<b>1043.31</b>	<b>100</b>	<b>1298.19</b>	<b>100</b>	<b>1154.77</b>	<b>100</b>	<b>1242.16</b>	<b>100</b>	<b>1256.57</b>	<b>100</b>	<b>1452.39</b>	<b>100</b>	<b>1643.37</b>	<b>100</b>

**(Rs million)**

	BOKL													
	2005/06		2006/07		2007/08		2008/09		2009/10		2010/11		2011/12	
Interest	237.91	64.07	310.48	60.93	285.01	50.69	279.71	50.21	286.30	47.81	241.64	39.19	308.16	44.52
Salaries, allowance	18.05	4.86	30.17	5.92	50.15	8.92	51.68	9.26	47.73	7.97	53.82	8.73	59.12	8.54
Provision for bonus	11.47	3.09	10.37	2.03	2.99	0.53	13.57	2.44	20.52	3.43	22.70	3.68	30.12	4.35
Other expenses	64.57	17.39	118.62	23.28	190.46	33.88	157.70	28.31	101.26	16.91	133.92	21.72	78.38	11.33
Depreciation	6.79	1.83	11.93	2.34	16.01	2.85	14.46	2.60	85.83	14.33	99.71	16.17	117.59	16.99
Provision for taxes	32.52	8.76	28.01	5.50	17.59	3.13	40.01	7.18	57.17	9.55	64.76	10.50	98.77	14.27
<b>Total</b>	<b>371.31</b>	<b>100</b>	<b>509.58</b>	<b>100</b>	<b>562.21</b>	<b>100</b>	<b>554.13</b>	<b>100</b>	<b>598.81</b>	<b>100</b>	<b>616.55</b>	<b>100</b>	<b>692.14</b>	<b>100</b>

(Sources: Annual report 2005/06 to 2011/12)

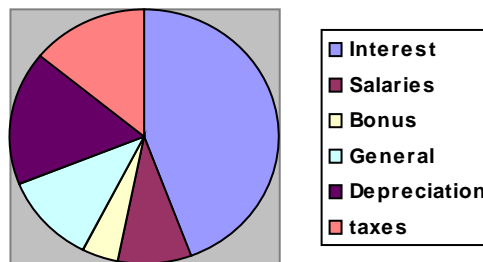
Interest expenses of both Banks are decreasing except FY 2011/12. It means both bank deposit interest rate is decreasing. Salary, allowance and provision for bonus are increasing. It shows both Banks are in expansion period. Operating expenses of HBL is increasing gradually then BOKL. Both Banks needs decreased their own operating expenses in

comparative other expenses. The above table shows that the each type of expenses is increasing both the banks. The interest payment is the highest portion of total cost for each year. Percentage wise classification of expenses of FY 2011/12 of Himalayan bank Limited and Bank of Kathmandu.

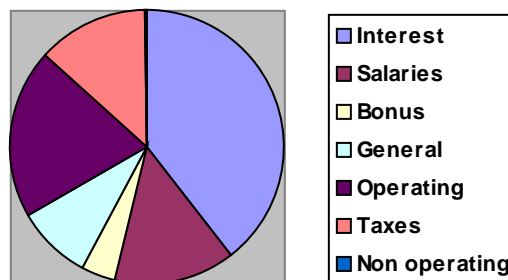
**Diagram No 8**

**Pie chart of expenses**

**BOKL**



**HBL**



**4.1.2.3.1 Interest Expenses:**

Interest Expenses are the expenditure incurred for making payment of interest to the borrowing and deposit mobilized by the bank. As the customer deposit holds a major share on total resources of the bank, so the interest expenses remained highest among other in total Expenses of the bank. Both banks have no long term loan provisions so far. They have only short term loan and pay less amount of interest on borrowing then deposits. Hence, the percentage of the interest expenses to the total deposit is presented in the following table.

**Table No. 11**  
**Status of Interest Expenses**

**(Rs million)**

	BOKL			HBL		
	Interest expenses	Total deposit	Cost of deposit	Interest Expenses	Total deposit	Cost of deposit
2005/06	230.78	4196.41	5.5	588.92	14043.1	4.19
2006/07	287.37	5724.13	5.02	721.8	17532.4	4.12
2007/08	282.42	5723.28	4.93	571.64	18619.38	3.07
2008/09	273.77	6170.7	4.44	517.99	21007.38	2.46
2009/10	279.50	7741.64	3.61	455.87	22010.33	2.07
2010/11	232.66	8942.75	2.6	525.75	24814.01	2.12
2011/12	294.51	10485.36	2.81	613.88	26490.85	2.32
Average			4.12			2.91

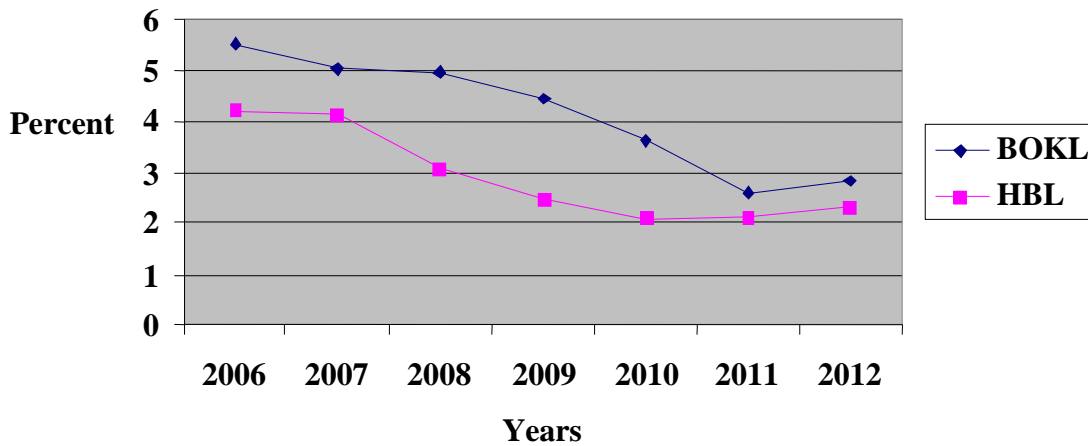
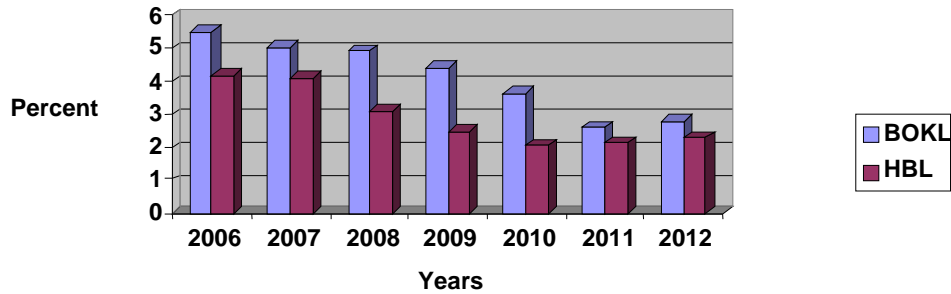
Sources: Annual report 2005/06 to 2011/2012.

There are various kinds of deposit accounts like interest free deposit and varying interest deposit accounts. The average cost incurred by the banks for cost of deposit (COD) of the bank. The lower COD refers to better position in terms of profitability.

The above table shows that the yearly COD of deposit of BOKL ranges from 2.6 to 5.5 percent and cost of deposit of HBL ranges from 2.07 to 4.19 percent. The average cost of deposit for the study period of BOKL is 4.12 percent and HBL is 2.91 percent. Hence the cost of deposit of HBL is better than COD of BOKL being lower. The status of COD is shown in bar diagram and scattered diagram as below.

**Diagram No. 9**  
**Status of bar diagram and scattered of COD**

(In %)



The figure of actual deposit amount and interest expenses amount can be presented in tabular form. In order to find out the variability of deposit collection and interest on deposit of different years the calculations of arithmetic mean, standard deviation and coefficient of variation technique and correlation of coefficient are required. The detailed of application of those statistical tools are presented in appendix 2. The summary of the results of appendix 2 are given below.

**Table No. 12**  
**Summary of the Deposit & Interest Expenses relation**

**(Rs million)**

	BOKL		HBL	
	Deposit (x)	Interest exp.(Y)	Deposit (X)	Interest exp (Y)
Mean	6997.75	268.72	20645.35	570.84
S.D	2009.89	24.15	3980.78	78.39
C.V	0.2872	0.08987	0.1928	0.1373
'r'				
PE				

The above results show that the customer deposit is more variable than interest expenses in both banks. Hence the coefficient of variation of deposit is higher of BOKL than HBL and C.V (coefficient or variation) of interest expenses of HBL is higher than BOKL. Another statistical tool correlation of coefficient can be used to a show relationship between total deposit and interest expenses. In this analysis deposit is independent variable (x) and Interest Expenses is dependent Variable (Y) the main objective of this analysis is to find out whether deposit are significantly used to interest Expenses in proper way or not. The above table shoe the relationship between X and Y variables.

Above table show correlation coefficient of BOKL is positive correlation between these two variables but correlation coefficient of HBL is Negative correlation between these two variables. Thus, deposit and interest is not correlation with each other of HBL.

After this significance of 'r' is tested with probable error of r, the detail calculation of 'r' and probable error of 'r' is presented in Appendix 2a, 2b. The value of 'r' and P.E of HBL are -0.3220 and 0.2285 respectively. Similarly value of 'Y' and P.E of BOKL are 0.2611 and 0.2376 respectively.

Since  $r > 6 PE$

**HBL**

$$= -0.3222 < 6 \times 0.2285$$

$$= -0.3220 < 1.371$$

**BOKL**

$$= 0.2611 < 6 \times 0.2376$$

$$= 0.2611 < 1.4256$$

Hence, there is negative correlation in deposit and interest expenses of HBL but positive correlation in BOKL.

