

CHAPTER -I

INTRODUCTION

1.1 General Background

Commercial Bank is one of the financial institutions which provide public borrowing and lending along with other financial services. It collects scattered fund and channels to productive use along with remitting funds. Except above, a commercial bank performs many subsidiary functions like collection of cheques and promissory notes, invests in government securities and treasury bills, deals in foreign exchange, and underwrites shares, makes payment of bills, works as guarantor, and many other functions. Nowadays, the banking sector has reached to the most remote areas of Nepal, and has gained a good experience in the growth of the economy.

Modern banking was originated in medieval Italy. The first bank called "*Bank of Venice*" was established in Italy in 1157. The "*Bank of Barcelona*" and "*Bank of Genoa*" were established in 1401 and 1407 respectively. Banking slowly spread to the rest of Europe. Then, the "*Bank of England*" came into existence in 1694. The bank on modern line developed in India only after the British rule. In Nepal, development of banking is relatively recent. But there was no complete absence of banking activities. The record of banking system in Nepal gives detail account of mixture of slow and steady evolution in the financial and global economy of Nepalese life. But the history of financial institution in Nepal started with the practices followed by money lenders of ancient times. For many years, wealthy individuals, agriculturists, landlords, merchants and traders conducted some banking activities as a side business. The regular history of coinage in Nepal began from the 5th century. In the year 879/80, "Shankhadar Shankhwa" introduced a new era after paying all the debt that existed in the country. Silver coinage was introduced during 12th century. The term "Tanka Dhari" meaning "money dealer" was used at the end of the

14th century. The establishment of “*Kaushi Tosha Khana*” could be considered as the first step towards initiating banking development in Nepal as a bank, which deals in money and credit. In the year 1877, the “*Tejarath Adda*” was established to provide credit facilities to the general public at a concessional interest rate on collateral of gold and silver. In 1938, Nepal Bank Ltd laid the foundation of modern financial system in Nepal. This was the first commercial bank, and was owned by the government of Nepal. It played a dual role of a commercial bank and Central Bank, prior to the establishment of Central Bank in the country. But note issuing function was entrusted to “*Muluki Khana*”, the treasury of the government. In 1956, Nepal Rastra Bank was established to carry out all the functions of central bank focusing on the monetary stability of the country, to manage the issuance of Nepalese currency throughout the country, to stabilize exchange rates of Nepalese currency and to enhance financial intermediation by developing sound banking system in order to mobilize capital for development of trade and industry. The entire business of currency note, exchange and other concerned activities were entrusted to this bank. It was empowered by Act to have direct control over banking institutions within the country. NRB led to the gradual expansion of the specialized institution in the financial sector in order to provide institutional credit for different purposes.

Since the private sector did not take any initiative to establish another commercial bank for a long time, government established Rastriya Banijya Bank in 1966 under RBB Act 1965. This commercial bank was entrusted to perform the commercial banking activities and to look after the convenience and economic interest of general public. In the absence of proper commercial banking Act, it was impossible to meet the financial needs of the country. So, a newly introduced Act, Commercial Banking Act 1974, was enforced, and was amended later in 1984 to increase competition among commercial banks. Hence, provision was made to allow private sectors including foreign investment to open commercial banks. As a result, Nabil Bank Ltd. the then

Nepal Arab Bank Ltd. was established in 1984 with the partnership of Dubai Bank Ltd.

Liberalization in 1985 gave impetus to the global market and deregulation of both product and capital market. Several new policy majors have been adopted in line with the open market oriented and liberal economic policy to establish the economy, and paved the way for accelerating economy and social development. The monetary policies, being fine-tuned to increase domestic resource mobilization, enhance efficiency of capital and provide credit to the priority and production sectors. Steps were taken in a wide range of financial reforms. With the restoration of democracy in 1990, numbers of commercial banks were opened in the economy and many more were in the pipeline. Government owned banks or financial institutions were also restructured. After the introduction of development Bank Act 1995, there was a rush to establish banks.

Nepalese financial sector can be divided into two parts: namely, the banking system and the non-banking financial system. The banking system comprises of the Central Bank, Commercial Banks, Development Banks, Gramin Bikas Banks (Rural Development Banks), Exchange bank, Saving Bank, Industrial Bank, Merchant Bank, Co-operative Bank etc. The non-financial system comprises of Financial Companies, Cooperatives, NGO's conducting limited banking activities, Postal Saving Offices and Nepal Stock Exchange Ltd. Till 5th August 2011, there are 31 Commercial Banks, 87 Development Banks, 79 Finance Companies and 21 Micro-Credit Development Banks and 16 NRB-licensed Saving and Credit Cooperatives, and 38 NRB-Licensed NGOs according to the Central Bank. Some more financial institutions are underway to get operating license and others are planning to upgrade to the class-A Commercial Banks. But some are going to merge too.

