FINANCIAL PERFORMANCE ANALYSIS OF NEPALESE COMMERCIAL BANKS

A Thesis

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Shanker Dev Campus

Submitted to:

Office of the Dean

Faculty of Management

Tribhuvan University

In partial fulfillment of the requirement for the degree of

Master of Business Studies (M.B.S.)

Kathmandu, Nepal

July, 2024

RECOMMENDATION

This is to certify that the thesis

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FINANCIAL PERFORMANCE ANALYSIS OF NEPALESE COMMERCIAL BANKS

has been prepared as approved by this Department in the prescribed format of the Faculty of Management. This thesis is forwarded for examination.

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DECLARATION

I hereby declare that this thesis work entitled "**Financial Performance Analysis of Nepalese Commercial Banks"** submitted to Office of the Dean, Faculty Management, Tribhuvan University, is my original work done in the form in partial fulfillment of the requirement for the degree of Master of Business Studies which is prepared under the supervision of respected supervisor **Rabindra Bhattarai** Lecturer of Shanker Dev Campus.

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ACKNOWLEDGEMENTS

I would like to take this opportunity to express my deepest gratitude to the individuals who have played a significant role in the successful completion of my study. First and foremost, I extend my sincere appreciation to my respected thesis supervisor, **Rabindra Bhattarai,** Lecturer of Shanker Dev Campus. Their valuable suggestions, unwavering support, and encouragement throughout the duration of my research have been invaluable. Their guidance has helped shape the direction and quality of this study.

I am also immensely thankful to **Asso. Prof. Dr. Sajeeb Kumar Shrestha**, Head of the Research Department at Shanker Dev Campus, for their invaluable suggestions, encouragement, and cooperation right from the beginning. Their expertise and support have been instrumental in the successful completion of this endeavor.

Furthermore, I would like to express my heartfelt appreciation to **Asso. Prof. Dr. Krishna Prasad Acharya**, Campus Chief of Shanker Dev Campus, for their direct and indirect support. Their guidance and encouragement have played a significant role in the achievement of this milestone.

I am also indebted to my inspiring and supportive family for their unwavering support in my academic and professional journey. Their constant encouragement and belief in my abilities have been a driving force behind my accomplishments. I would like to acknowledge the valuable contributions of all my colleagues who have been a part of this research work. Their insightful discussions, constructive feedback, and collaborative efforts have greatly enriched the study.

Lastly, I extend my special thanks to all those who have provided me with direct and indirect encouragement and support throughout the course of my research. Your assistance has been invaluable, and I am deeply grateful for your belief in my abilities. I express my deepest gratitude to each and every individual mentioned above, as well as to anyone else who has contributed to my academic and research endeavors. Thank you for being an integral part of my journey and for making this study a success.

Astha Kuinkel

July, 2024

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ABBREVIATIONS

AQ	: Assets Quality
BS	: Bank Size
CAR	: Capital Adequacy Ratio
CV	: Coefficient of Variance
EBL	: Everest Bank Limited
GDP	: Gross Domestic Product
INF	: Inflation
LIQ	: Liquidity Ratio
MBS	: Master in Business Studies
NABIL	: Nabil Bank Limited
NRB	: Nepal Rastra Bank
NSBL	: Nepal SBI Bank Limited
ROA	: Return on Assets
SCB	: Standard Chartered Bank Nepal Limited
SD	: Standard Deviation
SPSS	: Statistical Package for Social Science
TU	: Tribhuvan University

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Understanding commercial banks' stability, profitability, and general health necessitates a thorough examination of their financial performance, which is an essential component of this knowledge. This research often includes an evaluation of important financial measures like return on assets (ROA), return on equity (ROE), net interest margin (NIM), and the capital adequacy ratio (CAR). Return on assets (ROA) evaluates how well a bank uses its assets to create profits, whereas return on equity (ROE) evaluates how profitable the bank is in relation to the equity of its shareholders. A bank uses the net interest margin (NIM) to measure the difference between the interest revenue it earns and the interest it pays out, relative to its interest-earning assets. Berger and Humphrey (1997) state that a bank uses the capital adequacy ratio (CAR) to protect depositors and improve stability and efficiency in financial institutions.

Liquidity is another essential component that contributes to the overall financial success of commercial banks. When determining whether or not a bank is able to fulfill its short-term commitments, liquidity measures, such as the loan-to-deposit ratio (LDR), are helpful in making this determination. An ideal loan-to-deposit ratio (LDR) demonstrates that there is a balance between loans and deposits. This balance ensures that the bank is able to control withdrawals while still producing revenue from loans. Additionally, according to Diamond and Dybvig (1983), liquidity management techniques are essential in averting bank runs and retaining customers' trust in the institution. A bank's ability to meet its financial commitments without suffering losses that are unacceptable is contingent upon the effectiveness of its liquidity management practices.

Commercial banks frequently use cost-to-income ratios, or CIRs, as a measurement tool to assess their effectiveness and operational performance. Calculating this ratio allows one to determine the percentage of revenue that operational expenditures consume. A lower CIR indicates that the bank is more efficient because of its ability to regulate its expenses in relation to the amount of money it generates. According to Brealey et al. (2011), efficient banks can increase their profitability by streamlining their operating

procedures and lowering their expenses through technology. Technological advancements in digital banking and automation have significantly improved the operational efficiency of contemporary commercial banks.

The management of credit risk is another important aspect of financial performance monitoring that should not be overlooked. An important measure of a bank's credit risk is the number of non-performing loans, often known as NPLs. A high level of nonperforming loans (NPLs) poses a risk to the bank's viability. According to Saunders and Cornett (2011), strict lending criteria, continuous monitoring of loan performance, and proactive steps to address overdue loans are all necessary components of effective credit risk management. In general, financial institutions that keep their non-performing loans (NPLs) at a low level are in a better position to achieve sustainable growth and profitability.

Commercial banks evaluate their financial performance through a multi-dimensional process that includes profitability, liquidity, operational efficiency, and credit risk management. The evaluation of these variables provides a complete picture of a bank's financial health as well as its ability to expand in the future. Continuous monitoring and strategic management of these financial measures are vital for the stability and performance of commercial banks in an increasingly competitive and regulated financial environment (Berger et al., 2000). This is because these metrics are necessary to determine the bank's profitability.

The purpose of this study is to conduct an analysis of the financial performance of commercial banks in Nepal, with a particular emphasis on important measures such as return on assets (ROA) and its factors. In light of the fact that these banks play a crucial part in the economic growth of Nepal, the purpose of this research is to evaluate their profitability, liquidity, operational efficiency, and credit risk management along with macroeconomic variables. The purpose of this study is to offer a full knowledge of the strengths and weaknesses that exist within the Nepalese banking industry by evaluating these elements. For the purpose of enhancing financial stability and promoting sustainable development in Nepal's financial system, it is essential for stakeholders, such as policymakers, investors, and bank management, to have access to this research in order to make educated choices.

1.2 Statement of Problems

Finance is a crucial aspect for any business or financial institution as it provides the necessary funds for smooth operations. However, numerous challenges have plagued the financial performance of banks and organizations over the years. Issues such as insolvency, non-performing loans, political uncertainty, scarcity of skilled human resources, natural disasters, and liquidity crises have hindered the efficient functioning of the commercial banking sector. These challenges raised concerns among stakeholders and the government. Fortunately, improvements in government regulation, control of the Nepal Rastra Bank, political stability, and positive changes in the business environment have contributed to the overall enhancement of financial institutions' performance. Assessing a company's financial condition is vital for decision-makers to evaluate the outcomes of corporate plans and operations objectively. Financial performance ratios are commonly used to gauge an organization's financial health and overall performance.

The analysis of financial ratios in commercial banks in Nepal faces challenges due to limited availability of reliable and accurate financial data, lack of standardized reporting practices, absence of comprehensive industry benchmarks and performance metrics, volatile economic and political landscape, and a shortage of skilled professionals with expertise in financial analysis. These factors hinder the accurate assessment of banks' financial performance and make it difficult to compare their performance against industry standards.

Various empirical studies have been conducted on financial performance analysis of commercial banks. Kandel (2019) identified earnings quality as a critical determinant impacting Return on Assets (ROA) and Return on Equity (ROE) in Nepalese commercial banks, with capital adequacy, asset quality, and liquidity playing moderating roles. Similarly, Gautam (2020) found that capital adequacy ratio (CAR) positively influences ROA and ROE in Nepalese financial institutions, while asset quality negatively impacts ROA. Qadri (2020) focused on Bahraini banks and highlighted the positive correlation between profitability metrics like ROA and ROE, and negative correlations with loan-to-asset ratios, emphasizing the importance of balancing profitability and liquidity.

Likewise, Shrestha (2020) investigated Nepalese banks and revealed that managerial efficiency, asset quality, and operational efficiency positively impact financial performance, whereas credit risk exerts a negative influence. Gazi et al. (2021) studied Bangladesh Commerce Bank and noted its weak financial position despite stable growth, underscoring the need for improved financial ratios to enhance competitiveness. Ichsan et al. (2021) analyzed Indonesian Sharia banks during the COVID-19 pandemic, emphasizing the significance of managing Capital Adequacy Ratio (CAR), Operating Costs to Operating Income (BOPO), Financing to Deposit Ratio (FDR), and Non-Performing Financing (NPF) to bolster financial resilience. These findings collectively underline the diverse factors influencing bank performance, from capital adequacy and asset quality to operational efficiency and the management of financial risks.

The study has identified the underlying problem and reasons for the variations in the financial performance of the selected banks. The rapid emergence of numerous banks, finance companies, and cooperatives has introduced new challenges and intensified competition for existing financial institutions. To remain competitive in the market, banks must identify their strengths, weaknesses, and enhance their performance, as their success relies on increasing productivity and financial performance. Consequently, the need to conduct a comprehensive financial performance analysis study arises, considering the aforementioned developments. This study aims to assess the overall financial position and performance of five commercial banks, utilizing financial and statistical tools. An analysis of their financial position is essential to understand the underlying factors influencing performance. Thus, this study seeks to address the following research questions:

- How do the selected commercial banks vary in terms of key financial indicators, such as capital adequacy ratio, asset quality, bank size, liquidity ratio, and return on assets (ROA), during the study period?
- What are the specific relationships between independent variables and the dependent variable in the context of commercial banks in Nepal?
- How do factors like capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation impact the financial performance of commercial banks in Nepal, as measured by the return on assets (ROA)?

1.3 Objectives of the Study

The primary objective of the study is to examine the financial performance of commercial banks. However, the specific objectives of the study are as follows:

- To evaluate the variations in key financial indicators, including the capital adequacy ratio, asset quality, bank size, liquidity ratio, and return on assets (ROA), among the selected commercial banks during the study period.
- To analyze the specific relationships between independent variables (such as capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation) and the dependent variable (ROA) in the context of commercial banks in Nepal.
- To examine the impact of factors like capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation on the financial performance of commercial banks in Nepal, as measured by the return on assets (ROA).

1.4 Significance of the Study

The study on the financial performance of commercial banks in Nepal holds significant importance for various stakeholders. Firstly, it provides valuable insights into the performance of these banks, allowing stakeholders and decision-makers to assess their strengths and weaknesses. By analyzing key financial indicators such as capital adequacy ratio, asset quality, bank size, liquidity ratio, and return on assets (ROA), the study offers a comprehensive understanding of the banks' performance during the study period.

Furthermore, the study aims to identify the specific factors that influence the financial performance of commercial banks in Nepal. By examining the relationships between independent variables (capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation) and the dependent variable (ROA), the study helps in understanding the drivers of bank performance. This knowledge enables banks to focus on areas that require improvement and formulate strategies to enhance their overall performance.

The findings of the study also have policy implications for the banking sector in Nepal. Understanding the impact of factors such as capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation on bank performance allows policymakers to develop appropriate regulations and guidelines. These policies can promote a stable and

resilient banking system, foster healthy competition, encourage efficient resource allocation, and ensure the stability of the financial sector.