### 4.1.3 Revenue Planning:

Banks generate revenue from its income earning activities. Such activities are mostly fund based, that is generated out of the deployment of fund, and some portion from non fund based business activities. It can be categorized into two types like interest income and other income. Interest income is the interest earned from the loan advances and overdraft provided to the borrower's investment in Nepal government bonds etc. interest income holds major share in total income portfolio of the banks. Other income consists excluding interest incomes, which are shown as follows.

- a) Income from commission and discount.
- b) Dividend received from investment in shares.
- c) Income from foreign exchange transactions.
- d) Various kinds service fees and charges etc.

**Table No 13**  
**Status of Yearly Income structure**

(Rs million)

	BOK													
	2005/06		2006/07		2007/08		2008/09		2009/10		2010/11		2011/12	
Interest	371.68	84.08	465.03	80.88	473.33	82.82	496.81	78.08	567.10	78.08	607.10	80.25	718.12	79.77
Commission & discount	30.47	6.89	46.22	8.04	47.87	8.38	60.75	9.55	77.71	10.70	72.35	9.56	70.78	7.86
Foreign exchange	38.66	8.75	63.06	10.97	48.65	8.51	67.44	10.60	64.05	8.81	72.11	9.54	78.95	8.77
Other exp.	1.11	0.25	0.63	0.11	0.74	0.13	11.24	1.767	1.97	0.27	4.47	0.59	16.97	1.88
Non operating	0.11	0.03	-----	0	0.93	0.16	0.02	0.003	15.46	2.14	0.47	0.06	15.46	1.72
Total	442.03	100	574.94	100	571.49	100	636.26	100	726.29	100	755.56	100	900.28	100

(Sources: Annual report 2005/06 to 2011/2012).

(Rs million)

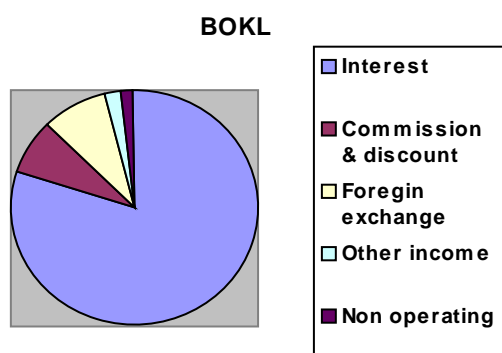
	HBL													
	2005/06		2006/07		2007/08		2008/09		2009/10		2010/11		2011/12	
Interest	1033.66	83.18	1326.38	84.20	1149.00	82.67	1201.23	82.60	1245.89	81.99	1446.47	82.15	1626.47	77.42

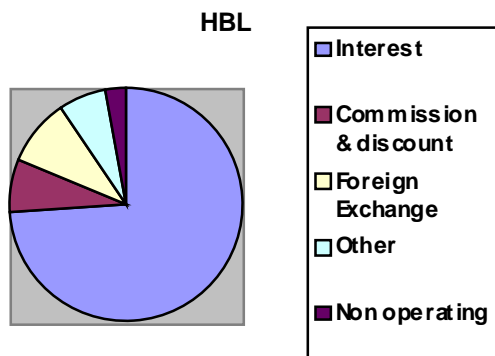
Commission & discount	110.33	8.88	96.06	6.10	101.70	7.32	102.56	7.05	123.93	8.15	132.82	7.54	165.45	7.87
Foreign exchange	87.33	7.03	119.26	7.57	104.60	7.53	109.60	7.54	112.42	7.40	137.30	7.80	198.13	9.44
Other Income	9.68	0.78	31.22	1.98	32.04	2.30	30.15	2.07	34.08	2.24	41.30	2.35	52.32	2.49
Non operating	1.69	0.13	2.30	0.15	2.45	0.18	10.76	0.74	3.30	0.22	2.79	0.16	58.45	2.78
Total	1242.69	100	1575.22	100	1389.79	100	1454.30	100	1519.62	100	1760.68	100	2100.82	100

(Sources: Annual report 2005/06 to 2011/12).

The above table shows that interest income of both banks are decreasing. Both banks give more facility in low interest rate. Both bank foreign exchanges are fluctuating because of operating new bank and agencies for remittance. Commission are discount of HBL is fluctuating because there own facilities. BOKL commission and discount also fluctuating because there new scheme for opening bank account.

**Diagram No. 10**  
**Pie charts of income generate**





#### 4.1.3.1 Interest Income:

Interest income contributes the major portion of total revenue mix, this study attempts to analyze the interest income amount with other relevant data. Interest income is generated out of the loan and advances made by the bank. Therefore, this is popularly called yield on fund (YOE) Bills discounting is also one form of advances there fore, for this study purpose, we have grouped the outstanding loan, advance and overdraft and the bills discounting commission too into the total interest income amount (YOE). The picture of total YOE with the total LABP are presented with the help of the following table, bar and scatter diagrams.

**Table No 14**  
**Status of Interest and LABP of BOKL & HBL**

(Rs million)

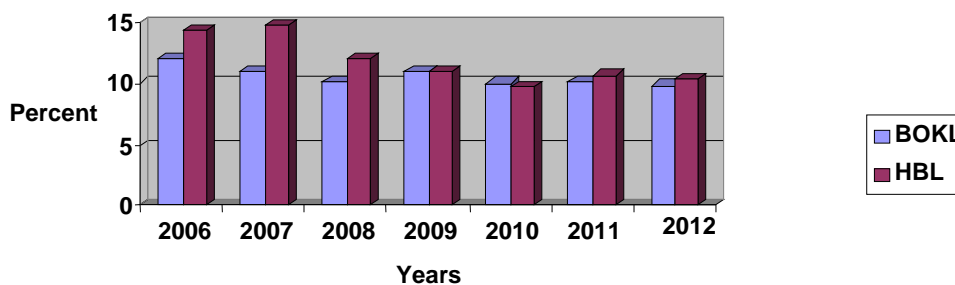
	BOKL			HBL		
	Interest income	LABP	Yield on LABP	Interest income	LABP	Yield on LABP
2005/06	371.68	3087.63	12.04	1033.66	7224.73	14.31
2006/07	465.03	4256.28	10.93	1326.38	9015.35	14.71
2007/08	473.30	4613.7	10.26	1148.99	9557.12	12.02
2008/09	496.81	4542.7	10.94	1201.23	10844.6	11.08
2009/10	567.1	5646.7	10.04	1245.89	12919.63	9.64
2010/11	607.1	5912.58	10.27	1446.47	13451.17	10.75
2011/12	718.12	7259.08	9.89	1626.47	15761.98	10.32
Average			10.62			11.83

Sources: Annual reports 2005/06 to 2011/12.

Yield on LABP of BOKL is decreased in first three then after fluctuating. HBL first year increased then after three years decreasing after first fourth years it is fluctuating. The main reason of decreasing of BOKL is more LABP in low interest rate. Same as HBL has own policy in low interest rate investment because that time bank have collected more deposit

from different scheme. After first four year both bank yield on LABP is fluctuating by their investment policy some time in LABP sometime other than LABP. High LABP is more suitable for to getting profit.

**Diagram No 11**  
**Bar diagram showing interest to total LABP (In %)**



The above diagram shows, that both interest income and LABP are decreasing in the both the banks.

#### 4.1.4 Interest Spread:

Interest spread refers to the deviation of total interest expenses and the total interest earned. It is the margin on interest earned. It is the margin on interest or net interest income of the bank. It can be shown in formula:

Interest spread = interest income-interest expenses.

The following table shows the interest shows in the different year.

**Table No 15**  
**Net spread of the Banks**  
**(Rs million)**

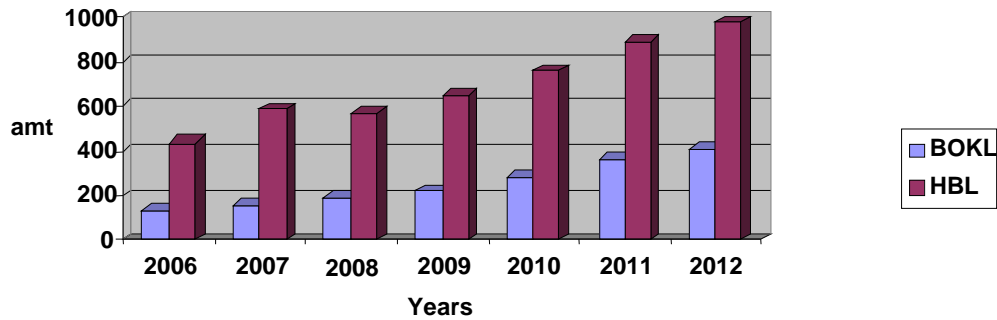
	BOKL				BOKL			
	Interest income	Interest expenses	Interest spread	%	Interest income	Interest expenses	Interest spread	%
2005/06	371.68	237.91	133.77	100	1033.66	594.8	438.86	100
2006/07	465.03	310.48	154.55	115.53	1326.38	743.52	582.86	133.27
2007/08	473.3	285.01	188.29	121.83	1149	578.13	570.87	97.94
2008/09	496.81	276.71	220.1	116.89	1201.23	554.13	647.1	113.35
2009/10	567.1	286.3	280.8	127.58	1245.9	491.54	754.36	116.58
2010/11	607.1	241.64	365.46	130.15	1446.47	561.96	884.51	117.25
2011/12	718.12	308.16	409.96	112.18	1626.47	648.84	977.63	110.53
Average			250.42				693.74	

Sources: Annual reports 2005/06 to 2011/12.

Percentage change of interest spread in compare last year for every year of BOKL and HBL

is fluctuating. The main cause of fluctuating of BOKL is high interest rate in deposit and low interest rate in loan because in competition with others join venture and new commercial bank. Same as HBL, the min causes of fluctuating is investment policy in different interest rate.