1.2 Profiles of Machhapuchchhare Bank Ltd. and Nepal Investment Bank Ltd.

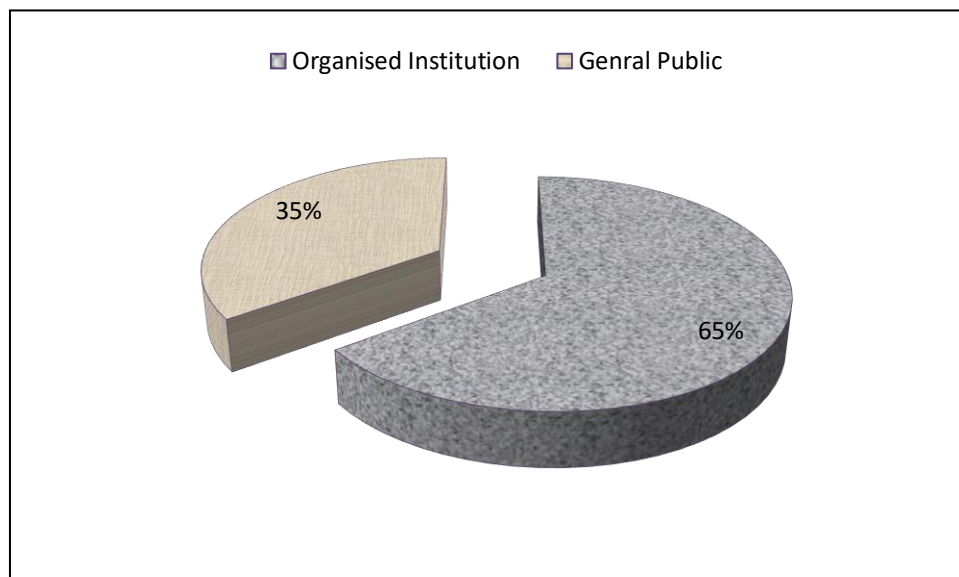
The study entitled “**Financial Performance Analysis of Machhapuchchhare Bank Ltd. in comparison to the Nepal Investment Bank Ltd.**” mainly focuses on the financial analysis and its comparative study of these banks. These both banks are commercial banks in private sector. Due to similarity of nature of works, it is pertinent to make a comparison for more detail analysis.

1.2.1 Introduction to Machhapuchchhare Bank Ltd. in Nepal

Machhapuchchhare Bank was first established in Pokhara as a regional bank in 1998, and become a national bank in 2000. Since then, it has been providing the most advanced and consumer-oriented banking services to its customers. At present, it has 39 branches all over the country till January 10- 2011 along with extension counters. It has installed 51 ATMs in various locations. It has authorized capital of 2000 million Rupees and a share capital of 65% of the local promoters and 35% of the general public. It has paid up capital of NPR.1.47 billion. It has about 12957 shareholders and more than 153000 depositors and thousands of other customers. This bank has been placed in ‘A’ class category bank by NRB. The bank started banking business which has become more challenging and more competitive.

Figure: 1.1

Share Structure of MBL Ltd.



The bank has registered a total deposit of NPR.18.54 billion till the end of 2009/10. In addition to commercial and industrial loan, it also provides home loan, higher purchase loan, education loan, transportation loan, business loan, and mortgage loan. The bank also invests money in different schemes. It has floated NPR. 14.97 billion loans. Till the end of 2009/2010, the bank has posted operating profit of NPR.86.6 million as per bank's press release.

The bank is providing facility of different saving accounts to different level of its customers. The savings like *Royal Saving A/C, Salary Management Program, Shareholder's Saving A/C, Yuva Saving A/C, Honor Saving A/C, Higher Education Deposit A/C and Pewa Saving A/C* are being facilitated to the concern people. The bank also does foreign currency exchange works. This bank is providing agency services, money transfer services, bill payment, letter of credit facilities, telephone bill payment, locker facilities, etc. The bank has given priority to tap into remittance amount by increasing international network.

MBL has the motto of providing *service with personal touch*. It has been providing many kinds of services. With the help of GLOBUS Banking Software, Machhapuchchhre bank is providing “*Anywhere banking services, Internet banking, SMS/ Mobile banking, ATM/Debit Card, Evening banking, 365 days banking and Evening counters facilities*”. The bank is trying to increase its scope in international Trade. To make technological base even sounder, it has upgraded current Globus System to T24 with nonstop version. The bank is committed to provide continuity in quality management by increasing ATM expansion and opening newer branches and extension counters at different places.

Some objectives of the Machhapuchchhre Bank are as listed below:

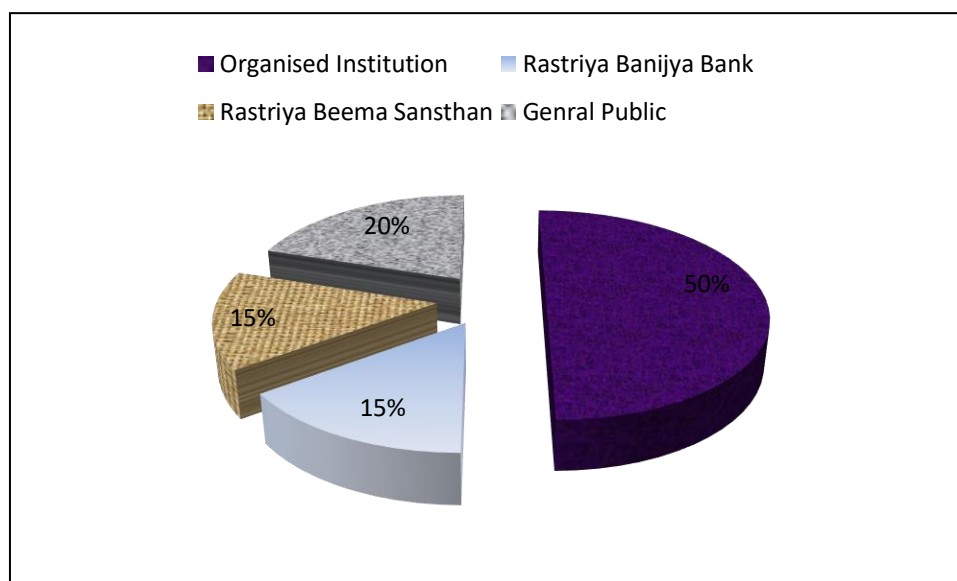
- This bank will continue its deposit policy to reduce dependency on corporate deposit by encouraging and increasing personal deposit with focus on saving deposit.
- It will continue its selective, qualitative and diverse loan disbursement policies.
- Giving due priority to fund management and international trade, it would continue to improve on capacity and effectiveness.
- Opening a separate department to risk management.
- It is focusing on corporate governance by obeying the rules and regulations laid down by the government. Also, following the decisions made by the Board of Directors, and suggestion given by the internal as well as the external auditor.
- Technology up gradation of present Software to T 24, installing switching system equipment and Visa electron card with a view to provide value added banking products and services.
- Providing training to human resource to cope up with the international banking system.
- Opening new branches and Spreading ATM network.
- Developing new services and product with a strategy to develop market.
- This bank is also committed to provide higher return to shareholders.
- Adopting Nepal accounting standard.
- Bearing corporate social responsibilities like Natural disaster and social activities and helping culture and musical activities.
- Adopting internal control as per Nepal Rastra Bank directives.
- Adopting transparency in information dissemination.