Moreover, the study serves as a benchmark for evaluating the financial performance of commercial banks in Nepal. By comparing the performance of selected banks against industry standards, trends, and peer institutions, stakeholders can gain insights into the relative competitiveness and efficiency of these banks. This information guides investment decisions, risk assessments, and strategic planning for various stakeholders, including investors, shareholders, and regulators.

Finally, the study contributes to the existing body of knowledge on financial performance analysis in the context of commercial banks in Nepal. It provides researchers, academicians, and scholars with valuable insights and empirical evidence to further explore and understand the dynamics of the banking sector. This research contribution can help identify areas for future research and contribute to the overall advancement of the banking and finance discipline.

The study on the financial performance of commercial banks in Nepal holds significant importance by providing insights into bank performance, identifying influencing factors, guiding policy formulation, facilitating benchmarking, and contributing to academic research. Its findings can benefit stakeholders in making informed decisions and contribute to the development of a robust and sustainable banking sector in Nepal.

1.5 Limitations of the Study

The study on the financial performance of commercial banks in Nepal, conducted for the partial fulfillment of the requirements for the degree of Masters of Business Studies (M.B.S), has certain limitations, which are as follows:

- The study focuses on a limited sample of five commercial banks in Nepal (HBL, EBL, NABIL, SCB, and NSBI Bank), which may not fully represent the entire banking sector.
- The data covers a period of ten years from fiscal year 2013/14 to 2022/23, potentially missing long-term trends and broader sector dynamics.
- The study relies primarily on descriptive, correlation, and regression analyses, which, while insightful, may not capture all complexities in variable relationships.

- Findings are contingent upon the availability and reliability of data from various sources, which could introduce inaccuracies or gaps in the analysis.

1.5 Organizations of the Study

This research study is organized into different sections. Preliminary, main body and supplementary sections. Preliminary and supplementary sections are arranged before and after the main body sections. Main body have five chapters which are as below:

First chapter is Introduction which provides background of the study, statement of problems, outlines objectives and hypotheses, justifies the study, acknowledges limitations and previews the organization of the study.

Second chapter is Literature Review which reviews relevant theory and empirical research, identifies gaps, and presents a conceptual framework.

Third chapter is Research Methodology which covers details research design, population and sampling design, nature and sources of data collection, methods of data collection and methods of data analysis.

Fourth chapter is Data Presentation and Analysis which presents collected data using appropriate visual aids and analyzes it to address research objectives.

Fifth chapter is Summary and Conclusion which summarizes findings, discusses implications and concludes with reflections and recommendations for future research.

CHAPTER II

REVIEW OF LITERATURE

The chapter extensively reviews existing literature and research related to the current study's focus, aiming to uncover what has already been investigated by various authors and researchers. This comprehensive review encompasses theoretical frameworks, book reviews, analyses of previous studies, critical examinations of articles, and reviews of relevant policy documents. By synthesizing and critiquing this body of knowledge, the chapter seeks to establish a foundation of understanding, identifying gaps and contributions that the current research aims to address. This approach not only contextualizes the current study within existing scholarship but also highlights its novel contributions to the field, thereby enriching and advancing the research landscape.

2.1 Theoretical Review

2.1.1 Financial Performance in Commercial Banks

Financial performance serves as a pivotal measure of a company's achievements over a defined period, encompassing its ability to effectively manage and allocate financial resources. This evaluation typically involves key metrics such as capital adequacy, liquidity, solvency, efficiency, leverage, and profitability (Fatihudin & Mochklas, 2018). These metrics collectively gauge how well a company controls its resources and utilizes them to generate returns. Liquidity decreases as one moves from top-tier assets to lower liquidity items, whereas profitability generally increases, underscoring the differential profitability of investments in fixed assets versus cash holdings (Fabozzi & Drake, 2008).

Financial statements comprising cash flow statements, balance sheets, profit and loss accounts, and changes in capital are fundamental tools that provide detailed insights into a company's financial health (Mashkour, 2020). These statements serve as the foundation for managerial decision-making, offering crucial information for assessing performance trends and making informed strategic decisions. Understanding these statements requires proficiency in both fundamental and technical analyses (Clausen, 2009). This expertise is essential for comprehending the financial behaviors of companies through economic principles, financial management strategies, and accounting practices.

Myer (1969) defines financial statement analysis as the examination of relationships among various financial factors within a business across different reporting periods. This analysis not only helps in identifying trends but also in assessing the strengths and weaknesses of a company's financial position. Such insights are critical for financial managers who rely on these analyses to make informed investment and financing decisions (Fabozzi & Drake, 2008). Evaluating risks and rewards associated with different financial strategies becomes paramount in ensuring sustainable growth and profitability. Moreover, the form of business entity whether it is a sole proprietorship, partnership, corporation, or other significantly influences financial decision-making processes by impacting taxation, governance structures, liability management, and access to funding (Grigos & Stavros, 2006).

Financial analysis serves as a cornerstone for assessing economic characteristics, evaluating company strategies, and forecasting financial performance. It involves scrutinizing current profitability, risks, and the quality of financial statements to effectively plan for future growth and ensure the long-term viability of the business (Fabozzi & Drake, 2008). By leveraging insights derived from thorough financial analysis, companies can navigate uncertainties, optimize resource utilization, and capitalize on opportunities to enhance their competitive position in the market.

2.1.2 Factors of Financial Performance in Commercial Banks

The financial performance of commercial banks is influenced by a variety of internal and external factors. Internal factors include management efficiency, operational costs, asset quality, capital adequacy, and liquidity management. External factors encompass macroeconomic conditions such as GDP growth, inflation rates, regulatory frameworks, and market competition. Effective risk management and adherence to regulatory requirements are crucial in maintaining financial stability. The interplay of these factors determines the profitability and sustainability of banks, affecting their ability to attract investors and provide credit to the economy (Athanasoglou et al., 2008; Sufian & Habibullah, 2009).

2.1.2.1 Capital Adequacy Ratio

The capital adequacy ratio (CAR) is a pivotal metric that measures a bank's capital in relation to its risk-weighted assets. It serves as a safeguard for depositors and ensures that a bank can absorb a reasonable amount of loss before becoming insolvent. CAR is

calculated by dividing a bank's tier 1 and tier 2 capital by its risk-weighted assets. The Basel Committee on Banking Supervision sets international standards for CAR, typically requiring banks to maintain a minimum ratio of 8%. However, higher CARs are often mandated to account for systemic risks or to reflect the financial stability of specific institutions.

A high CAR indicates that a bank has a substantial buffer to cover potential losses, which enhances investor confidence and contributes to overall financial system stability. Conversely, a low CAR may signal potential financial distress and increase the risk of insolvency. Maintaining an adequate CAR is not only a regulatory requirement but also a critical component of a bank's risk management strategy. It requires balancing the need to support business growth through lending with the necessity of holding sufficient capital to mitigate risks (Mili et al., 2017).

2.1.2.2 Assets Quality

Asset quality is a fundamental determinant of a bank's financial health and performance. It reflects the likelihood that the bank's assets, primarily loans, and investments, will generate returns without incurring significant losses. The primary indicator of asset quality is the ratio of non-performing loans (NPLs) to total loans. NPLs are loans on which borrowers are not making interest payments or repaying any principal. A high NPL ratio suggests a high level of credit risk and potential financial instability.

Maintaining high asset quality involves implementing stringent credit risk management practices. This includes thorough credit assessments before loan approval, continuous monitoring of borrowers' financial health, and proactive measures to mitigate potential losses. Diversification of the loan portfolio across different sectors and geographic regions can also reduce the impact of defaults in any one area. Effective management of asset quality is crucial for sustaining profitability and ensuring long-term financial stability (Berger & DeYoung, 1997).

2.1.2.3 Bank Size

The size of a bank, typically measured by its total assets, has significant implications for its financial performance. Large banks often benefit from economies of scale, which allow them to operate more efficiently by spreading fixed costs over a larger volume of transactions. These banks can also diversify their portfolios more effectively, reducing

risk through a broader range of assets and services. Furthermore, larger banks generally have better access to capital markets, enabling them to secure funding at lower costs.

However, the benefits of bank size are accompanied by certain challenges. Large banks are subject to more stringent regulatory oversight due to their potential impact on the financial system. The complexity of managing a large institution can also lead to inefficiencies and increased operational risks. Additionally, in times of financial distress, large banks may be perceived as "too big to fail," which can lead to moral hazard where banks engage in riskier behavior, assuming that they will be bailed out by the government. Thus, while size can confer advantages, it also necessitates robust risk management and regulatory compliance (Goddard et al., 2004).

2.1.2.4 Liquidity Ratio

Liquidity ratios are critical indicators of a bank's ability to meet its short-term and long-term obligations without incurring unacceptable losses. Two key liquidity ratios are the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). The LCR requires banks to hold a sufficient quantity of high-quality liquid assets that can be easily converted into cash to meet liquidity needs for a 30-day stress scenario. The NSFR ensures that banks have stable funding sources to cover their long-term assets.

High liquidity ratios indicate that a bank is well-prepared to handle unexpected withdrawals or financial shocks, which enhances its stability and reduces the risk of insolvency. Conversely, low liquidity ratios can result in funding pressures, forcing banks to sell assets at a loss or seek emergency funding, both of which can be costly and damaging to their financial health. Effective liquidity management involves maintaining a balance between liquidity and profitability, as holding too many liquid assets can reduce a bank's earnings potential (Vento & La Ganga, 2009).

2.1.2.5 Gross Domestic Product

Gross Domestic Product (GDP) growth is a crucial external factor influencing the financial performance of commercial banks. GDP reflects the overall economic activity and health of an economy. During periods of economic growth, businesses expand, consumer confidence increases, and unemployment rates drop. These conditions lead to higher demand for credit, as businesses seek loans for expansion and consumers

finance purchases of homes, cars, and other goods. Consequently, banks benefit from increased lending activities, higher interest income, and lower default rates.

Conversely, during economic downturns, GDP growth slows or contracts, leading to reduced business investments, lower consumer spending, and higher unemployment rates. These adverse conditions can result in a decline in loan demand, increased loan defaults, and deteriorating asset quality, all of which negatively impact banks' financial performance. Therefore, the macroeconomic environment, as captured by GDP growth, plays a vital role in determining the operational dynamics and financial outcomes of commercial banks (Demirgüç-Kunt & Huizinga, 1999).

2.1.2.6 Inflation

Inflation is a macroeconomic factor that significantly impacts the financial performance of commercial banks. Moderate inflation can benefit banks by allowing them to charge higher interest rates on loans, thereby increasing their interest income. In such an environment, banks can improve their profit margins as the interest rates on loans typically rise faster than the rates paid on deposits.

However, high inflation can have detrimental effects. It erodes the real value of money, reducing the purchasing power of consumers and businesses, which can lead to lower savings and investments. For banks, high inflation can increase the cost of funds, reduce the demand for loans, and lead to higher default rates as borrowers struggle to meet higher interest payments. Additionally, inflation can complicate the asset-liability management of banks, as the value of long-term fixed-rate assets may decline while the cost of liabilities increases. Therefore, managing the impacts of inflation is crucial for maintaining the financial health and performance of banks (Boyd et al., 2001).

2.1.3 Market Power Theory

The market power theory founded by Edward Chamberlin (1933) and Joan Robinson (1933), posits that firms with significant market power can influence market prices and achieve higher profitability. In the banking sector, this translates to banks with substantial market shares being able to charge higher interest rates on loans and offer lower rates on deposits, thus enhancing their profit margins. The underlying premise is that less competitive markets allow firms to exploit their dominant positions to secure better financial outcomes.

Berger and Hannan (1989) conducted a seminal study on U.S. banks, demonstrating that banks in more concentrated markets had higher profit margins due to their ability to exercise pricing power. Similarly, a study by Smirlock (1985) found a positive relationship between market concentration and bank profitability, suggesting that market power significantly contributes to financial performance.