**Diagram No 12**  
**Bar diagram of interest spread.**



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#### 4.1.5 Burden:

Burden is the overall expenses of the bank, excepting interest expenses incurred for the payment of interest on deposit. The operating cost of the bank excepting cost interest cost is called the burden. The net burden is the net amount of burden cost obtained which is the difference between other expenses and other income. The nature of the cost is semi fixed where as interest cost is variable cost. The following table shows the status of net burden.

**Table No 16**  
**Status of net burden**

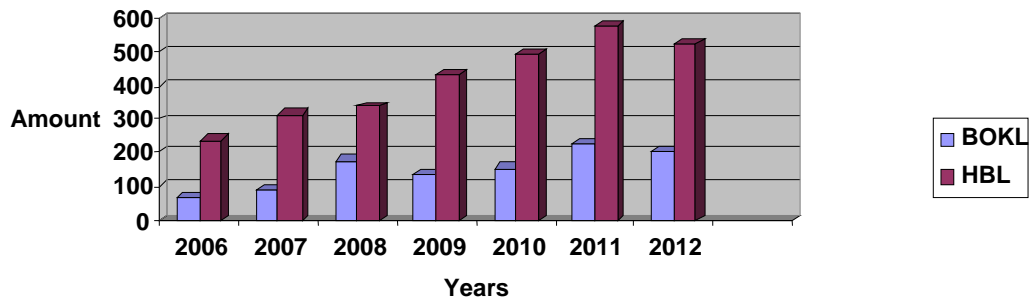
(Rs million)

	BOKL				HBL			
	Other expenses	Other income	Net burden	%	Other expenses	Other income	Net burden	%
2005/06	133.4	70.35	63.05	100	448.51	209.03	239.48	100
2006/07	199.1	109.91	89.19	141.46	563.67	248.84	314.83	131.46
2007/08	277.2	98.19	179.01	200.71	576.64	240.8	335.84	106.67
2008/09	277.42	139.45	137.97	77.07	688.03	253.07	434.96	129.51
2009/10	312.51	159.19	153.32	111.13	765.03	273.73	491.3	112.95
2010/11	374.91	148.46	226.45	147.70	890.43	314.21	576.22	117.28
2011/12	383.98	182.16	201.82	89.12	994.53	474.35	520.18	90.27

Sources: Annual reports 2005/06 to 2011/2012.

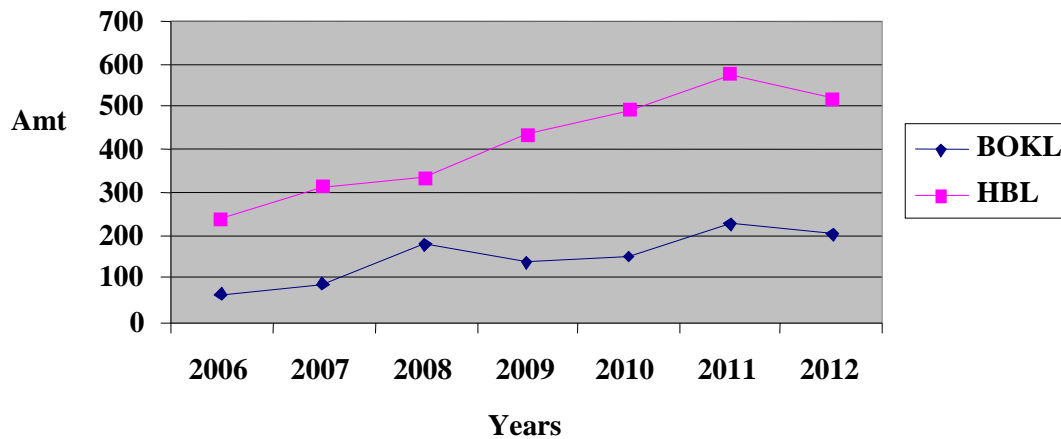
**Diagram No 13**

**Bar diagram of annual net burden**



**Diagram No 14**

**Scatter diagram of annual net burden**



The above table, bar diagram and scatter diagram shows that the net burden of HBL is higher than BOKL. The net burden is increasing trend of HBL and BOKL at 2010/11 and at last both bank burdens are decreasing.

#### **4.1.6 Net profit:**

Profit is excess of income over expenses net profit is a reward to the bank for efficient mobilization of its deposit. The net profit is the excess spread over the net burden. Spread is the net interest income (excess interest income over interest expenses), and the net burden is the difference between other expenses and other income. The following table shows the status of net profit.

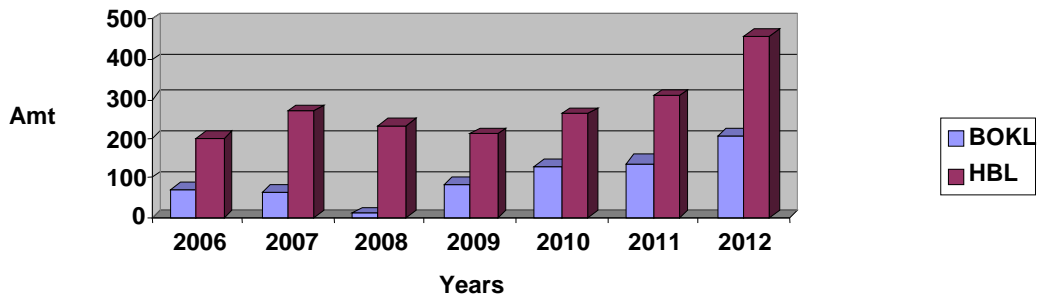
**Table No 17**  
**Status of net profit**

**(Rs million)**

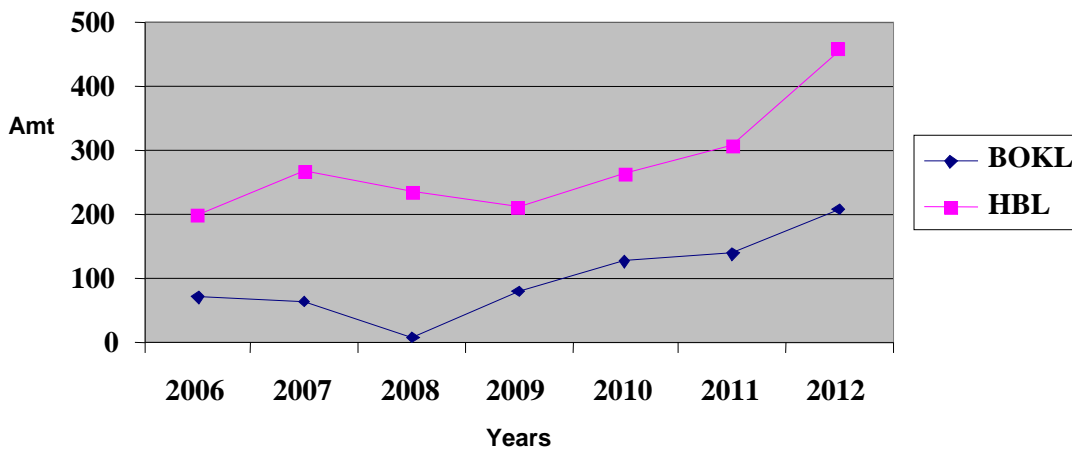
	BOKL				HBL			
	Spread	Burden	Profit	%	Spread	Burden	Profit	%
2005/06	133.77	63.05	70.72	100	438.86	239.48	199.38	100
2006/07	154.55	89.19	65.36	92.42	582.86	314.83	268.03	134.43
2007/08	188.29	179.01	9.28	14.88	570.87	335.84	235.03	87.69
2008/09	220.10	137.97	82.13	885.02	647.1	434.96	212.14	90.26
2009/10	280.8	153.32	127.48	155.22	754.36	491.30	263.06	124.00
2010/11	365.46	226.45	139.01	109.04	884.51	576.22	308.29	117.19
2011/12	409.96	201.82	208.14	149.73	977.63	520.18	457.45	148.38

Sources: Annual reports 2005/06 to 2011/12.

**Diagram No 15**  
**Bar diagram of net profit**



**Diagram No 16**  
**Scatter diagram of net profit**



The above diagram shows that the net profit of BOKL is decreasing trend in the first three years and then after that is increasing gradually. Similarly, the net profit of HBL is increased in first two years then after that is decreasing at 2008/09 that after, increasing gradually. Both bank burdens is increased in comparative of there spread so both bank decrease their burden to get high net profit.

#### **4.1.7 Performance Evaluation:**

Performance evaluation is an important part for profit planning and control system. Non manufacturing or service firm can also use performance evaluation tools. We can use various techniques and criteria to evaluate performance.

Ratio analysis is the numerical relationship between any two variables of financial statements, which should serve some meaningful purpose. Ratios are expressions of logical relationships between items in the financial statements of a single period. Analysis can compute many ratios from the same set of financial statements. A ratio can show a relationship between two items on the same financial statement or between two items on different financial statements e.g. ratios is the required that the items used to construct a ratio have a logical relationship to one another.

##### **4.1.7.1 Ratio Analysis:**

Ratio's measure a firm's crucial relationships by relating its inputs (costs) with outputs (benefits) and facilitate comparisons of these relationships over time and across firms. The objective of ratio analysis is a comparative measurement of risk and return, facilitating intelligent investment and credit decisions. For this purpose profitability ratio can be used. Which is classified as follows:

1. Net Profit to Total Assets Ratio
2. Net Income to Total Deposit Ratio
3. Return on net worth (shareholders equity)
4. Return on loan and advance Ratio

Profitability ratios are very helpful to measure the overall efficiency of operation of financial institutions. In the context of banks, strictly speaking no bank can survive without profit. Profit is the indicator of providing different services to its customers or by making investment of different kinds. Sufficient profit is must to have good liquidity, grab investment opportunities, expand banking transaction, financial government in need of development

fund, overcome the future contingencies and need fixed internal obligation for a bank. Profitability ratios measure the efficiency of bank. Higher the profit ratio shows that shows that higher the efficiency of a bank.