1.2.2 Introduction to Nepal Investment Bank Ltd in Nepal

Nepal Investment Bank Limited, previously Nepal Indosuez Bank Ltd, was established in 1986 as a joint venture between Nepalese and French partner.

The French partner holding 50% of the capital was Credit Agricole Indosuez, a subsidiary of one of the largest banking groups in the world. With the decision of Credit Agricole Indosuez to divest, a group of Nepalese companies acquired 50% of the holding Credit Agricole Indosuz in Nepal in April 2002. Thus, the shareholding structure comprises of a group of companies holding 50%, Rastriya Banijya Bank Nepal and Rastriya Beema Sansthan Nepal holds 15% share each and 20% share is held by general public.

Figure: 1.2
Share Structure of NIBL Ltd.



The name of the bank was changed to Nepal Investment Bank Ltd upon approval of the Bank's Annual General Meeting, Nepal Rastra Bank and Company Registrar Office. At present, till 5th January 2011, the bank has 41 branches in the country.

It has recently launched the "Premier Banking Cell" that caters to us its high net worth clients and renders consultancy services in taxation, legal, insurance and travel and tours. It also emphasizes a continuous effort made to provide prompt and convenient services to the customers by limiting the customer's turnaround time to fifteen minutes. The Bank has formed consortium of banks and financial institutions for issuance and acquiring of Visa products. It also

provides international banking. To increasing remittance disbursement, agents all over the country have been appointed. It strongly recognizes the important role of human resource in successfully meeting its business objectives. It has been focusing on improving the efficiency of employees by providing specialized technical training pertinent to their job /function. It has been constantly endeavoring to develop the skills set of employees to Empower them to provide excellent customer service.

It has been awarded the prestigious “Bank of the Year 2003”, “Bank of the year 2005” and “Bank of the year 2008” by the London-based Financial Times Groups. It is the first Nepali Bank to win this award three times in three years due to its remarkable achievement in the field of deposits, lending, profit, products, services, etc.

Some of the major objectives and scope of the bank are as below:

- To develop a customer oriented service culture with special emphasis on customer care and convenience.
- To increase market share by following a disciplined growth strategy.
- To leverage technology platform and open scalable systems to achieve cost-effective operations, efficient MIS, improved delivery capability and high service standards.
- To develop innovative products and services that attracts targeted customers and market segments.
- To continue to develop products and services that reduces cost of funds.
- To maintain a high quality asset portfolio to achieve strong and sustainable returns and to continuously build Shareholders’ value.
- To expand its branches and the ATM networks throughout the country.
- It plans to strengthen its position in products such as remittance and plastic money by joining hands with established Exchange Houses in Middle East and other banks and financial institutions.

- The Bank is in the Process of appointing more distributing agents to the existing fleet.
- Supporting projects ranging from steel and cement to mining.
- Financing hospitals, clinics and pharmaceuticals.
- Assisting the aviation industry and introducing innovative solutions such as e- ticketing via e- banking.
- Supporting hotels and tourism sector.
- Financing energy and water resources power projects.
- Financing agriculture commodities and fertilizers, tea estate, poultry, etc.

1.3 Statement of the Problem

With the adoption of liberalization, Nepal is also trying to accelerate economy. Though Nepal started planned economy in the year 1956, the pace of development is very slow. So, in regard to banking sector, it has been rightly said, “When a sector of economy catches cold, banking sector sneezes.” At present, banking in Nepal suffers from low economic growth. On the other, the global economic crisis created unemployment of Nepalese manpower abroad resulting low revenue as remittance amount. Except above, country’s political instability hampers banking business. There is unhealthy competition in this field. Energy crisis and labor unrest are hampering banking business, too. Apart from this, there are fraud cases occasionally.

There are many other problems that can be enlisted below:

- Inflation due to decrease in agriculture products.
- Improper ways of lending with weak collateral.
- Lack of Investment friendly atmosphere.
- Person’s saving capacity and investment awareness is low.
- Poor expansion of banking activities in rural and urban areas.
- Lack of required management efficiency.

Thus, the researcher is trying to find out following financial aspects of the MBL and NIBL, and they are:

How is the financial performance of MBL and NIBL?

Are both the banks maintaining sufficient liquidity?

Are both the banks in profitable position?