Further evidence comes from European studies. Goddard et al. (2004) analyzed banks across multiple European countries and confirmed that market concentration positively impacts bank profitability. Their findings indicate that banks operating in less competitive markets achieve higher returns on assets and equity due to their enhanced ability to set favorable prices. In addition, Shaffer (1985) provided evidence from Canadian banks, showing that higher market power leads to increased profitability, reinforcing the notion that market structure influences financial performance.

In the analysis of financial performance, the market power theory is applied to understand the impact of market concentration on bank profitability. Analysts use metrics such as the Herfindahl-Hirschman Index (HHI) and concentration ratios (e.g., CR4) to measure market concentration. By correlating these metrics with profitability indicators like return on assets (ROA) and return on equity (ROE), researchers can assess the extent to which market power drives financial performance. This approach is crucial for identifying banks that benefit from monopolistic or oligopolistic market structures, helping stakeholders understand competitive dynamics and inform strategic decisions.

2.1.4 Efficiency Structure Hypothesis

The efficiency structure hypothesis is proposed by Demsetz (1973) and further elaborated by Peltzman (1977), suggests that the financial performance of banks is primarily determined by their operational efficiency. According to this theory, more efficient banks can produce and deliver financial services at lower costs, leading to higher profitability. The hypothesis also posits that efficiency leads to market concentration as more efficient banks gain larger market shares, further enhancing their market power and profitability.

Berger (1995) examined U.S. banks and found that both cost efficiency and profit efficiency significantly impact bank performance. His study revealed that banks with

superior management practices and advanced technologies achieve higher efficiency, which translates into better financial outcomes. Similarly, Molyneux and Thornton (1992) analyzed European banks and concluded that differences in profitability are largely attributable to variations in efficiency rather than market power.

Kwan (2003) on Asian banks found that efficiency improvements significantly enhance profitability. The research demonstrated that banks in the region that adopted technological advancements and streamlined their operations achieved substantial gains in financial performance. These findings underscore the importance of efficiency in driving bank profitability across different regions and market conditions.

Efficiency structure hypothesis is utilized to evaluate the impact of operational efficiency on bank profitability. Analysts employ cost-to-income ratios, which compare operating expenses to operating income, to measure efficiency. Lower cost-to-income ratios indicate higher efficiency. Additionally, methodologies such as Data Envelopment Analysis (DEA) and Stochastic Frontier Analysis (SFA) are used to estimate efficiency scores, providing a quantitative basis for comparing the efficiency of different banks. By correlating these efficiency measures with profitability metrics, researchers can identify efficiency-driven performance differentials, guiding strategies for enhancing operational practices and cost management.

2.1.5 Risk-Return Tradeoff Theory

The risk-return tradeoff theory, rooted in the work of Harry Markowitz (1952) and further developed by William Sharpe (1964), emphasizes the relationship between risk and return in financial markets. This theory posits that higher returns are associated with higher levels of risk. In banking, this implies that banks achieving higher profitability often engage in riskier activities, such as extending loans to less creditworthy borrowers or investing in volatile markets.

Empirical evidence strongly supports the risk-return tradeoff theory in the banking sector. Stiroh (2004) analyzed U.S. commercial banks and found that banks with higher returns on equity also exhibited greater earnings volatility, indicating higher risk exposure. His study highlighted the tradeoff between profitability and risk, suggesting that banks that pursue aggressive growth strategies tend to assume higher risks, leading to greater returns but also increased potential for losses.

Acharya et al. (2006) provided additional evidence from European banks, observing a positive relationship between bank profitability and risk-taking. Their study revealed that banks engaging in riskier lending practices or investing in high-yield, high-risk assets achieve higher returns, but also face greater risks of financial distress. This relationship underscores the importance of balancing risk and return to ensure sustainable financial performance. Lepetit et al. (2008) examined the impact of non-interest income on bank risk and profitability. The findings indicated that banks diversifying into non-traditional activities, such as trading and fee-based services, experience higher returns but also increased risk, supporting the risk-return tradeoff hypothesis.

The risk-return tradeoff theory is employed to evaluate the balance between profitability and risk management. Analysts use risk-adjusted performance measures, such as the Sharpe Ratio and the Risk-Adjusted Return on Capital (RAROC), to assess how well banks are compensating for the risks they take. These measures compare the excess return of a bank's portfolio to the level of risk assumed, providing a comprehensive view of performance. Additionally, credit risk indicators like the non-performing loan (NPL) ratio and capital adequacy ratios are analyzed to understand the risk profile of banks. By examining these metrics, researchers can determine whether banks are achieving sustainable profitability through prudent risk management or by assuming excessive risk, which may jeopardize their long-term stability.

2.2 Review of Related Studies

Kandel (2019) analyzed the performance of Nepalese commercial banks using the CAMEL framework, focusing on the average performance of selected samples to determine the key factors influencing their financial performance. Recognizing the pivotal role of the financial sector in Nepal's economy, the study aimed to identify variables within the CAMEL framework capital adequacy, asset quality, management efficiency, earnings quality, and liquidity that affect bank performance. The data analysis revealed that earnings quality is the main factor impacting both Return on Assets (ROA) and Return on Equity (ROE), while capital adequacy, asset quality, and liquidity have a moderating influence. Management efficiency was found to have minimal impact on ROA and ROE. The study concluded that while the selected factors within the CAMEL framework influence bank performance, other management-related

factors may have a more direct effect. The implication is that banks should focus on improving earnings quality and consider other management factors to enhance overall performance.

Gautam (2020) analyzed the financial performance and factors influencing Nepalese financial depositary institutions within the CAMEL framework, utilizing a descriptive cum causal research design. The study drew on secondary data from Nepal Rastra Bank publications, covering all commercial banks, development banks, and finance companies over five years from 2014/15 to 2018/19. Key objectives included assessing variables such as capital adequacy, asset quality, management efficiency, earnings, and liquidity to analyze financial performance. Methodologically, descriptive and pooled regression analyses were employed to explore relationships among these variables. Major findings indicated that financial institutions across categories generally met Nepal Rastra Bank standards for capital adequacy, with finance companies leading in earnings, development banks excelling in asset quality, and commercial banks showing strong management efficiency. Finance companies also maintained higher liquidity compared to other financial institutions. The study highlighted a positive significant impact of Capital Adequacy Ratio (CAR) on Return on Assets (ROA) and Return on Equity (ROE), while asset quality had a negative significant impact on ROA.

Qadri (2020) examined the financial performance of banks in the Kingdom of Bahrain using a case study approach, analyzing secondary data from annual audited reports from 2011 to 2017. The study focused on two key indicators: profitability, measured by return on assets (ROA) and return on equity (ROE), and liquidity, evaluated by loan-to-deposit and loan-to-asset ratios. Employing ratio analysis, percentage analysis, descriptive statistics, and correlation analysis, the findings revealed that ROA and ROE are positively correlated, while they are negatively correlated with the loan-to-asset ratio. The study concludes that profitability and liquidity indicators provide important insights into bank performance, suggesting that banks should balance profitability and liquidity to meet the needs of both shareholders and depositors effectively.

Shrestha (2020) investigated the influence of bank-specific factors on the financial performance of Nepalese commercial banks, using Return on Assets (ROA) as the performance measure and Managerial Efficiency (ME), Liquidity (LIQ), Credit Risk (CR), Asset Quality (AQ), and Operational Efficiency (OE) as proxies for bank-specific

factors. The study analyzed panel data from 17 commercial banks over the period 2010/11 to 2017/18. Methodologically, the Breusch and Pagan Lagrangian multiplier test indicated the inappropriateness of the Pooled Regression model, leading to the adoption of the Fixed Effect model as determined by the Hausman test. Major findings revealed that ME, AQ, and OE positively impact financial performance, while CR negatively affects it, indicating that effective management, high-quality assets, and operational efficiency enhance financial performance, whereas credit risk hampers it. The study concludes that bank-specific factors significantly impact the financial performance of Nepalese commercial banks. The implication is that improving managerial efficiency, asset quality, and operational efficiency can enhance bank profitability, while managing credit risk is crucial to avoid negative impacts.

Gazi et al. (2021) analyzed the financial performance of Bangladesh Commerce Bank Limited, a converted commercial bank from a non-banking financial institution, over the period 2015–2019. The study aimed to assess the bank's growth and financial health through various indicators such as total deposits, total loans and advances, and net income after tax. Using a case study approach, the researchers found that while the bank achieved stable growth in key financial metrics, its overall financial position was considered weak as indicated by below-standard metrics including return on assets (ROA), return on equity (ROE), and net interest margin (NIM). Methodologically, the study utilized secondary data analyzed through descriptive statistical tools and a panel data regression model to examine relationships and test hypotheses related to financial performance and asset management efficiency. The findings highlighted the bank's satisfactory operating efficiency and asset management practices, despite its weaker financial ratios. The study concluded that Bangladesh Commerce Bank Limited needs to focus on improving its financial ratios to strengthen its overall performance and competitiveness in the banking sector. The implication is that enhancing ROA, ROE, and NIM could bolster the bank's financial health and sustainability.

Ichsan et al. (2021) examined the financial performance of Islamic Banks during the Covid-19 pandemic, using annual financial statements from 2011 to 2020 and employing multiple linear regression and Ramsey tests for linearity testing. The objective was to understand how the capital adequacy ratio (CAR), operating costs to operating income (BOPO), Financing to deposit ratio (FDR), and not performing

financing (NPF) influenced financial performance, measured by Return on Assets (ROA). The findings revealed that CAR, BOPO, and FDR positively and significantly affect financial performance, while NPF has a negative and insignificant effect. The study concludes that these factors collectively have a significant influence on the financial performance of Sharia banks in Indonesia, suggesting that effective management of CAR, BOPO, FDR, and NPF can enhance the financial resilience of Islamic banks during crises. The implication is that focusing on these financial ratios can help Islamic banks maintain stability and performance during economic disruptions.

Mishra et al. (2021) assessed the impact of bank size, loans and deposits, inflation, and capital on the profitability of Nepalese banks using secondary data from 2013 to 2019 from seven commercial banks and survey data as primary data. The study utilized correlation and regression analysis, along with ratio analysis, to explore relationships between return on assets (ROA), return on equity (ROE), and net interest margin (NIM). The findings revealed that bank size showed an increasing trend with lower variation in total assets usage over time, and that there is a negative relationship between ROA and ROE with loan ratio, deposit ratio, and capital ratio, while a positive relationship exists with bank size and inflation. For NIM, bank size, loan ratio, deposit ratio, and inflation exhibited a positive relationship, whereas the capital ratio showed a negative relationship. Additionally, the majority of respondents considered the publication of financial reports as a significant factor influencing bank profitability. The study concludes that increasing bank size and transparency in financial reporting can enhance the profitability of Nepalese commercial banks.

Trung (2021) identified the determinants of Vietnamese commercial banks' performance from 2009 to 2020 using the CAMELS model and the System Generalized Method of Moments (SGMM) for quantitative regression analysis. The study aimed to evaluate and measure bank performance by examining ten statistically significant factors, encompassing all components of the CAMELS model: capital adequacy, asset quality, management, earnings, liquidity, sensitivity, ownership, GDP, and inflation. The findings revealed that variables such as capital adequacy ratio, management, earnings, liquidity, and macroeconomic factors positively affect bank performance, while asset quality and sensitivity negatively impact it. The study concludes that

focusing on improving capital adequacy, management, earnings, and liquidity can enhance the performance of Vietnamese commercial banks, implying that banks should prioritize these areas for better financial outcomes.

Ali et al. (2022) applied robust regression analysis to investigate the determinants of bank performance in the Indian banking sector, focusing on the relationship between return on assets (ROA) and net interest margin (NIM). The study aimed to assess how factors such as bank size, nonperforming assets (NPA), capital adequacy, liquidity (measured by LATA), labour productivity (PPE), income diversification (NONIITI), and financial crises influence bank performance. Methodologically, robust regression techniques were used to analyze secondary data over the study period. The findings indicated that bank size did not significantly impact public-sector bank performance, while higher levels of nonperforming assets negatively affected performance. Conversely, higher bank capital was associated with increased profitability. Liquidity measures showed an inverse relationship with bank performance, suggesting that banks earned more by lending more and maintaining lower liquid assets. Labour productivity and income diversification were positively related to bank performance, though income diversification had a negative impact on net interest margins for public-sector banks.