The following profitability ratios are related to study in this heading.

### 1. Net profit to total assets ratio

It is the ratio of net income and total asset. It measures the return on all the firm's assets after interest and taxes. ROA shows the management's capability to generate profit on using assets. A decrease in return on assets may mean that assets grow faster than sales. It is not good trend.

$$ROA = \frac{\text{Net Income}}{\text{Total Assets}}$$

**Table No 18**  
**Net Profit to total assets ratio**

(Rs million)

	BOKL			HBL		
	Net profit	Total asset	Ratio	Net profit	Total asset	Ratio
2005/06	70.72	4678.95	1.51	199.38	15863.74	1.26
2006/07	65.36	6409.39	1.02	277.04	19500.57	1.42
2007/08	9.28	6356.65	0.15	235.02	21315.85	1.10
2008/09	82.13	7444.81	1.10	212.13	24197.97	0.88
2009/10	127.47	9496.35	1.34	263.05	25729.79	1.02
2010/11	139.53	9857.13	1.42	308.23	28871.34	1.07
2011/12	202.44	12278.33	1.65	457.46	30579.81	1.5
Average			1.17			1.18

Sources: Annual reports 2005/06 to 2011/12.

The above table shows the ratio of net profit to total assets the net profit to total assets ratios of HBL, are in fluctuating trend and has ranged 0.88 percent to 1.50 percent. Similarly, in BOKL ratios are also in fluctuating trend, and have ranged 0.15 percent to 1.65 percent. Average ratio of HBL is 1.18 percent and BOKL is 1.17 percent. On the basis of average ratio, net profit to total assets ratio of HBL has appeared better position than BOKL. Comparatively HBL has been able to earn more profit by utilizing their resources and profit planning tools.

## 2. Net income to total deposit ratio

Net income is a reward to the bank for efficiency mobilization of its deposit. So, it would be reasonable meaningful and important from every angle to show the relationship between the net profit and total deposit. This ratio is used for measuring the internal ratio indicates the return from deposit. Higher ratio indicates ttturn from investment on loans and advances are better utilized. It is computed by dividing the net profit by total deposit.

**Table No 19**

**Net profit to total deposit ratio (in %)**

	BOKL			HBL		
	Net profit	Total deposit	Ratio	Net profit	Total deposit	Ratio
2005/06	70.72	4196.41	1.68	199.38	14043.10	1.42
2006/07	65.36	5724.13	1.14	277.04	17532.40	1.58
2007/08	9.28	5723.28	0.16	235.02	18619.37	1.26
2008/09	82.13	6170.7	1.33	212.13	21007.38	1.01
2009/10	127.47	7741.64	1.65	263.05	22010.33	1.19
2010/11	139.53	8942.75	1.56	308.28	24814.01	1.24
2011/12	202.44	10485.36	1.93	457.46	26490.85	1.73
Average			1.35			1.347

Sources: Annual reports 2005/06 to 2011/12.

The above table shows, in HBL the ratios are ranged 1.01 percent to 1.73 percent. The average ratio is 1.347 percent. Similarly, in BOKL the ratios are ranged 0.16 percent to 1.93 percent. The average ratio is 135 percent. Both banks have been able to earn near about same, so both bank has been able to earn more profit by utilizing their resources of total deposit.

## 3. Return on net worth (shareholders equity):

It is the ratio of net income to common equity. It measures the rate of return on common stockholder's investment. This is the king amongst ratio. Higher ROE ratios show better operating efficiency of a firm and vice versa.

$$ROE = \frac{\text{Net Income}}{\text{Common Equity}}$$

Following table shows the calculation of return of equity of the HBL and BOKL expressed in percent for the whole period of study.

**Table No 20**  
**Return on Net Worth**

**(Rs million)**

	BOKL			HBL		
	Net profit	Shareholder equity	Ratio	Net profit	Shareholder equity	Ratio
2005/06	70.72	255.49	27.68	199.38	526.05	37.90
2006/07	65.36	327.18	19.98	277.04	720.59	38.45
2007/08	9.28	520.18	1.78	235.02	858.11	27.39
2008/09	82.13	579.13	14.18	212.13	1063.13	19.95
2009/10	127.47	650.74	19.59	263.05	1324.17	19.86
2010/11	139.53	720.74	19.36	308.28	1541.75	20.00
2011/12	202.44	839.73	24.11	457.46	1766.18	25.90
Average			18.10			27.06

Sources: Annual reports 2005/06 to 2011/12.

The above table shows the ratio of return on not worth. The ratios of HBL are ranged 19.86 percent to 38.47 percent and average is 27.06 percent. Where the ratio of BOKL is ranged between 1.78 percent to 27.68 percent and average is 18.10 percent. On the basis of average ratio, HBL has high ratio. So it can be stated that HBL is efficiently utilizing its shareholders fund in generating profit.

#### **4. Return on Loan and Advance Ratio:**

It measures the earning capacity of a commercial banks on its deposits mobilized on loan & advances. Mostly loan & advances includes loan cash credit, overdraft bill purchased and discounted. We have

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

**Table No 21**  
**Return on Loan and Advance Ratio:**

**(Rs million)**

	BOKL			HBL		
	Net profit	Loan & advance	Ratio	Net profit	Loan & advance	Ratio
2005/06	70.72	2939.21	2.41	70.72	6891.27	2.89
2006/07	65.36	4210.88	1.55	65.36	8651.74	3.20
2007/08	9.28	4324.77	0.21	9.28	8653.57	2.72
2008/09	82.13	4494.45	1.83	82.13	9700.66	2.19
2009/10	127.47	5336.97	2.39	127.47	11635.31	2.26
2010/11	139.53	5831.07	2.39	139.53	12010.45	2.27
2011/12	202.44	7239.10	2.80	202.44	14395.85	3.18
Average			1.94			2.67

Sources: Annual reports 2005/06 to 2011/12.

The above table shows the ratio of return on loan and advance ratio of HBL are ranged 2.19 percent to 3.20 percent and average is 2.67 percent. Where the ratios of BOKL are ranged 0.21 percent to 2.80 percent and average is 1.94 percent on the basis of average ratio, HBL has high ratio. So it can be stated that HBL is efficiently utilizing its loan & advance in generation profit.

## **4.2 Statistical Tools**

In this chapter, some statistical tools such as trend analysis of deposit, loan and advances, and net profit are used to achieve the objective of the study.

### **4.2.1 Trend Analysis and Projection for Next Five Years.**

Under this topic, analysis trend of deposit collection, its utilization and net profit of HBL and BOKL are studied. To utilize deposits a commercial bank may grant loan and advances and investment in government securities and share & debentures of other companies. The objective of this topic, trend of deposit loan & advances, total investment and net profit are forecasted for next five years. The projections are based on the following assumptions.

**Assumptions:**

- a) The main assumption is that other thing will remain unchanged.
- b) The forecast will be true only when the limitation of least square method is carried out.
- c) The bank will run in present position.
- d) The economy will remain in the present stage.
- e) Nepal Rastra Bank will not change its guide lines to commercial banks.

**i) Trend Analysis of Total Deposit:**

Under this topic, an effort has been made to calculate the trend values of deposit of HBL and BOKL for seven years from mid July 2005/06 to 2011/12 and forecast of next five years from the mid July 2011/2012 to 2016/2017. The following table no 26 shows the trend value of deposit for twelve years from 2005/06 to 2016/2017 of HBL and BOKL.

**Table No 22**  
**Trend value of Total Deposit of HBL and BOKL**  
**(2005/06 to 2016/17)**

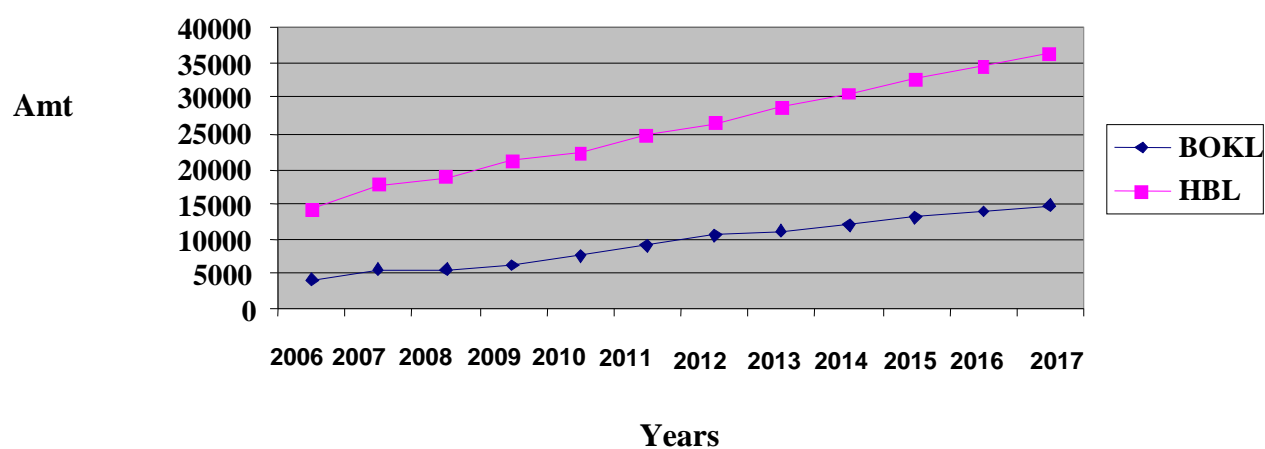
**(Rs million)**

FY	Trend value of BOKL	Trend value of HBL
2006	4196.41	14043.09
2007	5724.13	17532.40
2008	5723.28	18619.37
2009	6170.70	21007.38
2010	7741.64	22010.33
2011	8942.75	24814.01
2012	10485.36	26490.85
2013	10988.95	28544.99
2014	11964.75	30519.90
2015	12940.55	32494.81
2016	13916.35	34469.72
2017	14892.15	36444.63

Sources: Detail in Appendix 3

**Diagram No 17**

**Trend value of total deposit of HBL & BOKL**



The above table shows that the deposits of both banks have the increasing trend. If other thing remains the same the total deposit of the HBL will be Rs 36444.63 million in the fiscal year 2016/2017. Similarly, the deposit of BOKL will be Rs 14892.15 million in the fiscal year 2016/2017. From the above trend analysis, it is found that the deposit collection position of HBL is higher in comparison to BOKL. The calculated trend value of total deposit of HBL and BOKL are fitted in the trend line given.