Do they have proper banking policies?

1.4 Objective of the Study

The main objectives of this study is to find out facts and figures of MBL and NIBL so as to understand or figure out financial position of these banks and make a comparative study. Thus, the objectives of the study are as follows:

- To analyze the financial performance of the aforesaid Banks by using different financial ratios like liquidity ratio, activity ratio, profitability ratio and solvency ratio.
- To analyze trend value of these two banks on the basis of total deposit, dividend per share and earnings per share.

1.5 Significance of the Study

Financial analysis will be beneficial to the respective management or the owners of the Machhapuchchhare Bank and Nepal Investment Bank Ltd. They will be able to analyze their weak and strong points. The liquidity position will be of interest to the trade creditors. Also, suppliers of long term debt can get information about the profitability overtime. Its ability to generate cash to make payments of interest and principal will be enhanced, and can create relationship between various sources of funds. The investors will be interested to know the firm's financial structure to the extent it influences the firm's earning ability and risk. They can also speculate as how to improve their position. Similarly, they will be able to trace the difference in its performances from its historical perspective to its present context. Besides, employees of the bank can gain from this report to know about the real profit, since it affects the bonuses and

other incentives. Thus, they can evaluate if they are being treated inappropriately in the payment matters. The government also will get proper information as regard to revenue collection. More or less, the customers and tourist, of course, can be benefited from it by having glimpse on its financial performance.

1.6 Scope of Study

The scope of this study lies mainly in filling research gap on the study of investment policy and financial performance of commercial banks. This study is basically confined to reviewing the investment policy of commercial banks in five fiscal years (2005/06 to 2009/10).

This study may provide feedback to the policy makers of commercial banks and also to the government and central bank in formulating appropriate strategies for improvement in performance of commercial banks.

The study aims to analyses both the banks financial performance. Financial tools and statistical tools have been used to check its liquidity status, investment, deposits and profits. In addition to that it's also been studied to see its earning on share values. These are some of the parameter based on which a bank's performance can be evaluated.

1.7 Limitations of the Study

There are few limitations that need to be acknowledged and addressed regarding the present study.

- The study mainly concentrates on the financial performance of MBL and NIBL.
- The financial analysis of the banks is carried out based on secondary data. They are mainly taken from annual reports of the respective banks.

- This study covers only last five years (2005/06 to 2009/10) trends and data.
- Time constraints may limit the areas covered by the study.
- This study deals with certain financial tools such as Ratio Analysis, EPS, and DPS analysis.

1.8 Organization of the Study

The whole study is divided into five chapters, which are as follows:

Chapter I: Introduction:

This chapter deals with General background of banking in Nepal. It also outlines introduction to Machhapuchchhare bank Ltd. and Nepal Investment Bank Ltd. This chapter also deals with the statement of the problem, objectives of the study, significance and its limitations and organization of the study.

Chapter II: Review of Literature:

This chapter deals with the review of literature, articles, thesis, and research papers.

Chapter III: Research Methodology:

This chapter deals with research methodology used, which includes research design, source of data, tools and techniques of analysis.

Chapter IV: Data Presentation and Analysis:

This chapter deals with presentation and analysis of data.

Chapter V: Summary, Conclusion, and Suggestions and Recommendations:

This chapter summarizes the study, deals with the conclusion, and provides suggestions and recommendations for improvement.

CHAPTER-II

REVIEW OF LITERATURE

This chapter has been divided into three parts: conceptual framework, review of journals and articles, and review of thesis.

2.1 Conceptual Framework

Review of Literature is stock thinking of available literature in own's field. This part of the study highlights available literatures related to this research which makes base of knowledge for the study.

2.1.1 Financial Planning

Financial analysis is not similar to financial planning. Financial Planning refers to the determination in advance of a future course of action. It involves analyzing the financial flows of a company forecasting the consequences of various investments. "Effective financial planning and control are central to enhancing enterprise value. Financial plans may take many forms, but any good plan must be related to the firm's existing strengths and weaknesses. The strengths must be understood if they are to be used to proper advantage, and the weaknesses must be recognized if corrective action is to be taken." (*Weston and Copeland; 9th Edition: 185*). The advantage of financial planning is that it forces management to take account of possible deviations from the firm's anticipated path towards success. The financial manager can plan future financial requirements in accordance with the forecasting and budgeting procedures.

The planning horizon depends on the company. Most firms have a horizon of at least 1 year. Many will produce detailed plans for 1 year and more and general financial plans for 3 to 5 years. Some companies will plan ahead, 10 or even more years.

2.1.2 Financial Statement

Much can be learnt about a firm from a careful examination of its financial statements as invaluable documents. A financial statement is an official document of the firm, which explores the entire financial information of the firm. Financial information is communicated through financial statements, and these statements are prepared from the accounting records maintained by the firm. “The financial statements provide a summarized view of the financial position and operations of the firm” (*Khan and Jain; 1993:79*).

2.1.3 Financial Analysis

“Financial statements contain a wealth of information which, if properly analyzed and interpreted, can provide valuable insights into a firm’s performance and position” (*Chandra;1990:112*). Financial Analysis is concerned with analyzing the financial statement of an enterprise. “Analysis of financial statements may be done for a variety of purposes, which may range from a simple analysis of short-term liquidity position of a firm to a comprehensive assessment of the strengths and weaknesses of the firm in various areas” (*Chandra; 1990: 112*). For financial analysis, the most important document is financial statements. These statements are required for management’s own evaluation and decision making.