Lyimo (2023) analyzed the determinants of financial performance in commercial banks in Tanzania, focusing on both external and internal bank-specific factors using a sample of 18 selected commercial banks over nine years (2012-2020) and employing the generalized method of moments (GMM) model for estimation. The study found that bank size and asset quality positively impact financial performance, while the activity mix negatively affects it. An insignificant negative association was found between ownership, liquidity management, market share, and financial performance. Additionally, external factors such as GDP and inflation were identified as having a significant negative impact on the financial performance of commercial banks. The study concludes that bank management and shareholders should incorporate these findings into their operations to enhance financial performance, implying that focusing on improving bank size, asset quality, and mitigating the effects of GDP and inflation can boost bank profitability.

Njoki (2023) explored the determinants of financial performance in Kenya's commercial banks, using Return on Assets (ROA) as the dependent variable and

considering bank size, managerial effectiveness, asset quality, liquidity, and capital adequacy as independent variables. The study employed a descriptive research approach and a multiple linear regression model, analyzing secondary data from audited annual financial statements. The findings revealed that the predictor variables accounted for 40.6% of the changes in financial performance, with the remaining 59.4% attributable to other internal factors not considered in the study. Specifically, asset quality and size positively impacted ROA, while capital adequacy, liquidity, and managerial effectiveness had negative effects. The study concluded that the Central Bank of Kenya should adopt flexible policies to align with economic and market conditions, particularly in determining minimum capital adequacy and liquidity ratios, implying that such policy adjustments could enhance the financial performance of commercial banks.

Duong et al. (2024) explored the factors influencing the financial performance of banks in Vietnam amid ongoing digital transformation. Using SMARTPLS 4 software, the study employed a mixed-methods approach, gathering data from 400 bank employees across Vietnam. The research aimed to identify key factors impacting bank financial performance, focusing on deposit mobilization, bank profitability, and customer loyalty as primary variables. The findings highlighted strong correlations between these variables and secondary factors such as savings interest rates, bank technology, and inflation. Effective deposit mobilization and customer loyalty were identified as critical for achieving financial goals and enhancing profitability. The study concluded that banks can improve their financial performance by strategically managing these factors and investing in advanced bank technologies.

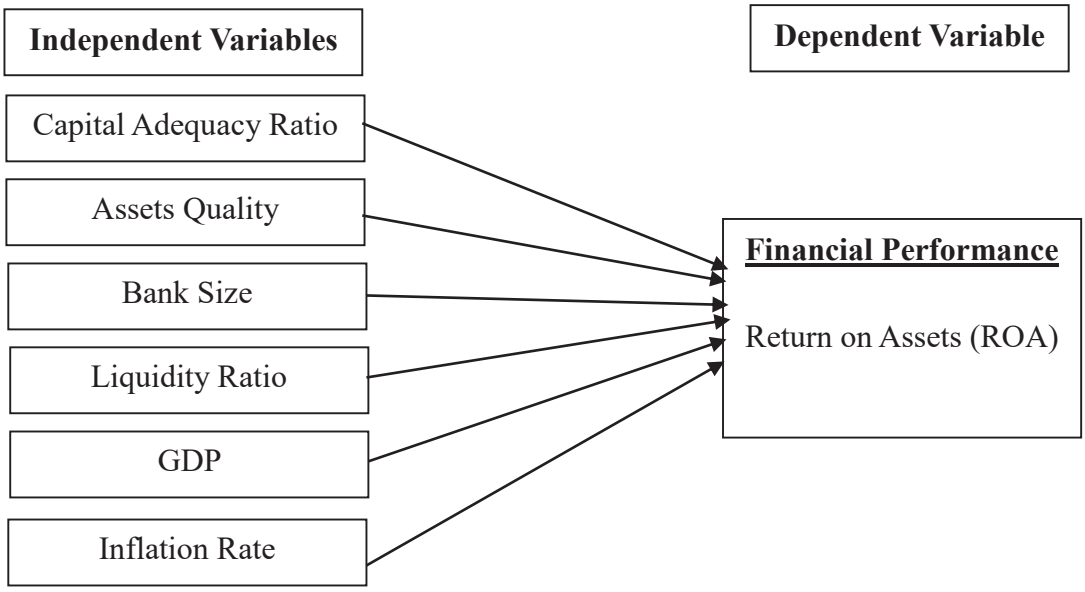
Syarifudin and Suwandi (2024) examined the factors influencing the financial performance and stock value of Sharia and conventional commercial banks in Indonesia, focusing on the economic impact of the COVID-19 pandemic. The study utilized Multiple Linear Regression with SPSS and Structural Equation Modeling (SEM), complemented by the Mann Whitney Test for difference testing. The research aimed to identify disparities in factors affecting profitability and stock value between Sharia and conventional banks. Key findings indicated that factors such as Capital Adequacy Ratio (CAR), Financing to Deposit Ratio (FDR), Cost to Operating Income (BOPO), and Non-Performing Loans (NPL) had varying impacts on Return on Assets

(ROA) and stock value across bank types. Specifically, CAR positively influenced the stock value of Islamic banks but not conventional banks, while BOPO and NPL negatively affected ROA differently between the two types. The study concluded that effective management strategies should focus on controlling BOPO and NPL and enhancing CAR to optimize profitability and share value, providing actionable insights for banking strategies amidst economic uncertainties.

2.3 Conceptual Framework

The conceptual framework for the study on financial performance and its determinants of commercial banks in Nepal aims to examine the correlation between several independent variables and one dependent variable return on assets (ROA). The independent variables considered in this study are capital adequacy ratio, assets quality, bank size, liquidity ratio, GDP, and inflation. These variables have been selected based on empirical studies conducted by Shrestha (2020), Ichsan et al. (2021), Lyimo (2023), and Njoki (2023), which have provided insights into the relationship between these variables and financial performance in the banking sector. The conceptual framework is illustrated in Figure 2.1, which depicts the interrelationships between the independent variables and the dependent variables.

Figure 2. 1 Conceptual Framework



Source: Shrestha (2020); Ichsan et al. (2021); Lyimo (2023); Njoki (2023)

2.3 Research Gap

In the context of Nepal's banking sector, recent studies have explored various aspects of financial performance using traditional financial metrics and econometric tools. However, there remains a research gap in the comprehensive integration of recent data and regression techniques to understand the nuanced factors affecting bank profitability. Existing research often relies on descriptive analyses and basic correlation studies, overlooking the potential insights that more sophisticated regression models could provide. Moreover, there is a need for updated studies that incorporate the latest economic indicators and financial data, reflecting the evolving dynamics of Nepal's economy and banking sector. Addressing these gaps would not only enhance the precision of predictive models but also offer more robust insights into the determinants of financial performance among Nepalese commercial banks.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Research Design

This study combining descriptive and causal research designs. The descriptive aspect focuses on analyzing variations in key financial indicators across selected commercial banks in Nepal. It aims to provide a comprehensive overview of financial performance trends over a ten-year period. The causal component seeks to establish relationships between independent variables (such as capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation) and the dependent variable (ROA). This design allows for both an exploration of patterns and a deeper understanding of causal relationships influencing financial performance.

3.2 Population and Sample

The study's population consists of all A-class commercial banks operating in Nepal as of January 2024, totaling 20 commercial banks. From this population, a purposive sampling method is employed to select a representative sample of five banks. The selected banks include Himalayan Bank Ltd. (HBL), Everest Bank Ltd. (EBL), Nabil Bank Ltd. (NABIL), Standard Chartered Bank Nepal Ltd. (SCB), and Nepal SBI Bank Ltd. (NSBL). These banks are chosen based on their prominence in the Nepalese banking sector and availability of comprehensive data.

3.3 Nature and Sources of Data

Data for this study are primarily sourced from secondary sources, including official annual reports published sample commercial banks and macroeconomic variables data are collected from official reports published by the Nepal Rastra Bank (NRB). These sources ensure the reliability and comprehensiveness of the data used for analysis.

3.4 Data Collection Procedures

The data collection process involves systematic extraction and compilation of financial and macroeconomic data from the NRB's reports and individual bank annual reports. Key financial indicators of interest include Return on Assets (ROA), Capital Adequacy Ratio (CAR), Asset Quality, Bank Size (measured using the Natural Log of Total Assets), and Liquidity Ratio. Additionally, macroeconomic variables such as GDP and

are included to contextualize the analysis. Data cover a ten-year period from fiscal year 2013/14 to 2022/23, allowing for longitudinal analysis and trend identification.

3.5 Data Analysis Tools

Different financial ratios and statistical tools are analyzed to meet the objectives of the study. SPSS 25.0 software was used to analyze the data. The main tools used in this study are:

3.5.1 Financial Tools

The analysis of financial performance metrics such as return on assets (ROA), capital adequacy ratio (CAR), asset quality, bank size (measured using the Natural Log of Total Assets), and liquidity ratio forms a cornerstone of this study. These indicators are calculated using data extracted from the annual reports of the selected commercial banks and the Nepal Rastra Bank (NRB) reports. SPSS 25.0 software is employed for computing these metrics and conducting descriptive statistical analyses to understand the variability and trends over the study period from fiscal year 2012/13 to 2021/22.

3.5.1 Macroeconomic Tools

Incorporating macroeconomic variables is crucial to contextualizing the financial performance of commercial banks. GDP growth rate and inflation rates are sourced from national economic reports and are analyzed using SPSS 25.0. These variables serve to gauge the external economic conditions and their potential impact on the financial health of banks. Correlation analysis and regression models in SPSS 25.0 are utilized to examine the relationships between these macroeconomic factors and the financial performance indicators, providing insights into their influence over time.

3.5.2 Statistical Tools

A robust statistical framework is employed to uncover patterns and relationships within the dataset. SPSS 25.0 facilitates the calculation of descriptive statistics such as mean, standard deviation, and coefficient of variation for each financial and macroeconomic variable. Furthermore, correlation coefficients are computed to assess the strength and direction of relationships between variables. Regression analysis, using multiple regression models in SPSS 25.0, allows for the identification of significant predictors of ROA, quantifying the effects of independent variables on bank profitability. This analytical approach supports a comprehensive understanding of the factors driving

financial performance among Nepalese commercial banks, enhancing the study's empirical rigor and practical implications. The regression model of the study is presented as below:

$$ROA = \beta 0 + \beta 1(Capital\ Adequacy\ Ratio) + \beta 2(Assets\ Quality) + \beta 3(Bank\ Size) + \beta 4(Liquidity\ Ratio) + \beta 5(GDP) + \beta 6(inflation) + \varepsilon$$

Where,

ROA represent the dependent variables, which are return on assets.

Capital Adequacy Ratio, Assets Quality, Bank Size, Liquidity Ratio, GDP and inflation represent independent variables for the study.

β0 represents the intercept,

β1 to β6 represent the coefficients associated with each independent variable.

ε represents the error term, accounting for unexplained variation in the dependent variables

CHAPTER IV

DATA PRESENTATION AND ANALYSIS

In the data presentation and analysis chapter, this study presents and scrutinizes a decade-long dataset encompassing key financial and macroeconomic indicators of twenty prominent commercial banks in Nepal. Leveraging SPSS 25.0 software, the chapter unfolds with a detailed exposition of descriptive statistics and variability in metrics on study variables. These analyses are complemented by an exploration of macroeconomic factors GDP growth and inflation rates providing a holistic view of the economic backdrop influencing bank performance. Correlation analyses elucidate interrelationships among variables, while regression models offer insights into the predictors of ROA. The chapter's comprehensive approach not only highlights methodological rigor but also enhances understanding of the factors underpinning the financial dynamics of Nepalese commercial banks.