**ii) Trend Analysis of Loan & Advances:**

Here, the trend value of loan & advances of HBL and BOKL have been calculated for seven years till 2016/2017 has also been done.

The following table no 27 shows that trend value of 12 years from 2005/06.

**Table No 23**

**Trend value of Loan & Advances of HBL & BOKL**

**(2005/06 to 2016/17)**

**(Rs million)**

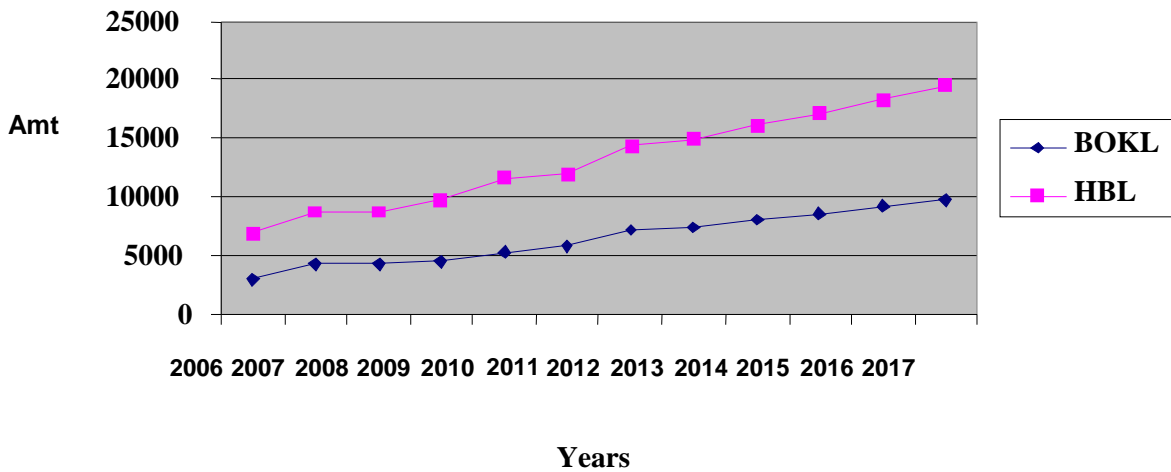
FY	Trend value of BOKL	Trend value of HBL
2006	2939.21	6891.27
2007	4210.88	8651.74
2008	4324.77	8653.57
2009	4494.45	9700.66
2010	5336.97	11635.31

2011	5831.07	12010.45
2012	7239.10	14395.85
2013	7361.24	14878.82
2014	7973.82	16029.28
2015	8586.40	17179.74
2016	9198.98	18330.20
2017	9811.56	19480.66

Sources: In Annex- 4a, 4b

**Diagram No 18**

**Trend value of loan & advances of BOKL & HBL**



The above table shows that the loan & advances of both banks have increasing trend. If other things remaining the same, the total loan & advances of HBL will be highest among the study period. Similarly, the total loan and advance of BOKL will be Rs 9811.56 million in the fiscal year 2016/17. From above trend analysis it is found that the loan and advances position of HBL is higher in compared with BOKL. The calculated trend values of loan and advances of HBL and BOKL are fitted in the trend line.

**iii) Trend Analysis of Net Profit**

Here, the trend value of net profit of HBL and BOKL have been calculated for seven years from 2005/06 to 2011/12. The forecast for next five years till 2016/16 has also been done.

The following table no 28 shows that trend values of 12 years from 2005/06 to 2016/2017.

**Table No 24**

**Trend value of net profit of BOK & HBL.**

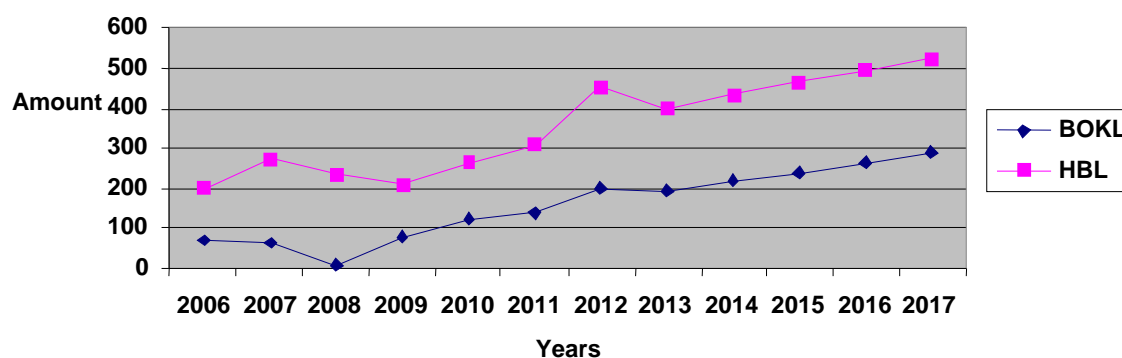
**(Rs million)**

FY	Trend value of BOKL	Trend value of HBL
2006	70.72	199.38
2007	65.36	277.04
2008	9.28	235.02
2009	82.13	212.13
2010	127.47	263.05
2011	139.53	308.23
2012	202.44	457.46
2013	194.08	402.42
2014	217.71	433.3
2015	241.34	464.18
2016	264.97	495.06
2017	288.60	525.94

Sources: In Annex- 5a, 5b)

**Diagram No 19**

**Trend value of net profit HBL & BOKL.**



The above table shows that the net profit of both banks have fluctuating trend. If other thing remains the same the net profit of HBL will be Rs 525.94 million in the fiscal year 2011/12. Similarly the net profit of BOKL will be Rs288.60 million in the FY 2011/12. From the above trend analysis, it is found that the net profit position of HBL is good in comparison to

BOKL. The calculated trend values of net profit of HBL and BOKL are fitted in the trend line given.

### **4.3 Major Finding:**

In the chapter various statistical tools, descriptive analysis method and accounting tools were used to found out the status of profit planning of Himalayan Bank Limited and Bank of Kathmandu Limited. The following findings can be drawn on the basis of the analysis of the profit planning of commercial Banks.

- 1 Major concentration of the analysis on profit planning in commercial banks is at deposit mobilization. In this respect, they are incurring higher cost toward deposit mobilizations. The average growth rate of total deposit of BOKL is more than of HBL i.e.  $17.0725\% > 11.36\%$ .
- 2 Form the data analysis of deposit budget and actual achievement. It is found that the actual deposit is more variable than the budgeted one.
- 3 The mean growth rate of capital fund of BOKL is less than of HBL i.e.  $13.81\% < 14.215\%$ .
- 4 Banks resources deployments for non yielding liquid assets (cash and Bank balance) are fluctuating every year, At the FY 2011/12, both bank growth rates is negative by  $-1.60\%$  and  $-14.75$  of BOKL and HBL respectively.
- 5 Major portion of the resources, have been deployed in LABP of the banks have found to the considerably increasing every year except 2008/2009 for BOKL. Comparatively the BOKL has been decreasing position than HBL.
- 6 Investment of the both banks have found to the considerably increasing every year except 2009/10 & 2011/12 of HBL. Comparatively HBL has been high investment than BOKL.
- 7 The LABP of both banks are fluctuating rate over the study period, but in the FY 2007/08 is negative growth of BOKL by  $-1.54\%$  (on the basis of FY 2007/08). Comparatively BOKL is good position than HBL. From the average growth rate i.e.  $16.08\% > 14.11\%$  respectively.
- 8 In the BOKL, NLABP has found high at first years and negative in second year then after fluctuate. At the last it growth rate is  $22.19$  percent (on the basis of 2011/12). Similarly the HBL, NLABP has found positive in 5 years and negative in two years. At last year it's growth rate is negative by  $-7.79$  percent ( on the basis of 2011/12)
- 9 Expenditure of the both banks are increasing trend but in the FY 2008/09 of BOKL and FY 2007/08 of HBL is decreased. In comparatively more increasing trend in the HBL

than BOKL.

- 10 Interest expenses is the highest portion in the total expenses items of the banks. The interest expenses of the banks are found increasing each year corresponding to the increase in deposit on the both bank. The cost of deposit (calculated as the ratio of total interest expenses during a year on the deposit) of Bank of Kathmandu and second last & last year of HBL is increasing trend.
- 11 Interest income amount of both bank are the highest among other income items in the total revenue. The other income of bank is also in increasing trend.
- 12 Interest income amount of both bank are decreasing up to FY 2007/08 then after fluctuate. At the last year yield on LABP is decreasing. The average yield on LABP of HBL is 11.83 percent and similarly yield on LABP of BOKL is 10.62 percent.
- 13 The interest spread or the amount of interest margin is found to be increasing every year in both the banks. The increasing trend of HBL is high volume than BOKL.
- 14 Net burden of both bank are increasing, except FY 2008/09 of BOKL. Average net burden is 150.12 million of BOKL and 416.12 of HBL. The average rate of growth of other expenses is higher than the other income, it can be expected that it would not hamper much to the profitability if the same trend were continued.
- 15 BOKL, net profit over the study period is decreased in the FY 2007/08. Then after it is going increasing. Then after it is increasing trend. The average net profit Rs 100.30 & 277.62 of BOKL & HBL respectively. It is show HBL is going good performance.
- 16 The average ratios of the HBL & BOKL have found to be lower than standard ratio 2:1, which shows the solvency position of both banks.