Financial statements analysis is largely a study of relationship among the various financial factors in a business as disclosed by the statement, and a study of the trend of these factors. Financial analysis is to analyze the achieved statement to see, if the results meet the objectives of the firms to identify problems, if any in the past or present and/or likely to be in the future, and to provide recommendation to solve the problems. “Financial analysis is the process of identifying the financial strengths and weaknesses of the firm by properly establishing relationship between the items of the balance sheet and profit and loss account” (*Pandey; 1991: 109*).

“The focus of financial analysis is on key figures in the financial statements and its significant relationships that exist between them. The analysis of financial statements is a process of evaluating relationships between component parts of financial statements to obtain a better understanding of the firm’s position and performance” (*Khan and Jain; 1993: 79*). The first and foremost task of the financial analysis is to select the information relevant to the decision under consideration from the total information contained in the financial statement. The second step involved in financial analysis is to arrange the information in a way to highlight significant relationships. The final step is interpretation and drawing of inferences and conclusions. Thus, the process of financial analysis involves selecting the information, arranging information in a way to highlight significant relationship and finally the interpretation and drawing of conclusion. It is both the analytical and judgmental process that helps answer and question that have been posed. Therefore, it is a means to an end. Apart from the specific analytical answer, the solutions to financial problems and issues depend significantly on the view of the issue, and nature and reliability of the information available.

Analysis of financial statements is of interest to creditors, investors, managers and others. “The firm itself and outside suppliers of capital—creditors and investors—all undertake financial analysis.....” “In addition to suppliers of capital and the firm itself, various government regulations may use financial analysis” (*Van Horne; 1991: 752,753*). It may be done on a variety of purposes. The type of analysis varies according to the specific interests of the party involved.

Financial analysis examines relationships between two numbers to measure financial soundness, profitability, and efficiency. We will recognize two points in receiving and evaluating financial data.

- External Analysis: The outsiders perform this.

- **Internal Analysis:** The corporate finance and accounting department perform this in more detailed than the external analysis.

2.1.4 Objectives of Financial Analysis

The main objectives of financial analysis explain various facts related to the past performance of business and predict the potentials for achieving desired results. Some of the main objectives of financial analysis can be pointed out as follows:

- To understand the solvency of a firm in short term and long term.
- To know the present and future profitability of the firm.
- To compare performance with different firms.
- Forecast the future & preparing budget.
- The financial stability of business firm.
- The long term liquidity of its fund.

2.1.5 Techniques of Financial Statement Analysis

Financial statement analysis may be done for a variety of purposes.

Comparative Statement Analysis: Comparative statement analysis is an analysis of financial statement at different period of time. This statement helps to understand the comparative position of financial and operational performance at different period of time. Comparative financial statements again classified into two major parts such as comparative balance sheet analysis and comparative profit and loss account analysis.

i) Comparative Balance Sheet Analysis

Comparative balance sheet analysis concentrates only the balance sheet of the concern at different period of time. Under this analysis the balance sheets are compared with previous year's figures or one-year balance sheet figures are compared with other years. Comparative balance sheet analysis may be horizontal or vertical basis. This type of analysis helps to understand the real

financial position of the concern as well as how the assets, liabilities and capitals are placed during a particular period.

ii) Comparative Profit and Loss Account Analysis

Another comparative financial statement analysis is comparative profit and loss account analysis. Under this analysis, only profit and loss account is taken to compare with previous year's figure or compare within the statement. This analysis helps to understand the operational performance of the business concern in a given period. It may be analyzed on horizontal basis or vertical basis.

2.1.6 Types of Financial Statement Analysis

Financial statement analysis is interpreted mainly to determine the financial and operational performance of the business concern. A number of methods or techniques are used to analyze the financial statement of the business concern. The followings are the common methods or techniques, which are widely used by the business concern.

i) Trend Analysis

The financial statements may be analyzed by computing trends of series of information. It may be upward or downward directions which involve the percentage relationship of each and every item of the statement with the common value of 100%. Trend analysis helps to understand the trend relationship with various items, which appear in the financial statements. These percentages may also be taken as index number showing relative changes in the financial information resulting with the various period of time. In this analysis, only major items are considered for calculating the trend percentage.

ii) Common Size Analysis

Another important financial statement analysis technique is common size analysis in which figures reported are converted into percentage to some

common base. In the balance sheet the total assets figures is assumed to be 100 and all figures are expressed as a percentage of this total. It is one of the simplest methods of financial statement analysis, which reflects the relationship of each and every item with the base value of 100.

iii) Funds Flow statement

Funds flow statement is one of the important tools, which is used in many ways. It helps to understand the changes in the financial position of a business enterprise between the beginning and ending financial statement dates. It is also called as statement of sources and uses of funds. Institute of Cost and Works Accounts of India, funds flow statement is defined as “a statement prospective or retrospective, setting out the sources and application of the funds of an enterprise. The purpose of the statement is to indicate clearly the requirement of funds and how they are proposed to be raised and the efficient utilization and application of the same”.

iv) Cash flow Statement

Cash flow statement is a statement which shows the sources of cash inflow and uses of cash out-flow of the business concern during a particular period of time. It is the statement, which involves only short-term financial position of the business concern. Cash flow statement provides a summary of operating, investment and financing cash flows and reconciles them with changes in its cash and cash equivalents such as marketable securities.

v) Ratio Analysis

Alexander Wall is the pioneer of the ratio analysis. He prescribed a detailed system of ratio analysis in 1909, and explained that the work of interpretation could be made easier by establishing quantitative relationship between the facts given in the financial statements.