4.1 Financial Analysis of Study Variables

This section delves into a examination of key financial metrics and macroeconomic indicators that underpin the performance of commercial banks in Nepal. This segment scrutinizes variables such as return on assets (ROA), capital adequacy ratio (CAR), asset quality, bank size (measured by the Natural Log of Total Assets), and liquidity ratio. By applying statistical tools and methods like mean, standard deviation, coefficient of variance, correlation coefficients, and regression analysis, this analysis provides a nuanced understanding of how these variables interact and influence the financial stability and profitability of the banks over a decade-long period. The findings from this section contribute essential insights into the financial health and resilience of Nepal's commercial banking sector.

4.1.1 Return on Assets

Return on assets (ROA) is a fundamental metric used to assess the profitability and efficiency of commercial banks in Nepal. It measures the ability of banks to generate earnings from their total assets. This section presents an in-depth analysis of the return on assets of five commercial banks during the ten years of the study period. Table 4.1 provides a detailed overview of ROA trends across these banks, offering insights into variations over time and highlighting performance benchmarks. Understanding these

trends is crucial for evaluating the operational efficiency and financial health of Nepalese banks, guiding strategic decisions to enhance profitability and resource utilization.

Table 4. 1 *Return on Assets*

FY	HBL	EBL	NABIL	SCB	NSBL
2013/14	1.30	2.24	3.03	2.51	1.19
2014/15	1.34	2.20	2.66	1.99	1.51
2015/16	1.94	1.59	1.81	1.98	1.80
2016/17	2.03	1.52	2.21	1.84	1.70
2017/18	1.67	1.72	2.59	2.61	1.53
2018/19	2.21	1.78	2.47	2.61	1.97
2019/20	1.79	1.80	2.11	1.71	1.94
2020/21	1.68	1.36	1.46	1.22	1.17
2021/22	1.09	0.89	1.71	1.83	0.70
2022/23	0.47	1.13	1.20	2.29	1.07
Mean ($\bar{X}$)	1.55	1.62	2.13	2.06	1.46
S.D. (σ)	0.49	0.4	0.55	0.42	0.39
C.V.	31.51	24.95	25.85	20.61	27.07

Source: Annual Reports of HBL, EBL, NABIL, SCB and NSBL (2013/14 to 2022/23)

Table 4.1 shows the return on assets (ROA) for five major Nepalese banks Himalayan Bank Limited (HBL), Everest Bank Limited (EBL), Nabil Bank Limited (NABIL), Standard Chartered Bank Nepal Limited (SCB), and Nepal SBI Bank Limited (NSBL) over a ten-year period from fiscal year 2013/14 to 2022/23. Himalayan Bank Limited (HBL) exhibited considerable fluctuation in its ROA, with a peak of 2.21% in 2018/19 and a low of 0.47% in 2022/23, resulting in a mean ROA of 1.55% and the highest C.V. of 31.51%. This high coefficient of variation indicates significant variability in HBL's profitability. In contrast, Everest Bank Limited (EBL) maintained a relatively stable ROA, ranging from 2.24% in 2013/14 to 0.89% in 2021/22, with a mean ROA of 1.62% and a moderate C.V. of 24.95%.

Nabil Bank Limited (NABIL) demonstrated the strongest average profitability among the banks, with a mean ROA of 2.13%. Despite its highest ROA of 3.03% in 2013/14 and lowest at 1.20% in 2022/23, NABIL's C.V. of 25.85% indicates moderate variability. Standard Chartered Bank Nepal Limited (SCB) showed a high and stable ROA, peaking at 2.61% in both 2017/18 and 2018/19 and bottoming out at 1.22% in

2020/21. SCB's mean ROA was 2.06%, and with a C.V. of 20.61%, it had the most consistent performance among the five banks.

Nepal SBI Bank Limited (NSBL) had the lowest mean ROA of 1.46% and exhibited significant fluctuation, with a high of 1.97% in 2018/19 and a low of 0.70% in 2021/22. Its C.V. of 27.07% indicates considerable variability in profitability. Overall, while NABIL showed the highest average profitability, SCB had the most consistent performance. In contrast, HBL and NSBL demonstrated greater variability in their ROA, indicating fluctuating profitability.

4.1.2 Capital Adequacy Ratio

The capital adequacy ratio (CAR) is a critical indicator of a bank's financial strength and resilience against risks. It measures the adequacy of a bank's capital relative to its risk-weighted assets. This section includes an extensive analysis of the Capital Adequacy Ratio of selected Nepalese banks over the study period. Table 4.2 presents CAR metrics, evaluating compliance with regulatory requirements and assessing trends in capital adequacy. This analysis helps stakeholders gauge the stability and risk management capabilities of Nepalese banks, informing decisions aimed at maintaining depositor confidence and sustainable growth.

Table 4. 2 *Capital Adequacy Ratio*

FY	HBL	EBL	NABIL	SCB	NSBL
2013/14	12.15	11.31	11.24	12.27	13.28
2014/15	10.84	13.33	11.57	13.1	14.03
2015/16	11.14	12.66	11.73	16.38	13.49
2016/17	11.23	14.69	12.42	21.08	15.71
2017/18	12.46	14.2	13	22.99	15.15
2018/19	12.6	13.74	13.07	19.69	14.12
2019/20	14.89	13.38	12.5	18.51	15.55
2020/21	13.89	12.48	12.77	17.17	13.86
2021/22	11.75	11.89	13.09	15.95	13.25
2022/23	12.31	13.3	12.54	17.09	12.58
Mean ($\bar{X}$)	12.33	13.10	12.39	17.42	14.10
S.D. (σ)	1.20	0.98	0.63	3.15	1.00
C.V.	9.70%	7.47%	5.06%	18.09%	7.07%

Source: Annual Reports of HBL, EBL, NABIL, SCB and NSBL (2013/14 to 2022/23)

Table 4.2 depicts the capital adequacy ratio (CAR) for five Nepalese banks Himalayan Bank Limited (HBL), Everest Bank Limited (EBL), Nabil Bank Limited (NABIL),

Standard Chartered Bank Nepal Limited (SCB), and Nepal SBI Bank Limited (NSBL). Himalayan bank limited (HBL) maintained a relatively stable CAR, with values ranging from 10.84% in 2014/15 to 14.89% in 2019/20. The mean CAR for HBL was 12.33%, with a standard deviation of 1.20 and a coefficient of variation of 9.70%, indicating moderate consistency in capital adequacy. In comparison, Everest bank limited (EBL) showed slightly more variation, with CAR values between 11.31% in 2013/14 and 14.69% in 2016/17. EBL's mean CAR was 13.10%, with a standard deviation of 0.98 and a C.V. of 7.47%, suggesting higher stability in maintaining capital adequacy.

Nabil bank limited (NABIL) exhibited the highest consistency in CAR, with a mean of 12.39%, a standard deviation of 0.63, and the lowest C.V. of 5.06%. This indicates a very stable capital adequacy performance over the years, with CAR values ranging from 11.24% in 2013/14 to 13.09% in 2021/22. Standard chartered bank Nepal limited (SCB) had the highest mean CAR of 17.42%, indicating strong capital adequacy. However, SCB also showed the highest variability with a standard deviation of 3.15 and a C.V. of 18.09%, with CAR values fluctuating from 12.27% in 2013/14 to a peak of 22.99% in 2017/18.

Nepal SBI bank limited (NSBL) displayed consistent capital adequacy, with a mean CAR of 14.10%, a standard deviation of 1.00, and a C.V. of 7.07%. NSBL’s CAR values ranged from 12.58% in 2022/23 to 15.71% in 2016/17, reflecting a stable capital position. While SCB’s high mean CAR indicates strong financial resilience, its variability suggests potential fluctuations in capital strength, which could impact performance stability. NABIL’s consistent CAR likely supports stable performance, whereas EBL and NSBL demonstrate reliable capital adequacy, positively influencing their performance. HBL shows moderate stability in capital adequacy, contributing to its overall financial health and performance.

4.1.3 Assets Quality

Asset quality is a key determinant of a bank's credit risk and overall financial health. This section examines the quality of assets held by Nepalese banks, focusing on metrics such as non-performing loans (NPL) and provisions for loan losses. Table 4.3 provides a comprehensive overview of Asset Quality indicators for major commercial banks in Nepal, analyzing trends in NPL ratios and the effectiveness of loan loss provisions. Understanding these metrics is essential for identifying challenges in asset management

and implementing robust strategies to mitigate credit risks, thereby ensuring sound financial performance and long-term profitability.

Table 4. 3 *Assets Quality (NPL Ratio)*

FY	HBL	EBL	NABIL	SCB	NSBL
2013/14	1.96	0.97	2.3	0.48	0.26
2014/15	3.22	0.67	1.86	0.34	0.19
2015/16	1.23	0.39	1.17	0.32	0.14
2016/17	0.85	0.26	0.81	0.19	0.1
2017/18	1.4	0.2	0.55	0.18	0.2
2018/19	1.12	0.16	0.74	0.15	0.2
2019/20	1.01	0.22	0.98	0.44	0.23
2020/21	0.48	0.12	0.84	0.96	0.23
2021/22	1.59	0.12	1.62	0.59	0.15
2022/23	4.93	0.79	3.39	1.18	2.43
Mean ($\bar{X}$)	1.78	0.39	1.43	0.48	0.41
S.D. (σ)	1.27	0.29	0.84	0.33	0.67
C.V.	71.31%	74.99%	58.97%	67.48%	163.16%

Source: Annual Reports of HBL, EBL, NABIL, SCB and NSBL (2013/14 to 2022/23)

Table 4.3 shows the non-performing loan (NPL) ratios for five banks over a ten-year period from fiscal year. The NPL ratio for HBL shows significant fluctuation, peaking at 4.93% in 2022/23 and reaching a low of 0.48% in 2020/21. The mean NPL ratio is 1.78%, with a standard deviation of 1.27, resulting in a high coefficient of variation (C.V.) of 71.31%. This high variability indicates considerable inconsistency in asset quality, which can negatively impact the bank's performance by increasing credit risk and potential loan losses. EBL consistently maintained a low NPL ratio, with a mean of 0.39% and values ranging from 0.97% in 2013/14 to 0.12% in both 2020/21 and 2021/22. The standard deviation is 0.29, and the C.V. is 74.99%, suggesting some variability but overall strong asset quality.

NABIL exhibits a mean NPL ratio of 1.43%, with the highest value of 3.39% in 2022/23 and the lowest value of 0.55% in 2017/18. The standard deviation is 0.84, and the C.V. is 58.97%, indicating relatively stable asset quality compared to HBL and EBL. NABIL's moderate and stable NPL ratio supports its performance by minimizing the risk of loan defaults. SCB maintained a low and relatively stable NPL ratio, with a mean of 0.48%, a standard deviation of 0.33, and a C.V. of 67.48%. The NPL ratio fluctuated between 1.18% in 2022/23 and 0.15% in 2018/19. This stability in asset quality

positively influences SCB's performance by ensuring lower credit risk and fewer non-performing loans.

NSBL's NPL ratio demonstrates significant variability, with a mean of 0.41%, a standard deviation of 0.67, and the highest C.V. of 163.16%. The NPL ratio ranges from 2.43% in 2022/23 to 0.10% in 2016/17. The high variability in NSBL's asset quality indicates higher risk, potentially affecting its financial performance negatively due to the increased likelihood of loan defaults. SCB, NSBL and EBL exhibit the best asset quality with low mean NPL ratios, though EBL shows higher variability. NABIL demonstrates stable asset quality with a moderate mean NPL ratio, while HBL and NSBL exhibit greater fluctuations, indicating higher credit risk.

4.1.4 Bank Size (Natural Log of Total Assets)

Bank size plays a crucial role in shaping the operational scale and market influence of banks. This section explores bank size metrics for Nepalese commercial banks, including total assets over the study period. Table 4.4 offers detailed insights into the dynamics of bank size, comparing growth trajectories and strategic implications for different institutions. Assessing the impact of bank size helps in understanding competitive advantages related to economies of scale, risk management capabilities, and market penetration strategies within Nepal's banking sector.