## **CHAPTER – FIVE**

### **SUMMARY, CONCLUSION AND RECOMMENDATION**

The last chapter of this study is conclusions and recommendations developed from the comparative analysis of various aspects of the profit planning of two commercial banks i.e. Bank of Kathmandu Limited and Himalayan Bank Limited. After completing the basic analysis required for the study the final and the most important tasks of the researcher is to be summarized the study and recommended for the further importance. This would be meaningful to the top management of the concerned banks to initiate the action and achieve the desired results.

#### **5.1 Summary:**

The prosperity of every developing country can only be ensured by its economic growth. The role of commercial banks in the economic growth of the nation can be fairly estimated to be very prominent, by mobilizing the scattered idle resources from the savers, commercial banks pools the fund in a sizeable volume in order to feed to the fund requirement of productive sector of the economy. Such investments in the productive sector promote trade and industrialization in the country. Thereby raising the employment opportunities ad earning to the labours, materials and service providers to such industries and trades, which as a chain effect promotes saving into the banks and more saving means more funds available in the banks for further investment, in this way, as the chain moves rolling on the economic of the nation also grows.

Therefore, profit for commercial organizations has been defined as the life-blood for them. A commercial Bank also, being a commercial institution, has to plan for the reasonable profit earnings. Profit planning, in short, is the planning of activities in such a way that it helps in increasing the income at a minimum possible cost or at optimum cast. This study aims at examining the applications of profit planning in commercial banks with a specific case study of Bank of Kathmandu and Himalayan Bank Limited comparatively.

To remain as the major contribution factor to the growth of the nation's economy, the banks also have to have sustainable existence and growth of themselves. For the sustainable existence and growth of a bank, it must ensure reasonable profitability. As the Banks are

formed as joint stock companies promoted by shareholder's investment, it must give reasonable return on the fund of the shareholders. Further by the profit made by the bank, it may choose to increase its capital base to make it stronger and more sustainable for facing any future threat that may come up. A profit earning organization can better feed to their employee, thereby enhancing the morale of the employees and motivates them for better performance.

Himalayan Bank Limited is one of the well-run commercial banks in Nepal established in the year 2049/10/05 with joint venture between Nepalese promoters and Habib Bank Limited, one of the largest commercial banks of Pakistan. Similarly, the Bank of Kathmandu is also one of the well-run commercial banks in Nepal established in year 1993 with a joint venture between SIAM commercial bank PCC and Nepalese promoters.

This study has tried to cover the various aspects of Budgeting and profit planning in the bank from the time of its latest seven fiscal years. This study is focused on the profit planning of those two commercial banks. It primarily focused on how commercial banks have planned their profit in order to maximize their return. The general objective of this study is to analyze the profit planning of commercial banks in Nepal.

Data of the respective banks within the last seven years (2005/06 to 2011/12) are only considered. Data relating to various activities of the bank collected presented in tabular and various diagrams from and are tried to be interpreted in the study report in logical way.

The study is based on secondary as well as primary data. So various books, annual reports of the banks, NRB are the secondary sources of data official websites of the concerned companies have also been used for the collection of secondary data. Likewise, primary data have been collected through informal talk with concerned staffs of the banks.

## **5.2 Conclusions:**

The effectiveness of intermediation role played by the banking sector ultimately contributes to the economic development of a country. No doubt, the monetary and regulatory measures adopted by central banks to regulate and supervise the banks and financial institutions determine the extent of banking sector development. The trend thus far has been towards a more open and liberal policies that help the banking sector to grow and flourish. Results

visualized are increased competition, internationalisation of banking business, economic cooperation and innovation in financial instruments. Banking is no longer a national phenomenon. Now the banking business has crossed more risks and challenges to the regulatory framework in the SAARC countries and this call the needs for harmonization for banking policies to manage the banking business in this globalise world.

The following conclusions can be drawn on the basis of the study on profit planning of the commercial banks during the study period.

- 1 The banks have high resources mobilisation in the both banks during the study period. Comparatively the HBL has good growth rate having than BOKL.
- 2 Both banks management policy is very strong. It keep minimum number of Employees & highly qualified for maintain the job.
- 3 Both banks are provides 24 hours services and ATM services for the consumers.
- 4 The budgeted and actual deposits have highly perfect positive correlation in both the banks.
- 5 Customer deposit collection is the main resources mobilization of the banks.
- 6 Loan, allowance and bill purchasing hold the highest outlet of resources deployment.
- 7 Deployment for liquidity of HBL increased in first study year and deceased in next year then after increasing up to second last year. At last year it its decreasing trend. Similarly BOKL is increased in first year and increased in second last & last years, then after it is increasing up to 2008/09.
- 8 LABP of both banks has increasing trend except in FY 2008/09 of BOKL and NLABP of both banks has increasing except in FY 2009/10 & 2011/12 of HBL and FY 2007/08 of BOKL. Average rate of NLABP of BOKL is better than HBL.
- 9 Interest expenses amount is the highest among total expenses items of the bank every year interest expenses of the bank is found increasing each year corresponding to the increase in deposit of BOKL but not HBL. So interest expenses are negative correlation with deposit of HBL.
- 10 Interest income amount of both banks are the highest among other income in the total revenue. The average yield on LABP of both banks is 10.62 percent and 11.83 percent, BOKL and HBL respectively.
- 11 The interest spread of the banks found to be increasing every year.
- 12 Net burden of both banks are increasing in first 3<sup>rd</sup> years and 6<sup>th</sup> years of BOKL & HBL. At the last year it is decreased.
- 13 Net profit of BOKL is decreasing in first three years and then after it is increasing trend.

Similarly HBL is increasing and decreasing up to FY 2008/09 that after it is increasing trend.

- 14 The average current ratio of both banks have found to be always lower than standard ratio of 2:1, which shows dissatisfactory liquidity position of both banks.
- 15 The mean ratio of debt equity of HBL is lower than that of BOKL.
- 16 The average interest coverage ratios of the banks are 1.53 times and 1.74 times of BOKL & HBL respectively.
- 17 Net profit to assets shows the bank's ability to earn a rate of return on the total assets invested. Both the banks have satisfactory return on assets ratio.
- 18 Both banks have high net profit to total deposit ratio and average of 1.85 percent and 1.347 percent of BOKL and HBL.
- 19 The mean ratio of return on loan and advance of HBL is greater than that of BOKL.
- 20 Trend analysis of total deposit and loan & advance of both banks are increasing every year. HBL increasing rate is higher than BOKL.

### **5.3 Recommendations:**

Recommendations are the final output of the whole study. It helps to convey positive information and proper way of improvement to concern banks HBL and BOKL and other interest researcher in upcoming days. Various analyses have been done still these steps. One the basis of analysis and finding of this study following suggestion and recommendation can be advanced to overcome weakness, inefficiency and satisfactory improvement policy of HBL and BOKL.

#### **a. In the internal management and personal part:**

- 1 Mentioned clearly in both banks.
- 2 Banks management should adopt the policy of appropriate authority delegation at all.
- 3 Productive use.
- 4 Employee training at advance level should be given more focus in order to keep manpower updated with the changing practice and the technologies.
- 5 It is suggested to the Banks to form a specific planning and research department, which shall be responsible for developing new innovative products, further development and up gradation of existing products, which in turn ensure better profitable business for the bank.

6 Objectives of both banks should be clearly defined in order to avoid the risk of it being misinterpreted.

**b. In the business part:**

- The deposit collections of both the banks are increasing over the period but the collection of HBL is not satisfactory in comparison with BOKL. So, it is recommended to HBL to collect more amounts as deposit through large variety of deposit scheme and facilities, like cumulative deposit scheme, gift cheques recurring deposit scheme (life insurance), and monthly interest income. The minimum amount needed to open an account should be minimized so that it will attract other small deposits.
- The average cost of deposit of BOKL is high than HBL. Therefore BOKL should try to lower it by mobilizing more and more low cost or lost free deposits thereby reducing the interest cost because due to high cost of deposit, bank is forced to invest its fund more on high yield assets, which are generally not liquid and obviously risky for the bank.
- Correlation between interest expenses and deposit of HBL is negative, it shows there is no relation between interest expenses and deposit but it is not possible. So HBL should increase its cost of deposit rate.
- Expenses cannot be avoided and always are growing with increasing activities, but it should be optimized and should be related with income generating activities. The expense of HBL is higher than BOKL but the growth resource mobilization of BOKL is higher. It can be suggested that, both the bank should minimize these expenses, which are not related to income generating.
- The Nepal Rastra Bank has put the restriction on the difference of average rate of interest income and average rate of interest expenses of the Bank (i.e. spread) not to exceed 5 percent. Therefore the banks have to put more focus on the other kind of non-funded activities by which it shall increase income from other sources than interest to increase its profitability.
- The liquidity positions in terms of current ratio of both banks are below normal standard. So both banks should increase current assets by investing government security not only long term loan.
- Net profit of the HBL is higher than BOKL during the study period. The profit planning is not properly used in FY 2007/08 of BOKL and FY 2008/09 of HBL. So, it can be suggested for both the banks that they should decrease burden to achieve higher net profit.

- Profitability position of HBL in term of net profit to total assets, net profit to shareholder equity and net profit it to loan & advance are better than BOKL. In term of average net profit to total deposit is near about it. Here comparatively, HBL has better profitability position. However, both the banks are not in satisfactory level. So both the banks are required to utilize the resources more efficiently for profit generating sector.
- In banking history, there are many difficulties in recovery loan and advances and their large amount of loan is blocked as non- performing assets and which some time reduce income. So, it is essential to exercise a suitable mechanism through which the overdue loan can be recovered within time. To fulfil this purpose both banks are suggested the special “loan Recovery Act” should be enacted.