“To evaluate the financial condition and performance of a firm, the financial analyst needs certain yardsticks. The yardsticks frequently used are a ratio, or index, relating two pieces of financial data to each other” (*Van Horne; 1991:753*). Ratio analysis is such a powerful tool of financial analysis that through it economic and financial position of a business unit can be fully analyzed. It is a widely used tool of financial analysis. “It is defined as the systematic use of ratio to interpret the financial analysis statements so that the strengths and weaknesses of a firm as well as its historical performance and current financial condition can be determined” (*Khan and Jain; 1993; 80*).

Ratio is a mathematical relationship between one numbers to another number. Financial ratio analysis is a study between various items in financial statements. It is used as an index for evaluating the financial performance of the business concern. But “no one ratio gives us sufficient information by which to judge the financial condition and performance of the firm. Only when we analyze a group of ratios are we able to make reasonable judgments” (*Van Horne; 1991:755*). Ratio can be classified into various types. Classification from the point of view of financial management is as follows:

a) Liquidity Ratio

It is also called as short-term ratio. This ratio helps to understand the liquidity in a business which is the potential ability to meet current obligations. “Liquidity ratios are generally based on the relationship between current assets and current liabilities” (*Chandra; 1990; 114*). The following are the major liquidity ratio:

1. Current Ratio
2. Quick ratio

b) Activity Ratio

It is also called as turnover ratio or assets management ratio. This ratio measures the efficiency of the current assets and liabilities in the business

concern during a particular period. This ratio is helpful to understand the performance of the business concern. Some of the activity ratios are given below:

1. Stock Turnover Ratio
2. Debtors Turnover Ratio
3. Creditors Turnover Ratio
4. Working Capital Turnover Ratio

c) Solvency Ratio

It is also called as leverage ratio or capital structure ratio, which measures the long-term obligation of the business concern. This ratio helps to understand, how the long-term funds are used in the business concern. Some of the solvency ratios are given below:

1. Debt-Equity Ratio
2. Debt to total capital ratio
3. Interest Coverage Ratio
4. Total debt to total assets ratio

d) Profitability Ratio

“Profitability reflects the final result of business operations. There are two types of profitability ratio: profit margins ratios and rate of return ratios” (*Chandra; 1990: 119*). Profitability ratio helps to measure the profitability position of the business concern. Some of the major profitability ratios are given below.

1. Gross Profit Ratio
2. Net Profit Ratio
3. Operating Profit Ratio
4. Return in Investment

2.1.7 Need of Financial Analysis

The analysis of financial statement is mainly focused with some questions.

1. What is the present performance of the firm?
2. Which are the problems existing areas?
3. What will be the position of the firm in future? What are the projections?
4. Are there any likely problems in the future?
5. What are the recommendations?

2.1.8 Problems of Financial Statement Analysis

The followings are the problems of financial statement analysis:

- Development of bench marks: Difficult to find suitable benchmarks for evaluating their financial performance and condition.
- Window-dressing: Average level of inventory at just one point of time is suspected.
- Price level change: Profits are misreported as the price level changes.
- Variations in Accounting Policies: Due to diversity of accounting practices, comparative financial statement analysis may be vitiated.
- Interpretation of Results: Difficulty to judge whether a certain ratio is good or bad.

Correlation among Ratios: Some ratios have common element and some items tend to move in harmony because of a certain common underlying factor.

2.1.9 Legal Provision of Financial Statement Analysis

Country's policies, rules and regulations, government attitude towards a particular sector is to be studied under legal provisions of concerned field. Financial institutions are one of the most heavily regulated institutions of all business in the world. The followings are the important reasons behind the regulations of financial institutions: a) to safeguard of the public funds, b) to provide equal opportunities and fairness, and c) to control inflation and creation of money. Lots of countries established central bank to regularize and supervise

commercial banks of their own countries. Nepal also established Nepal Rastra Bank as a central bank of Nepal in 1956 under Nepal Rastra Bank act 1955, which empowered this NRB to have direct control over banking institutions within the country. The aforesaid act has been amended time to time. Since then, the NRB has been functioning as governments bank and contributed to the growth of country's financial sectors.

One of the main objectives of NRB is to regulate, inspect, supervise and control banking and the financial sectors with a view to develop confidence among the people for the entire banking and financial system. In this regard, NRB has given some directives to the commercial banks in relation to the capital adequacy ratio of a bank, classification of loan, loan depreciation (loss) provision and assessment of interest income, single borrower limit, liquidity, directive to credit, and asset quality and off balance sheet activities. NRB can ask clarification if compliance is not found in respect of loan classification and provisioning. In case NRB is not satisfied by the classification, a penalty can be levied on the amount involved to the bank. NRB issues written orders to stop a repeated violation, suspend or call of services of NRB, restrict dividend distribution, suspend acceptance of deposit and acceptance of credit, restrict partially or wholly the transaction of bank, suspend or cancel banking license and issue orders requiring to terminate services of directors/ staffs. To perform these duties, NRB use to conduct regulatory role, supervisory role and monitoring role.

2.2 Review of Journals and Articles

Review of journals and articles published in the following journals.

Shrestha (1990), in his article "*Commercial Bank's Comparative Performance Evaluation*", emphasizes on a proper risk management with appropriate classification of loans under performing and non performing category. He further clarifies that adequate provisioning is the surest way to get relief from

sinking loan after careful consideration of portfolio risk. A clear cut criterion is necessary to treat interest suspense account and it is advisable that all interest unpaid for more than six months need to be treated as unearned income.