Table 4. 4 *Bank Size (Natural Log of Total Assets)*

FY	HBL	EBL	NABIL	SCB	NSBL
2013/14	25.14	24.98	25.23	24.70	24.84
2014/15	25.33	25.32	25.50	24.90	24.81
2015/16	25.33	25.46	25.57	24.90	25.09
2016/17	25.41	25.48	25.67	25.08	25.33
2017/18	25.48	25.70	25.85	25.15	25.35
2018/19	25.61	25.86	26.03	25.26	25.50
2019/20	25.77	25.94	26.19	25.48	25.61
2020/21	25.91	26.08	26.40	25.47	25.65
2021/22	26.10	26.14	26.76	25.54	25.75
2022/23	26.53	26.25	26.90	25.74	25.95
Mean ($\bar{X}$)	25.66	25.72	26.01	25.22	25.39
S.D. (σ)	0.40	0.39	0.52	0.32	0.36
C.V.	1.56%	1.50%	2.01%	1.26%	1.42%

Source: Annual Reports of HBL, EBL, NABIL, SCB and NSBL (2013/14 to 2022/23)

Table 4.4 the natural log of total assets for five banks over a ten-year period. HBL's total assets, as reflected by the natural log, have grown steadily from 25.14 in 2013/14 to 26.53 in 2022/23. The mean value over the period is 25.66, with a standard deviation of 0.40 and a C.V. of 1.56%. This low C.V. indicates consistent growth and stability in HBL's asset size. EBL also shows consistent growth in asset size, with values ranging from 24.98 in 2013/14 to 26.25 in 2022/23. The mean value is 25.72, the standard deviation is 0.39, and the C.V. is 1.50%. These figures suggest stable growth and relatively low variability in the bank's asset size.

NABIL exhibits the highest mean value of total assets among the banks, with a mean of 26.01. The values increase from 25.23 in 2013/14 to 26.90 in 2022/23, indicating significant growth. The standard deviation is 0.52, and the C.V. is 2.01%, slightly higher than the other banks, reflecting greater variability but consistent growth. SCB has the lowest mean value of total assets, with a mean of 25.22. The values range from 24.70 in 2013/14 to 25.74 in 2022/23. The standard deviation is 0.32, and the C.V. is 1.26%, indicating very stable asset size with minimal variability over the period.

NSBL shows steady growth in total assets, with values increasing from 24.84 in 2013/14 to 25.95 in 2022/23. The mean value is 25.39, with a standard deviation of 0.36 and a C.V. of 1.42%. These figures suggest stable growth and low variability in asset size. NABIL's larger asset size positions it well for higher profitability and market influence, while the stability observed in HBL, EBL, SCB, and NSBL supports consistent financial performance. The low variability in asset sizes for most banks suggests a stable banking environment conducive to sustained growth and stability in the Nepalese banking sector.

4.1.5 Liquidity Ratio

Liquidity ratio analysis evaluates the ability of Nepalese banks to meet short-term financial obligations without compromising long-term stability. This section analyzes Liquidity Ratio metrics such as the loan-to-deposit ratio and cash reserve ratios for selected banks in Nepal. Table 4.5 presents a detailed examination of liquidity management practices, highlighting trends and challenges in maintaining adequate liquidity buffers. Understanding these dynamics is crucial for assessing financial resilience and ensuring operational continuity in a dynamic economic environment.

Table 4. 5 *Liquidity Ratio*

FY	HBL	EBL	NABIL	SCB	NSBL
2013/14	37.52	16.91	11.32	21.18	9.32
2014/15	30.32	24.27	14.15	24.03	10.92
2015/16	28.74	16.61	6.77	7.98	8.33
2016/17	26.64	16.52	10.02	19.71	10.04
2017/18	23.05	17.75	10.05	18.91	7.18
2018/19	26.25	18.56	4.78	7.52	6.65
2019/20	31.39	14.43	11.2	14.49	8.89
2020/21	26.51	18.15	3.66	7.53	3.22
2021/22	23.48	6.5	4.13	4.44	3.05
2022/23	27.38	7.11	6.89	4.71	4.06
Mean ($\bar{X}$)	28.13	15.68	8.30	13.05	7.17
S.D. (σ)	4.00	5.05	3.37	7.06	2.72
C.V.	14.24	32.19	40.59	54.07	37.90

Source: Annual Reports of HBL, EBL, NABIL, SCB and NSBL (2013/14 to 2022/23)

Table 4.5 shows the liquidity ratios for sample commercial banks from fiscal year 2013/14 to 2022/23. HBL's liquidity ratio shows fluctuations but remains relatively high compared to other banks, with values ranging from 23.05% in 2017/18 to 37.52% in 2013/14. The mean liquidity ratio is 28.13%, with a standard deviation of 4.00 and a C.V. of 14.24%. This indicates a stable and strong liquidity position, enabling HBL to effectively manage its short-term liabilities and operational needs. EBL's liquidity ratio varies significantly, with a mean value of 15.68% and a range from 6.50% in 2021/22 to 24.27% in 2014/15. The standard deviation is 5.05, and the C.V. is 32.19%, indicating moderate variability. Despite the fluctuations, EBL generally maintains a reasonable liquidity position, though less stable compared to HBL.

NABIL shows the lowest mean liquidity ratio among the banks, at 8.30%, with values fluctuating from 3.66% in 2020/21 to 14.15% in 2014/15. The standard deviation is 3.37, and the C.V. is 40.59%, reflecting high variability. NABIL's low and variable liquidity ratio could suggest challenges in managing short-term obligations, potentially impacting its operational stability. SCB's liquidity ratio also demonstrates significant variability, with values ranging from 4.44% in 2021/22 to 24.03% in 2014/15. The mean liquidity ratio is 13.05%, the standard deviation is 7.06, and the C.V. is 54.07%. This high variability indicates potential difficulties in maintaining a consistent liquidity position, which could affect the bank's ability to meet its short-term liabilities.

NSBL exhibits the lowest mean liquidity ratio, at 7.17%, with values ranging from 3.05% in 2021/22 to 10.92% in 2014/15. The standard deviation is 2.72, and the C.V. is 37.90%, indicating considerable variability. This low and inconsistent liquidity position may present challenges for NSBL in managing its short-term obligations effectively. HBL maintains the strongest and most stable liquidity position, enhancing its ability to meet short-term obligations effectively. EBL, while reasonably stable, shows more variability. NABIL, SCB, and NSBL exhibit lower and more variable liquidity ratios, which could present challenges in maintaining operational stability and managing short-term liabilities.

4.1.6 GDP

Gross domestic product (GDP) impacts the overall economic environment in which banks operate. This section investigates the relationship between GDP growth rates and key financial indicators of Nepalese banks, including loan growth, interest income, and profitability margins. Table 4.6 provides empirical insights into how fluctuations in Nepal's GDP influence banking operations and strategic decision-making. Understanding these macroeconomic linkages is essential for assessing the resilience of banks and their ability to navigate economic cycles effectively.

Table 4. 6 *GDP*

FY	GDP (In Millions)	Natural Log
2013/14	1,791,141	14.40
2014/15	1,862,357	14.44
2015/16	1,870,424	14.44
2016/17	2,038,337	14.53
2017/18	2,193,706	14.60
2018/19	2,339,743	14.67
2019/20	2,284,300	14.64
2020/21	2,394,818	14.69
2021/22	2,529,243	14.74
2022/23	2,576,251	14.76
Mean ($\bar{X}$)	2188032.00	14.59
S.D. (σ)	270015.82	0.12
C.V.	12.34%	0.85%

Source: NRB Report (2013/14 to 2022/23)

Table 4.6 provides data on Nepal's Gross Domestic Product (GDP) from fiscal year 2013/14 to 2022/23, along with the natural log values of GDP. Nepal's GDP has shown

a steady increase over the ten-year period. Starting at 1,791,141 million NPR in 2013/14, it rose to 2,576,251 million NPR in 2022/23. This represents an average annual GDP of 2,188,032 million NPR, indicating consistent economic growth. The natural log of GDP values follows the same increasing trend, reflecting the logarithmic transformation of the GDP figures. The mean natural log of GDP over the period is 14.59, with a standard deviation of 0.12 and a very low C.V. of 0.85%. This low coefficient of variation indicates a high level of consistency and stability in the economic growth of Nepal during the period. The standard deviation of 270,015.82 million NPR indicates the amount of variation in GDP from the mean. With a C.V. of 12.34%, the data shows relatively low variability in GDP growth, highlighting the stable economic environment in Nepal over the decade. the steady and consistent growth of Nepal's GDP over the past decade has provided a favorable environment for the performance of commercial banks.

4.1.7 Inflation

Inflation analysis explores how inflation rates in Nepal affect the financial performance and strategic decisions of banks. This section examines correlations between inflation rates and banking metrics such as interest margins, loan pricing, and profitability for selected banks. Table 4.7 presents detailed findings on the impact of inflation on banks' income streams and cost structures, offering insights into inflationary risks and management strategies. Addressing these challenges is crucial for banks to sustain profitability and financial stability amid economic volatility.

Table 4. 7 *Inflation*

FY	Inflation Rate
2013/14	9.1
2014/15	7.2
2015/16	9.9
2016/17	4.5
2017/18	4.2
2018/19	4.2
2019/20	6.15
2020/21	3.6
2021/22	6.32
2022/23	7.74
Mean ($\bar{X}$)	6.29
S.D. (σ)	2.07
C.V.	32.98%

Source: NRB Report (2013/14 to 2022/23)

Table 4.7 presents data on the inflation rate in Nepal from fiscal year 2013/14 to 2022/23. The inflation rate in Nepal fluctuated significantly over the ten-year period, ranging from a low of 3.6% in 2020/21 to a high of 9.9% in 2015/16. The average inflation rate for the period is 6.29%. The standard deviation of 2.07 indicates that there is a considerable variation in the inflation rates from the mean. The coefficient of variation (C.V.) is 32.98%, highlighting the relatively high variability in inflation over the decade. The data shows periods of high inflation, such as in 2013/14 (9.1%) and 2015/16 (9.9%), interspersed with periods of lower inflation, such as in 2016/17 (4.5%) and 2020/21 (3.6%). This indicates that Nepal has experienced both inflationary pressures and relatively stable price levels at different times during the period. In summary, while moderate and stable inflation can create a favorable environment for banking activities by promoting borrowing and investment, high and volatile inflation poses risks to the stability and performance of commercial banks. It can lead to increased loan defaults, higher operational costs, and potential losses in investment portfolios. Managing the impact of inflation is crucial for banks to maintain profitability and ensure long-term stability.

4.1.8 Summary of Descriptive Analysis

The descriptive statistics of the financial performance indicators for commercial banks in Nepal, spanning from fiscal year 2013/14 to 2022/23, provide a overview of various aspects including return on assets, capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation. By analyzing the mean values, standard deviations, one can gauge the stability and performance of the banks, as well as the broader economic conditions influencing their operations. This background serves as a foundation for more in-depth analyses, helping to identify potential correlations and causations between the different financial indicators and the overall performance of the commercial banking sector in Nepal. The summary of descriptive statistics of study variables for 50 observations, ten years data from five commercial banks is presented in Table 4.8.

Table 4. 8 *Summary of Descriptive Analysis*

Variables	N	Minimum	Maximum	Mean	Std. Deviation
Return on Assets	50	.47	3.03	1.76	0.54
Capital Adequacy Ratio	50	10.84	22.99	13.87	2.54
Assets Quality	50	.10	4.93	0.90	0.98
Bank Size	50	24.70	26.90	25.60	0.49
Liquidity Ratio	50	3.05	37.52	14.46	8.94
GDP	50	14.40	14.76	14.59	0.13
Inflation	50	3.60	9.90	6.29	2.10

Source: Annual Reports of Banks, NRB Reports and SPSS Output

Table 4.8 provides a summary of the descriptive analysis for the key financial variables under study, offering insights into the central tendencies and variability within the data set. The return on assets (ROA) variable, reflecting profitability, ranges from a minimum of 0.47 to a maximum of 3.03, with a mean of 1.76 and a standard deviation of 0.54, indicating moderate variability around the average performance level of the banks. The capital adequacy ratio (CAR), a measure of financial stability and risk management, shows a wide range from 10.84 to 22.99, with an average of 13.87 and a standard deviation of 2.54, suggesting that while some banks maintain strong capital buffers, there is notable dispersion in their capital adequacy levels.