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### Appendix - 1

#### BOKL

F.Y.	Deposit (x)	Depositi t (y)	y = y - y	x = x - x	y <sup>2</sup>	x <sup>2</sup>	xy
2005/200 6	4196.41	3560	- 2801.34	- 2784.29	7847505.1	7752270.8	7799742.12
2006/200 7	5724.13	5150	- 1273.62	- 1194.29	1622107.90	1426328.6	1521071.69
2007/200 8	5723.28	5500	- 1274.47	-844.29	1624273.78	712825.6	1076022.28
2008/200 9	8170.70	6000	-827.05	-344.29	684011.70	118535.60	284745.04
2009/201 0	7741.64	6700	743.89	355.71	553372.33	126529.6	264609.11
2010/201 1	8942.75	8000	1945.00	1655.71	3783.25.00	2741375.6	3220355.95
2011/201 2	10485.3 6	9500	3487.61	3155.71	12163423.5 1	9958505.6	11005885.7 5
Total	48,984.2 7	44,410	y X0	x X0	28277719.3 2	22836371. 4	25172432.7 1

$$\text{Arithmetic Mean of } x = \frac{\sum fx}{N} = \frac{44410}{7} = 6344.29$$

$$\text{Arithmetic Mean of } y = \frac{\sum fy}{N} = \frac{48984.27}{7} = 6997.75$$

$$\text{S.D. of } y = \sqrt{\frac{\sum fy^2}{N} - \left(\frac{\sum fy}{N}\right)^2} = \sqrt{\frac{28277719.32}{7} - (6997.75)^2} = 2009.89$$

$$\text{S.D. of } x = \sqrt{\frac{\sum fx^2}{N} - \left(\frac{\sum fx}{N}\right)^2} = \sqrt{\frac{22836371.4}{7} - (6344.29)^2} = 1806.19$$

$$\text{C.V. of } y = \frac{\text{S.D. of } y}{y} = \frac{2009.89}{6997.75} = 0.2872$$

$$\text{C.V. of } x = \frac{\text{S.D. of } x}{x} = \frac{1806.19}{6344.29} = 0.2847$$

$$\begin{aligned} \text{Karl Pearson's Coefficient (r)} &= \frac{N \sum xy}{\sqrt{N \sum x^2} \sqrt{N \sum y^2}} \\ &= \frac{7 \mid 25172432.71}{\sqrt{7 \mid 28277719.32} \mid \sqrt{7 \mid 22836371.4}} \\ &= 0.9906 \end{aligned}$$

$$\begin{aligned} \text{Probable Error (PE)} &= \frac{1 Z r^2}{\sqrt{N}} \mid 0.6745 \\ &= \frac{1 Z \mid 0.9906^2}{\sqrt{7}} \mid 0.6745 \\ &= 0.00477 \end{aligned}$$

### Appendix - 1 (b)

#### Status of Budget and Actual Deposit of HBL

F.Y.	Budget ed Amt (x)	Actual Amt (y)	x = $x - \bar{x}$ (18492.8 6)	y = $y - \bar{y}$ (20,645.3 5)	$x^2$	$y^2$	xy
2005/20 06	13000	14,043.1 0	-5492.86	-6602.25	30171510. 98	43589705. 06	36265234. 94
2006/20 07	15600	17532.4 0	-2892.86	-3112.95	8368638.9 8	9690457.7 0	9005328.5 3
2007/20 08	16800	18619.3 7	-1692.86	-2025.98	2865774.9 8	4104594.9 6	3429700.5 03
2008/20 09	19150	21007.3 8	657.14	362.03	431832.98	131065.72	237904.39 42
2009/20 10	19500	22010.3 3	1007.14	1364.98	1014330.9 8	1863170.4	1374725.9 57
2010/20 11	21500	24,814.0 1	3007.14	4168.66	9042890.9 8	17377726. 2	12535744. 23
2011/20 12	23900	26,490.8 5	5407.14	5845.5	29237162. 98	34169870. 25	31607436. 87

Total	129450	144517.	$\sum x$	$\sum y$	81132142.	11092659	94456075.
		44			86	0.3	43

$$\text{Arithmetic Mean of } x = \frac{\sum fx}{N} = \frac{129450}{7} = 18,492.86$$

$$\text{Arithmetic Mean of } y = \frac{\sum fy}{N} = \frac{144577.44}{7} = 20645.35$$

$$\text{S.D. of } x = \sqrt{\frac{\sum fx^2}{N} - \left(\frac{\sum fx}{N}\right)^2} = \sqrt{\frac{81132142.86}{7} - (18492.86)^2} = 3404.45$$

$$\text{S.D. of } y = \sqrt{\frac{\sum fy^2}{N} - \left(\frac{\sum fy}{N}\right)^2} = \sqrt{\frac{110926590.3}{7} - (20645.35)^2} = 3980.78$$

$$\text{C.V. of } x = \frac{\text{S.D. of } x}{\text{A.M. of } x} = \frac{3404.45}{1806.1} = 0.2847$$

$$\text{C.V. of } y = \frac{\text{S.D. of } y}{\text{A.M. of } y} = \frac{3980.78}{20645.35} = 0.1928$$

$$\begin{aligned} \text{Karl Pearson's Coefficient (r)} &= \frac{\sum xy - \frac{\sum x \sum y}{N}}{\sqrt{\sum x^2 - \frac{(\sum x)^2}{N}} \sqrt{\sum y^2 - \frac{(\sum y)^2}{N}}} \\ &= \frac{7 \mid 94456075.43 - \frac{129450 \times 144577.44}{7}}{\sqrt{7 \mid 81132142.86 - \frac{(129450)^2}{7}} \sqrt{7 \mid 110926590.3 - \frac{(144577.44)^2}{7}}} \\ &= 0.9957 \end{aligned}$$

$$\begin{aligned} \text{Probable Error (PE)} &= 0.6745 \mid \frac{1 \mid Z r^2}{\sqrt{N}} \\ &= 0.6745 \mid \frac{1 \mid Z \mid 0.9957^2}{\sqrt{7}} \\ &= 0.002188 \text{ or } 0.00228 \end{aligned}$$

**Appendix - 2 (a)**

F.Y.	Deposit (x)	Int. Exp (y)	x = $\sum x$ (6997.75 )	y = $\sum y$ (268.72)	$x^2$	$y^2$	xy
2005/2006	4196.41	230.78	-2801.34	-37.94	7847505.1	1439.4 4	106282.8 4
2006/2007	5724.13	287.37	-1273.62	18.65	1622107.90	347.82	-23753.01
2007/2008	5723.28	282.42	-1274.47	13.70	1624273.78	187.69	-17460.24
2008/2009	8170.70	273.77	-827.05	5.05	684011.70	25.50	-4176.60
2009/2010	7741.64	279.56	743.89	10.78	553372.33	116.21	8019.13
2010/2011	8942.75	232.66	1945.00	-36.06	3783.25.00	1300.3 2	-70,136.7
2011/2012	10485.36	294.51	3487.61	25.79	12163423.5 1	665.12	89,945.46
Total	48,984.2 7	1881.0 1	$\sum x$	$\sum y$	28277719.3 2	4082.1	88720.88

$$\text{Arithmetic Mean of } x = \frac{\sum fx}{N} = \frac{48984.27}{7} = 6997.75$$

$$\text{Arithmetic Mean of } y = \frac{\sum fy}{N} = \frac{1881.01}{7} = 268.72$$

$$\text{S.D. of } x = \sqrt{\frac{\sum fx^2}{N} - \left(\frac{\sum fx}{N}\right)^2} = \sqrt{\frac{28277720.02}{7} - (6997.75)^2} = 2009.89$$

$$\text{S.D. of } y = \sqrt{\frac{\sum fy^2}{N} - \left(\frac{\sum fy}{N}\right)^2} = \sqrt{\frac{4082.1}{7} - (268.72)^2} = 24.15$$

$$\text{C.V. of } x = \frac{\text{S.D. of } x}{x} = \frac{2009.89}{6997.75} = 0.2847$$

$$\text{C.V. of } y = \frac{\text{S.D. of } y}{y} = \frac{24.15}{268.72} = 0.08987$$

$$\begin{aligned} \text{Karl Pearson's Coefficient (r)} &= \frac{N \sum xy}{\sqrt{N \sum x^2} \sqrt{N \sum y^2}} \\ &= \frac{7 \mid 88720.88}{\sqrt{7 \mid 28277720.02} \mid \sqrt{7 \mid 4082.1}} \\ &= 0.2611 \end{aligned}$$

$$\begin{aligned} \text{Probable Error (PE)} &= \frac{1 Z r^2}{\sqrt{N}} \mid 0.6745 \\ &= \frac{1 Z \mid 0.2611^2}{\sqrt{7}} \mid 0.6745 \\ &= 0.2376 \end{aligned}$$

### Appendix - 2 (b)

#### Status of Deposit and Interest Eyesores of HBL

F.Y.	Deposit (x)	Interes t Exp. (y)	$x = x - \bar{x}$ (20,645.35 )	$y = y - \bar{y}$ (570.84 )	$x^2$	$y^2$	xy
2005/200 6	14,043.1 0	588.92	-6602.25	18.08	43589705.0 6	326.89	- 119368.6 8
2006/200 7	17532.40	721.80	-3112.95	150.96	9690457.70	22788.9 2	- 469930.9 3
2007/200 8	18619.37	571.64	-2025.98	0.80	4104594.44	0.64	-1620.78
2008/200 9	21007.38	517.99	362.03	-52.85	131065.72	2793.12	- 19133.29
2009/201 0	22010.33	455.87	1364.98	-114.97	1863170.4	13218.1 0	- 156931.7 5
2010/201	24,814.0	525.75	4168.66	-45.09	17377726.2	2033.11	-