Regarding the risk management of the bank, Shrestha suggests that:

- Any customer, having overdue loan of two years or more in his account, should not be given other loan facilities.
- Strong provisioning or reservations are required in restructuring portfolio related to overdue loans.
- All credits including overdrafts should be given a maturity date and should be subjected to revision at that date, and consequently categorize as good, substandard or doubtful loans.
- Financial credit worthiness of the borrower must be evaluated properly before granting loans.

Central Bank is an important financial institution in every sovereign independent state in modern times. It is the apex body of Banking System. Of the various banks, the most supreme bank is the central Bank. The central bank plays an important role in the economic development of a country. This bank is established to develop banking through strategy on its own to issue the notes, to control the credit, to act as the bank of banks, in each country. Central Bank is the lender of the last resort. Having felt the need of development of banking sector and to help the government formulate monetary policies, Nepal Rastra Bank (NRB)-central Bank, was set up in 1956. Since then, it has been functioning as the government's bank and has contributed to the growth of financial sector.

Commercial banks, including JVBs, established under the company Act 2021 may perform various functions aimed at ensuring the economic interests and convenience of the public, facilitating the supply of credit to agriculture, industry and commerce by making available the banking and financial services

to the people as mentioned in the preamble of the 2031 Commercial Bank Act, and subject to Nepal Rastra Bank Act 2012, Foreign Exchange Regulation Act 2019 along with the current Nepalese law.

He finds JVBs are new, operationally more efficient, have better performance in comparison to NBL and RBB. Better performance of JVBs is due to their sophisticated technology, modern banking methods and skills. State owned banks are efficient at rural sector however they are facing growing constraints from social, economic, political system as well as the issues and challenges from JVBs.

Salmi and Martikainen (1994), in their article, "*A Review of the Theoretical and Empirical Basis of Financial Ratio Analysis*", indicates financial ratios are widely used for modeling purposes both by practitioners and researchers. The firm involves many interested parties each having their views in applying financial statement analysis in their evaluations. Practitioners use financial ratios to forecast the future success of companies, while the researcher's main interest has been to develop models exploiting these ratios. Many distinct areas of research involving financial ratios can be discerned. There is overlapping in the observable themes, and they do not necessarily coincide with what theoretically might be the best-founded areas. The existing themes include:

- Distributional characteristics of financial ratios.
- Classification of financial ratios.
- Comparability of ratios across industries, and industry effects.
- Time-series properties of individual financial ratios.
- Bankruptcy prediction models.
- Explaining (other) firm characteristics with financial ratios.
- Stock markets and financial ratio.
- Forecasting ability of financial analysis vs. financial models.

Paudel (1996) has published an article in Nepal Rastra Bank Samachar entitled, “*Financial Statement Analysis: An Approach to Evaluate Bank Performance*”, which expresses that balance Sheet, Profit and Loss accounts and the accompanying notes are most useful aspects of the banks. But the users of the financial statements of the bank need reliable, relevant and comparable information which assist them in evaluating the financial position and performance of the banks which is useful in making economic decisions.

According to Paudel, the main objectives of analyzing financial statements of the banks are to identify;

- Liquidity.
- Profitability.
- Solvency.

He says that most of the users are interested in assessing bank’s overall performance which is affected by following factors:

- Overall efficiency and internal management system.
- Managerial decisions regarding interest rate, exchange rate and lending policies.
- Environmental changes like technologies, government policies, competition and economy.

Baral (2005) has published an article, entitled “*Health Check Up of Commercial Banks in the Framework of CAMEL: A Case Study of Joint Venture Banks in Nepal*”, in The Journal of Nepalese Business Studies.

The analysis of the study is entirely based on CAMELS framework. It is a common method for evaluating the soundness of FIs. Theoretical prescription of CAMELS framework has been described as:

C for Capital Adequacy- It determines how well FIs can manage with shocks to their balance sheets. Thus, it tracks capital adequacy ratios that take into

account the most important financial risks---foreign exchange, credit, and interest rate risks---by assigning risk weightings to the institutions assets.

A for Asset quality- The quality of assets held by FIs depends on exposure to specific risks, trend in nonperforming loans, and the health and profitability of borrowers. The health of commercial banks largely depends on the quality of assets hold by them, and quality of assets relies on the financial health of their borrowers.

M for Management- Sound management is a key to the performance of any organization, but is difficult to measure. It is primarily a qualitative factor applicable to individual institution. Several indicators can jointly serve as an indicator of management soundness.

E for earning quality- Earning capacity largely counts on the efficiency of management. Losses making commercial banks reduce their capital base, risk the solvency and eventually bring down the wealth of their shareholders. Conversely, profit making banks add equity to the total capital fund, reduce the risk of insolvency, and finally increase the wealth of their shareholders.

L for Liquidity- Liquidity risk threat the solvency of FIs. In the case of commercial banks, first type of liquidity risk arises when depositors of commercial banks seek to withdraw their money and second type does when commitment holders want to exercise the commitment recorded off the balance sheet.

S for sensitivity to market risk- Commercial banks are increasingly involved in diversified operations such as lending and borrowing transaction in foreign exchange, selling of assets pledged for securities and so on.

Findings:

Nepal Rastra Bank, as an apex monetary authority of Nepal, started to monitor and control the finance industry especially at the end of 1990 by issuing the directives to the financial institutions. NRB has skipped up the component of CAMELS in the performance evaluation of commercial banks and has adopted the CAEL system.