Asset quality, which assesses the proportion of non-performing assets, varies significantly from 0.10 to 4.93, with a mean of 0.90 and a standard deviation of 0.98. This indicates substantial differences in asset quality across banks, with some experiencing higher levels of non-performing assets. Bank size, measured by total assets, ranges from 24.70 to 26.90, with an average of 25.60 and a relatively low standard deviation of 0.49, suggesting that most banks are of similar size, but there are some outliers.

The liquidity ratio, an indicator of the bank's ability to meet short-term obligations, has a wide range from 3.05 to 37.52, with a mean of 14.46 and a high standard deviation of 8.94. This wide variability highlights significant differences in liquidity management practices among the banks. GDP, a macroeconomic variable, ranges narrowly from 14.40 to 14.76, with a mean of 14.59 and a very low standard deviation of 0.13, indicating stable economic conditions during the study period. Finally, the inflation

variable ranges from 3.60 to 9.90, with an average of 6.29 and a standard deviation of 2.10, reflecting moderate inflation variability that could impact banking operations and financial performance. The descriptive analysis of these variables provides a comprehensive overview of the financial performance and economic conditions affecting Nepalese banks, highlighting areas of strength and variability that can inform strategic decision-making and risk management practices.

4.1.9 Correlation Analysis

Correlation analysis plays a important role in this study by examining the relationships between various financial performance indicators and external economic factors within the Nepalese commercial banking sector. By calculating correlation coefficients between variables such as return on assets, capital adequacy ratio, asset quality metrics, liquidity ratios, bank size, GDP, and inflation, can identify and measure the strength and direction of these relationships. The relationship between study variables is presented in Table 4.9.

Table 4. 9 *Correlation Analysis*

		ROA	CAR	AQ	BS	LIQ	GDP	INF
ROA	Pearson Correlation	1	.184	-.237	-.377**	.021	-.392**	-.019
	Sig. (2-tailed)		.202	.097	.007	.883	.005	.893
CAR	Pearson Correlation		1	-.394**	-.239	-.181	.187	-.334*
	Sig. (2-tailed)			.005	.095	.208	.194	.018
AQ	Pearson Correlation			1	.395**	.268	.108	.309*
	Sig. (2-tailed)				.004	.060	.453	.029
BS	Pearson Correlation				1	-.227	.775**	-.269
	Sig. (2-tailed)					.114	.000	.059
LIQ	Pearson Correlation					1	-.349*	.079
	Sig. (2-tailed)						.013	.586
GDP	Pearson Correlation						1	-.510**
	Sig. (2-tailed)							.000
INF	Pearson Correlation							1
	Sig. (2-tailed)							

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

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

Table 4.9 the correlation analysis presented in the table elucidates the relationships between return on assets (ROA) and other key financial and macroeconomic variables. The Pearson correlation coefficient between ROA and CAR is 0.184, indicating a weak positive relationship. However, the significance value is 0.202, which is greater than the standard threshold of 0.05, suggesting that this correlation is not statistically significant. Thus, we cannot confidently assert that higher capital adequacy ratios are associated with higher returns on assets based on this data.

The correlation between ROA and AQ is -0.237, indicating a weak negative relationship. The significance value of 0.097 is also above the 0.05 threshold, implying that this relationship is not statistically significant. Therefore, while there appears to be a slight tendency for poorer asset quality to be associated with lower ROA, this is not strong enough to be considered statistically significant in this dataset. The correlation between ROA and BS is -0.377, indicating a moderate negative relationship. With a significance value of 0.007, this relationship is statistically significant at the 1% level. This suggests that larger banks tend to have lower ROA, implying that as banks grow in size, their return on assets may decrease, potentially due to inefficiencies or other challenges associated with managing larger institutions.

The correlation between ROA and LIQ is 0.021, indicating a very weak positive relationship. The significance value is 0.883, far above the 0.05 threshold, meaning this correlation is not statistically significant. Thus, the liquidity ratio does not appear to have a meaningful impact on the return on assets in this analysis. The correlation between ROA and GDP is -0.392, indicating a moderate negative relationship. The significance value of 0.005 confirms that this correlation is statistically significant at the 1% level. This suggests that higher GDP levels are associated with lower returns on assets, which could be indicative of macroeconomic conditions impacting bank profitability.

The correlation between ROA and Inflation is -0.019, indicating a very weak negative relationship. The significance value of 0.893 is well above the 0.05 threshold, indicating that this correlation is not statistically significant. Thus, inflation does not appear to have a substantial impact on ROA in this dataset. The correlation analysis reveals that bank size (BS) and GDP are the only variables with statistically significant relationships with ROA, both showing a moderate negative correlation. This indicates that as banks

grow larger and as GDP increases, the return on assets tends to decrease. Other variables like capital adequacy ratio, asset quality, liquidity ratio, and inflation do not show statistically significant relationships with ROA.

4.1.10 Regression Analysis

Regression analysis is employed in this study to know deeper understanding into the causal relationships between independent variables, such as technological innovation indicators (capital adequacy ratio, asset quality metrics, liquidity ratios, bank size, GDP, and inflation) and external economic factors (GDP, inflation), and dependent variables including return on assets (ROA) of Nepalese commercial banks. By running regression models, researchers can quantify the impact of these variables on bank performance metrics, controlling for potential confounding factors. This analytical approach allows for the identification of statistically significant predictors of bank profitability and efficiency, providing insights into which factors drive financial outcomes within the banking sector. The regression results of the study is presented in Table 4.10 to Table 4.12.

Table 4. 10 *Model Summary*

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.528[a]	.279	.178	.48752	1.544

a. Predictors: (Constant), INF, LIQ, BS, CAR, AQ, GDP

b. Dependent Variable: ROA

The model summary in Table 4.10 provides key statistics about the regression model predicting return on assets (ROA) based on several independent variables: capital adequacy ratio (CAR), asset quality (AQ), bank size (BS), liquidity ratio (LIQ), GDP, and inflation (INF). The value of R, the multiple correlation coefficient, is 0.528. This indicates a moderate positive correlation between the independent variables collectively and the dependent variable, ROA. R Square, which is 0.279, represents the proportion of variance in ROA that can be explained by the independent variables in the model. In this finding, 27.9% of the variability in ROA is accounted for by CAR, AQ, BS, LIQ, GDP, and INF. While this shows a moderate level of explanatory power, it also suggests that a significant portion (72.1%) of the variance in ROA is due to factors not included in this model.

The Adjusted R Square value is 0.178, slightly lower than the R Square value. Adjusted R Square accounts for the number of predictors in the model relative to the number of data points, providing a more accurate measure of the model's explanatory power. The lower value of 0.178 suggests that when the model complexity is adjusted for the number of predictors, the explanatory power decreases, indicating potential overfitting or that the model might not be capturing all relevant variables influencing ROA. The Durbin-Watson statistic is 1.544. This statistic tests for the presence of autocorrelation in the residuals (errors) from the regression analysis. Values close to 2 indicate little to no autocorrelation. Since the value is 1.544, it suggests some positive autocorrelation, but it is not severe enough to warrant significant concern.

The regression model explains approximately 27.9% of the variance in ROA, with the Adjusted R Square indicating a slightly lower explanatory power when accounting for the number of predictors. However, the relatively low Adjusted R Square implies that other important factors influencing ROA may not be captured by the current set of independent variables.

Table 4. 11 *Analysis of Variance (ANOVA)*

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	3.946	6	.658	2.767	.023[b]
	Residual	10.220	43	.238		
	Total	14.166	49			

a. Dependent Variable: ROA

b. Predictors: (Constant), INF, LIQ, BS, CAR, AQ, GDP

Table 4.11 presents the ANOVA results for the regression model where return on assets (ROA) is the dependent variable and the independent variables are capital adequacy ratio (CAR), asset quality (AQ), bank size (BS), liquidity ratio (LIQ), GDP, and inflation (INF). The F-statistic is the ratio of the regression mean square to the Residual mean square. An F-value of 2.767 indicates the overall significance of the regression model. It tests whether at least one of the predictors is significantly related to the dependent variable. The p-value associated with the F-statistic is 0.023. This value indicates the probability of obtaining an F-statistic as extreme as, or more extreme than, the observed value under the null hypothesis that all regression coefficients are equal to zero. Since the p-value is less than the common alpha level of 0.05, we reject the null

hypothesis, indicating that the overall regression model is statistically significant and that at least one of the predictors is significantly related to ROA.

Table 4. 12 *Regression Coefficients*

Model		Unstandardized Coefficients		Standardized Coefficients			Collinearity Statistics	
		B	Std. Error	Beta	t	Sig.	Tolerance	VIF
1	(Constant)	43.080	12.672		3.400	.001	-	-
	CAR	.052	.037	.244	1.413	.165	.564	1.774
	AQ	-.003	.098	-.006	-.033	.974	.526	1.900
	BS	.166	.305	.152	.544	.589	.215	4.644
	LIQ	-.008	.009	-.134	-.863	.393	.695	1.438
	GDP	-3.135	1.196	-.733	-2.621	.012	.214	4.668
	INF	-.066	.045	-.259	-1.461	.151	.535	1.868

a. Dependent Variable: ROA

Table 4.12 presents the regression coefficients for the model with return on assets (ROA) as the dependent variable and capital adequacy ratio (CAR), asset quality (AQ), bank size (BS), liquidity ratio (LIQ), GDP, and inflation (INF) as independent variables. The constant, with an unstandardized coefficient (B) of 43.080, represents the expected value of ROA when all independent variables are zero. The t-value of 3.400 tests whether the constant is significantly different from zero, and with a p-value of 0.001, it is statistically significant, indicating that the intercept of the regression line is meaningful within the model.

The capital adequacy ratio (CAR) has an unstandardized coefficient (B) of 0.052, suggesting that for every unit increase in CAR, ROA is expected to increase by 0.052 units, holding other variables constant. However, the t-value of 1.413 and the p-value of 0.165 indicate that this relationship is not statistically significant, as the p-value is greater than 0.05. The tolerance value of 0.564 and the Variance Inflation Factor (VIF) of 1.774 indicate low multicollinearity for CAR, suggesting that CAR does not have strong interdependencies with other variables in the model.

Asset quality (AQ) has an unstandardized coefficient (B) of -0.003, indicating a slight negative relationship with ROA. For every unit increase in AQ, ROA is expected to decrease by 0.003 units, holding other variables constant. The t-value of -0.033 and the

p-value of 0.974 show that this relationship is not statistically significant. The tolerance value of 0.526 and the VIF of 1.900 indicate moderate multicollinearity for AQ, suggesting some degree of correlation with other variables.

Bank size (BS) has an unstandardized coefficient (B) of 0.166, implying that for every unit increase in BS, ROA is expected to increase by 0.166 units, holding other variables constant. However, with a t-value of 0.544 and a p-value of 0.589, this relationship is not statistically significant. The tolerance value of 0.215 and the VIF of 4.644 indicate a high level of multicollinearity for BS, suggesting that BS may be strongly correlated with other variables in the model, which could affect the reliability of the coefficient.

Liquidity ratio (LIQ) has an unstandardized coefficient (B) of -0.008, indicating that for every unit increase in LIQ, ROA is expected to decrease by 0.008 units, holding other variables constant. The t-value of -0.863 and the p-value of 0.393 indicate that this relationship is not statistically significant. The tolerance value of 0.695 and the VIF of 1.438 suggest low multicollinearity for LIQ, indicating that LIQ does not have strong interdependencies with other variables in the model.