1	1						187964.8
							8
2011/201	26,490.8	613.88	5845.5	43.04	34169870.2	1852.44	251590.3
2	5				5		2
Total	144517.4	3995.8	$\sum x$	$\sum y$	110926549.	43013.2	-
	4	5			8	2	703359.9
							9

$$\text{Arithmetic Mean of } x = \frac{\sum fx}{N} = \frac{144517.45}{7} = 20,645.35$$

$$\text{Arithmetic Mean of } y = \frac{\sum fy}{N} = \frac{3995.85}{7} = 570.84$$

$$\text{S.D. of } x = \sqrt{\frac{\sum fx^2}{N} - \left(\frac{\sum fx}{N}\right)^2} = \sqrt{\frac{110926549.8}{7} - (20,645.35)^2} = 3980.78$$

$$\text{S.D. of } y = \sqrt{\frac{\sum fy^2}{N} - \left(\frac{\sum fy}{N}\right)^2} = \sqrt{\frac{43013.22}{7} - (570.84)^2} = 78.39$$

$$\text{C.V. of } x = \frac{\text{S.D. of } x}{\text{A.M. of } x} = \frac{3980.78}{20,645.35} = 0.1928$$

$$\text{C.V. of } y = \frac{\text{S.D. of } y}{\text{A.M. of } y} = \frac{78.39}{570.84} = 0.1373$$

$$\begin{aligned} \text{Karl Pearson's Coefficient (r)} &= \frac{\sum xy}{\sqrt{\sum x^2} \sqrt{\sum y^2}} \\ &= \frac{703359.99}{\sqrt{703359.99} \sqrt{43013.22}} \\ &= -0.3220 \end{aligned}$$

$$\begin{aligned} \text{Probable Error (PE)} &= \frac{1}{\sqrt{N}} |Zr| = 0.6745 \\ &= \frac{1}{\sqrt{7}} |0.3220| = 0.6745 \\ &= 0.2285 \end{aligned}$$

**Annex - 3 (a)**

**Calculation of Trend Analysis of BOKL**

<b>Year (t)</b>	<b>Total Deposit (y)</b>	<b>X = t-2002/03</b>	<b>XY</b>	<b>X<sup>2</sup></b>
2005/2006	4196.41	-3	-12589.23	9
2006/2007	5724.13	-2	-11448.26	4
2007/2008	57230.28	-1	-5728.28	1
2008/2009	6170.70	0	0	0
2009/2010	7741.64	1	7741.64	1
2010/2011	8942.75	2	17885.5	4
2011/2012	10485.36	3	31456.08	9
<b>Total</b>	<b>48984.27</b>	<b>0</b>	<b>27322.45</b>	<b>28</b>

Since.

$$x \text{ X0}$$

$$a = \frac{y}{N} \times \frac{48984.27}{7} \text{ XRs.6997.75}$$

$$b = \frac{xy}{x^2} \times \frac{27322.45}{28} \text{ XRs.975.80}$$

$$Y_c = a + bx$$

$$= 6997.75 + 975.8 \times x$$

**The Value of Trend**

<b>Years</b>	<b>X= t-2002/03</b>	<b>Y<sub>c</sub> = (6997.75 + 975.80×x)</b>
2012/13	4	10,988.95
2013/14	5	11964.75
2014/15	6	12940.55
2015/16	7	13916.35
2016/17	8	14892.15

**Annex - 3 (b)**

**Calculation of Trend Analysis of HBL**

<b>Year (t)</b>	<b>Total Deposit (y)</b>	<b>X = t-2002/03</b>	<b>XY</b>	<b>X<sup>2</sup></b>
2005/2006	14043.09	-3	-42129.27	9
2006/2007	17532.40	-2	-35064.8	4
2007/2008	18619.37	-1	-18619.37	1
2008/2009	21007.38	0	0	0
2009/2010	22010.38	1	22010.33	1
2010/2011	24814.01	2	49628.02	4
2011/2012	26490.85	3	79472.55	9
<b>Total</b>	<b>144517.43</b>	<b>0</b>	<i>xy</i> <b>X55297.46</b>	<b>x<sup>2</sup> = 28</b>

Since.

$$x \sum X_0$$

$$a = \frac{y}{N} \times \frac{144517.43}{7} = 20645.35$$

$$b = \frac{xy}{x^2} \times \frac{55297.46}{28} = 1974.91$$

$$Y_c = a + bx$$

$$= 20645.35 + 1974.91 \times x$$

**The Value of Trend**

<b>Years (t)</b>	<b>X = t-2002/03</b>	<b>Y<sub>c</sub> = (20645.35 + 1974.91 × x)</b>
2012/13	4	28544.99
2013/14	5	30519.9
2014/15	6	32494.81
2015/16	7	34469.72
2016/17	8	36444.63

**Annex - 4 (a)**

**HBL**

<b>Year (T)</b>	<b>Loan &amp; Advance (y)</b>	<b>X = t-2002/03</b>	<b>XY</b>	<b>X<sup>2</sup></b>
2005/2006	6891.27	-3	-20673.81	9
2006/2007	8651.74	-2	-17303.48	4
2007/2008	8653.57	-1	-8653.57	1
2008/2009	9700.66	0	0	0
2009/2010	11635.31	1	11635.31	1
2010/2011	12010.45	2	24020.90	4
2011/2012	14395.85	3	43187.55	9
<b>Total</b>	<b>71938.85</b>	<b>x X0</b>	<b>xy X32212.9</b>	<b>x<sup>2</sup> = 28</b>

Since.

$$x X0$$

$$a = \frac{y}{N} X \frac{71938.85}{7} X10276.98$$

$$b = \frac{xy}{x^2} X \frac{32212.9}{28} X1150.46$$

$$Yc = a+bx$$

$$= 10276.78 + 1150.46 \times x$$

**The Value of Trend**

<b>Years</b>	<b>X= t-2002/03</b>	<b>Yc = (10276.78 + 1150.46 × x)</b>
2012/13	4	14878.82
2013/14	5	16029.28
2014/15	6	17179.74
2015/16	7	18330.20
2016/17	8	19480.66

**Annex - 4 (b)**

**BOKL**

<b>Year (t)</b>	<b>Loan &amp; Advance (y)</b>	<b>X = t- 2002/03</b>	<b>XY</b>	<b>X<sup>2</sup></b>
2005/2006	2939.21	-3	-8817.63	9
2006/2007	4210.88	-2	8421.76	4
2007/2008	4324.77	-1	-4324.77	1
2008/2009	4494.45	0	0	0
2009/2010	5336.97	1	5336.97	1
2010/2011	5831.07	2	11662.14	4
2011/2012	7239.10	3	21717.30	9
<b>Total</b>	<b>y X34376.45</b>	<b>x X 0</b>	<b>xy X17152.25</b>	<b>x<sup>2</sup> = 28</b>

Since.

$$x \text{ X} 0$$

$$a = \frac{y}{N} \text{ X} \frac{34376.45}{7} \text{ X} 4910.92$$

$$b = \frac{xy}{x^2} \text{ X} \frac{17152.25}{28} \text{ X} 612.58$$

$$Y_c = a + bx$$

$$= 4910.92 + 612.58 \times x$$

**The Value of Trend**

<b>Years (t)</b>	<b>X= t-2002/03</b>	<b>Y<sub>c</sub> = (4910.92 + 612.58 × x)</b>
2012/13	4	7381.24
2013/14	5	7973.82
2014/15	6	8586.4
2015/16	7	9198.98
2016/17	8	9811.56

**Annex - 5 (a)**

**HBL**

<b>Year (t)</b>	<b>Net Profit (y)</b>	<b>X = t-2002/03</b>	<b>XY</b>	<b>X<sup>2</sup></b>
2005/2006	199.38	-3	-598.14	9
2006/2007	277.04	-2	-554.08	4
2007/2008	235.02	-1	-235.02	1
2008/2009	212.13	0	0	0
2009/2010	263.05	1	263.05	1
2010/2011	308.23	2	616.46	4
2011/2012	457.46	3	1372.38	9
<b>Total</b>	<b>1952.31</b>	<b>x X0</b>	<b>xy X864.65</b>	<b>x<sup>2</sup> = 28</b>

Since.

$$x \text{ X}0$$

$$a = \frac{y}{N} \text{ X} \frac{1952.31}{7} \text{ X}278.90$$

$$b = \frac{xy}{x^2} \text{ X} \frac{864.65}{28} \text{ X}30.88$$

$$Y_c = a+bx$$

$$= 28278.90 + 30.88 \times x$$

**The Value of Trend**

<b>Years</b>	<b>X= t-2002/03</b>	<b>Yc = (28278.90 + 30.88 × x)</b>
2012/13	4	402.42
2013/14	5	433.3
2014/15	6	646.18
2015/16	7	495.06
2016/17	8	525.94

**Annex - 5 (b)**

**BOKL**

<b>Year (t)</b>	<b>Net Profit (y)</b>	<b>X = t-2002/03</b>	<b>XY</b>	<b>X<sup>2</sup></b>
2005/2006	70.72	-3	-212.16	9
2006/2007	65.36	-2	-130.72	4
2007/2008	9.28	-1	-9.28	1
2008/2009	82.13	0	0	0
2009/2010	127.47	1	127.47	1
2010/2011	139.53	2	279.06	4
2011/2012	202.44	3	607.32	9
<b>Total</b>	<b>y X696.93</b>	<b>x X 0</b>	<b>xy X661.69</b>	<b>x<sup>2</sup> = 28</b>

Since.

$$x \sum X 0$$

$$a = \frac{y}{N} \times \frac{696.93}{7} \times 99.56$$

$$b = \frac{xy}{x^2} \times \frac{661.69}{28} \times 23.63$$

$$Y_c = a + bx$$

$$= 99.56 + 23.63 \times x$$

**The Value of Trend**

<b>Years (t)</b>	<b>X= t-2002/03</b>	<b>Y<sub>c</sub> = (99.56 + 23.63 × x)</b>
2012/13	4	194.08
2013/14	5	217.71
2014/15	6	241.34
2015/16	7	264.97
2016/17	8	288.60