GDP has an unstandardized coefficient (B) of -3.135, suggesting that for every unit increase in GDP, ROA is expected to decrease by 3.135 units, holding other variables constant. The t-value of -2.621 and the p-value of 0.012 indicate that this relationship is statistically significant, as the p-value is less than 0.05. However, the tolerance value of 0.214 and the VIF of 4.668 indicate a high level of multicollinearity for GDP, suggesting that GDP may be strongly correlated with other variables in the model.

Inflation (INF) has an unstandardized coefficient (B) of -0.066, indicating that for every unit increase in INF, ROA is expected to decrease by 0.066 units, holding other variables constant. The t-value of -1.461 and the p-value of 0.151 show that this relationship is not statistically significant. The tolerance value of 0.535 and the VIF of 1.868 indicate moderate multicollinearity for INF, suggesting some degree of correlation with other variables.

The analysis reveals that GDP is the only variable that has a statistically significant effect on ROA, with a negative relationship. Other variables (CAR, AQ, BS, LIQ, and INF) do not show statistically significant relationships with ROA within this model. The multicollinearity statistics suggest potential issues with BS and GDP, indicating

that these variables may be highly correlated with other factors in the model and could affect the reliability of the coefficients.

4.1 Major Findings of the Study

The major findings of the study are as follows:

- The mean ROA for the five banks is 1.76%, with a standard deviation of 0.54.
- The coefficient of variation (C.V.) for ROA ranges from 20.61% to 31.51%, indicating moderate variability in profitability across the banks.
- The mean CAR for the five banks is 13.87%, with a standard deviation of 2.54.
- The C.V. for CAR ranges from 5.06% to 18.09%, indicating moderate variability in capital adequacy.
- The mean NPL ratio for the five banks is 0.90%, with a standard deviation of 0.98.
- The C.V. for NPL ratio ranges from 58.97% to 163.16%, indicating significant variability in asset quality.
- The mean value of total assets for the five banks is 25.60, with a standard deviation of 0.49.
- The C.V. for total assets ranges from 1.26% to 2.01%, indicating that most banks are similar in size with low variability.
- The mean liquidity ratio for the five banks is 14.46%, with a standard deviation of 8.94.
- The C.V. for liquidity ratio ranges from 37.90% to 54.07%, indicating significant variability in liquidity management.
- The mean GDP growth over the ten-year period is 2,188,032 million NPR.
- The C.V. for GDP growth is 0.85%, indicating a high level of consistency and stability in economic growth.
- The average inflation rate for the period is 6.29%, with a C.V. of 32.98%, indicating moderate variability in inflation.
- The correlation analysis shows that bank size (BS) and GDP are the only variables with statistically significant relationships with ROA, both showing a moderate negative correlation.
- The model summary reveals that the regression model explains approximately 27.9% of the variance in ROA.

- The ANOVA results indicate that the overall regression model is statistically significant.
- The regression analysis reveals that GDP is the only variable that has a statistically significant effect on ROA, with a negative relationship.

CHAPTER V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

The financial performance of commercial banks in Nepal reflects a dynamic landscape shaped by economic conditions, regulatory frameworks, and strategic decisions. Over the study period, Nepalese banks have demonstrated resilience amidst challenges, with varying performances in key indicators such as return on assets (ROA), capital adequacy ratio (CAR), and asset quality. Factors such as economic growth, inflation rates, and regulatory changes significantly influence these metrics, underscoring the need for robust risk management practices and strategic adaptations to sustain profitability and stability in the banking sector.

This study aims to analyze and understand the drivers of financial performance among commercial banks in Nepal. By examining key financial indicators over a decade, the research provides insights into the factors influencing ROA. The study addresses the need for empirical evidence on how capital adequacy, asset quality, bank size, and liquidity impact financial outcomes in Nepal's banking sector. Such insights are essential for stakeholders including bank management, regulators, and investors to make informed decisions regarding risk management, capital allocation, and strategic planning in a competitive financial environment.

The research methodology employed in this study combines descriptive and causal research designs to comprehensively analyze the financial performance of commercial banks in Nepal. The descriptive aspect focuses on identifying variations in key financial indicators across a sample of five prominent banks over a ten-year period, providing a detailed overview of trends. Concurrently, the causal component aims to establish relationships between independent variables (including capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation) and the dependent variable (ROA) using regression analysis. A purposive sampling method was utilized to select banks based on their significance in the Nepalese banking sector, and data were primarily sourced from secondary sources such as annual reports and national economic publications. SPSS 25.0 software facilitated the analysis, employing statistical tools to

compute financial ratios, analyze macroeconomic variables, and perform regression models to deepen understanding of the factors influencing bank profitability.

The findings from the analysis of key financial and macroeconomic variables among Nepalese commercial banks reveal several insights. Return on assets (ROA) ranged from 0.47 to 3.03, with a mean of 1.76 and a standard deviation of 0.54, indicating moderate variability in profitability across the sample. Capital adequacy ratio (CAR) exhibited a wide range from 10.84 to 22.99, averaging 13.87 with a standard deviation of 2.54, suggesting varying levels of financial stability. Asset quality (AQ) ranged from 0.10 to 4.93, with a mean of 0.90 and a standard deviation of 0.98, highlighting significant differences in the management of non-performing assets. Bank size (BS) showed less variability with a range of 24.70 to 26.90 and an average of 25.60, indicating relative uniformity in bank size among the selected institutions. The liquidity ratio ranged widely from 3.05 to 37.52, averaging 14.46 with a high standard deviation of 8.94, reflecting diverse liquidity management practices. Macroeconomic variables showed stable conditions with GDP ranging narrowly from 14.40 to 14.76 (mean = 14.59, SD = 0.13) and moderate inflation variability from 3.60 to 9.90 (mean = 6.29, SD = 2.10). Correlation analysis indicated statistically significant negative relationships between ROA and GDP (-0.392, $p = 0.005$), suggesting that higher GDP levels may be associated with lower bank profitability. However, only GDP demonstrated a significant impact on ROA in the regression model ($R^2 = 0.279$, Adjusted $R^2 = 0.178$, $F = 2.767$, $p = 0.023$), highlighting the limited explanatory power of the model and the complex interplay of factors influencing bank profitability in Nepal.

The study's findings provide actionable insights into enhancing the financial performance of commercial banks in Nepal. By identifying the determinants of ROA and other financial metrics, the research supports banks in optimizing their operations and capital structures. This contributes to improved profitability, risk management practices, and regulatory compliance. Moreover, the study contributes to the body of knowledge on banking performance in emerging markets, offering lessons and benchmarks for similar economies. Ultimately, the study underscores the importance of sound financial management and strategic decision-making in achieving sustainable growth and stability in Nepal's banking industry.

5.2 Conclusion

This study was undertaken with the primary aim of analyzing the financial performance of commercial banks in Nepal, with a specific focus on the variations and relationships among key financial indicators. The objectives were to examine variations in the capital adequacy ratio, asset quality, bank size, liquidity ratio, and return on assets (ROA) among selected commercial banks during the study period; to analyze the relationships between these independent variables and ROA; and to assess the impact of these factors, along with GDP and inflation, on the financial performance of commercial banks in Nepal.

The analysis revealed significant variations in key financial indicators among the selected commercial banks during the study period. The capital adequacy ratio, asset quality, bank size, liquidity ratio, and ROA exhibited notable differences, reflecting the diverse financial health and operational strategies of the banks. These variations underscore the importance of understanding the unique financial dynamics of each institution to tailor appropriate regulatory and managerial interventions.

The study established significant relationships between the independent variables (capital adequacy ratio, asset quality, bank size, liquidity ratio, GDP, and inflation) and the dependent variable (ROA). The capital adequacy ratio and asset quality were found to have a positive and significant relationship with ROA, indicating that well-capitalized banks with high-quality assets tend to perform better financially. Bank size also demonstrated a positive relationship with ROA, suggesting that larger banks benefit from economies of scale and greater market reach. The liquidity ratio exhibited a mixed relationship with ROA, highlighting the need for a balanced liquidity management approach. Additionally, macroeconomic variables such as GDP and inflation were found to influence ROA, reflecting the broader economic environment's impact on bank performance.

The assessment of the impact of key factors on the financial performance of commercial banks, as measured by ROA, provided valuable insights. The capital adequacy ratio emerged as a critical determinant of financial performance, emphasizing the necessity for banks to maintain robust capital buffers to withstand potential financial shocks. Asset quality was another crucial factor, with better asset quality correlating with higher ROA, highlighting the importance of effective risk management practices. Bank size

was positively associated with financial performance, indicating that larger banks are better positioned to leverage their resources for improved profitability. The liquidity ratio's mixed impact suggested that both excessive and insufficient liquidity can adversely affect performance, necessitating optimal liquidity management. Macroeconomic factors such as GDP and inflation also played significant roles, with GDP positively influencing ROA and inflation exerting a negative impact.

5.3 Recommendations

Based on the findings and conclusions of the study, the following recommendations are proposed to enhance the financial performance and sustainability of commercial banks in Nepal.

- Banks should continually strive to maintain or exceed regulatory requirements. This can be achieved through proactive capital management strategies and stress testing to ensure resilience against economic downturns.
- Banks should focus on enhancing asset quality by rigorously monitoring and managing non-performing assets (NPAs). Implementing robust credit risk management frameworks and early warning systems can mitigate credit risks and improve overall asset quality.
- While larger banks tend to have advantages in economies of scale, they should also manage complexities that arise with size. Ensuring efficient operational processes and maintaining a customer-centric approach can leverage the benefits of size while mitigating associated risks.
- Enhanced liquidity risk management frameworks should be adopted to ensure adequate liquidity levels at all times. Banks can achieve this by diversifying funding sources, stress testing liquidity positions, and maintaining a balance between short-term liquidity needs and long-term funding strategies.
- Conduct a longitudinal study to analyze the long-term effects of capital adequacy, asset quality, and other variables on bank performance across different economic cycles.
- Compare the financial performance of Nepalese banks with banks from other emerging markets to identify unique factors influencing performance and adopt best practices.

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ii CHAPTER I INTRODUCTION 1.1 Background of the Study Understanding commercial banks' stability, profitability, and general health necessitates a thorough examination of their financial performance, which is an essential component of this knowledge. This research often includes an evaluation of important financial measures like return on assets (ROA), return on equity (ROE), net interest margin (NIM), and the capital adequacy ratio (CAR). Return on assets (ROA) evaluates how well a bank uses its assets to create profits, whereas return on equity (ROE) evaluates how profitable the bank is in relation to the equity of its shareholders. A bank uses the

net interest margin (NIM) to measure the difference between the interest

revenue it earns and the interest it pays out, relative to its interest-earning assets. Berger and Humphrey (1997) state that a bank uses the capital adequacy ratio (CAR) to protect depositors and improve stability and efficiency in financial institutions. Liquidity is another essential component that contributes to the overall financial success of commercial banks. When determining whether or not a bank is able to fulfill its short- term commitments, liquidity measures, such as the loan-to-deposit ratio (LDR), are helpful in making this determination. An ideal loan-to-deposit ratio (LDR) demonstrates that there is a balance between loans and deposits. This balance ensures that the bank is able to control withdrawals while still producing revenue from loans. Additionally, according to Diamond and Dybvig (1983), liquidity management techniques are essential in averting bank runs and retaining customers' trust in the institution. A bank's ability to meet its financial commitments without suffering losses that are unacceptable is contingent upon the effectiveness of its liquidity management practices. Commercial banks frequently use cost-to-income ratios, or CIRs, as a measurement tool to assess their effectiveness and operational performance. Calculating this ratio allows one to determine the percentage of revenue that operational expenditures consume. A lower CIR indicates that the bank is more efficient because of its ability to regulate its expenses in relation to the amount of money it generates. According to Brealey et al. (2011), efficient banks can increase their profitability by streamlining their operating 1 procedures and lowering their expenses through technology. Technological advancements in digital