- NRB strictly directed all commercial banks that the amount of supplementary capital should not be in excess to the amount of the core capital.
- Public sector banks in Nepal are sustaining the loss during the study period. However, the private sector banks are earning the operating profit.
- Liquidity indicators of Joint venture banks show that they have stored high level of liquidity.

Diagnoses:

The researcher has prescribed following diagnoses after analyzing the health of Joint venture banks in Nepal in the framework of CAMEL.

- Capital of commercial banks in Nepal is negative due to heavy amount of negative capital of two public sectors—NBL and RBB. It is due to heavy accumulated losses.
- Quality of assets of joint venture banks on the average is satisfactory.
- Performance of management efficiency shows relatively healthy joint venture banks in Nepal.
- Earning profitability indicators show that financial health of joint venture banks is not so weak.

2.3 Review of thesis

Some relevant theses are briefly enumerated below. These theses are selected from the Shankar Dev Campus and Tribhuvan University libraries.

Sapkota (2000) has conducted a research in the topic of “*Risk and Return Analysis in Common Stock Investment*”, which includes eight commercial banks for his research.

Objectives:

The main objective of the study is to analyze the risk and return of the common stocks in Nepalese stock market. The study is focused on the common stock of commercial banks. It is found that banking industry is the biggest one in terms of market capitalization and turnover. Expected rate of return on common stock is maximum for Nepal Bank Limited and minimum for NSBI Ltd. In this regard, Common Stock of NBL is most risky and the same of NSBI Ltd is least risky. In the context of industries, expected return of finance and insurance industry is found highest. Expected return of banking industry is 60.83%.”

Findings:

He concludes that “Common stock is the most risky security and life blood of stock market because of the higher expected return, Common Stock attracts more investors. Private Common Stock holders are the passive owners of the company. But the private investors play a vital role in economic development of the nation by mobilizing the dispersed capital remained in different form in the society. As overall economy, Nepalese stocks market is in emerging state. Its development is accelerating since the political change in 1990 in effect of openness and liberalization in national economy. But lack of information and poor knowledge, Nepalese private investors cannot analyze the securities as well as market properly”.

Agrawal (2002) has conducted research on the topic “*A study on Deposit And Investment Position of Yeti Finance Company Limited.*” The study was conducted on the basis of secondary data and used various financial tools to analyze the data. Study just covered only period of 5 years (i.e. F/Y 1996/97 to 2000/2001).

Objectives:

He tried to examine the trend of the deposit position and investment position of the Yeti Finance Company.

Findings:

It was found that the deposit policy is not stable but has highly fluctuating trend and investment is gradually in increasing trend. The researcher found there is positive correlation between total deposit and total investment. The researcher concludes that finance companies have been found profit oriented, ignoring the social responsibility, which is not a fair a strategy to sustain in long run. Therefore, it is suggested that the company should involve in social program which helps the deprived people.

Tibrewal (2002) has studied “*Capital Structure and Profitability: A Comparative Study Between Nabil Bank and HBL*”.

Objectives:

The basic objectives of this study are to know the relationship between capital structure and value of the firm by analyzing the effect of financial leverage on the return and risk. This study also attempts to find out the relationship between capital structure and each of the selected explanatory variables such as size, growth, risk, return payout, liquidity and earning variability.

Findings:

The main findings of this study are:

- Fixed deposits of Nabil Bank is reducing, and average HBL fixed deposits are more than that of Nabil.
- Debt capacity of Nabil is higher than HBL as the interest coverage ratio of Nabil is higher than HBL.
- Capital adequacy ratio of HBL is found below the standard rate of 6% in all period. The Nabil is found higher than that of HBL.
- The proportion of shareholder's equity i.e. net worth in total claims of assets is found much lower in both Banks.

Sharma (April 2002) has conducted the thesis on the topic "*Profit planning in Commercial Bank*" (A case study of Nepal Bangladesh Bank Ltd.)

Objectives:

The main objective of this study is to appraise Nepal Bangladesh Bank Limited. Thus, the major objectives are: i) to highlight the current profit planning premises adopted and its effectiveness in NBBL, ii) to observe NBBL's profit planning on the basis of overall managerial budgets developed by the bank, iii) to analyze the variance of budgeted and actual achievement, iv) to study the growth of the business of the bank over the period, and v) to provide suggestion and recommendations for improvement.

Findings:

It is observed that the bank is adopting a policy to keep minimum number of employee as possible. But it has unnecessary long ladder at various levels without specific job description.

- NBBL is currently operating with its 15 branch offices making its presence at almost all of the cities of the country. It is one of the banks, having highest branch network among the joint venture private bank in Nepal.

- Objectives of the bank are expressed in literacy form, and not specified clearly; therefore there is a danger of it being misinterpreted in the ways of one's benefit by the concerned.
- Major concentration of resources mobilization of NBBL is at deposit mobilization. In this respect, they are incurring higher cost toward deposit mobilizations.
- Bank's resources development for non-yielding liquid assets (cash and Bank Balance) is increasing every year, which is detrimental to profitability objectives, but it is supportive to meeting liquidity requirements of the Bank.
- The interest expense of the bank is found increasing each year corresponding to the increase in deposit. The interest expenses are perfectly and positively correlated with deposit.
- Outstanding letter of credit liability of the Bank is increasing every year however the growth is not consistent.
- The amount of interest income is increasing every year.

Tiwari (2003) has submitted a thesis on "*A Profit Planning in Commercial Bank*" (A case study of Standard Chartered Bank Nepal Ltd.)

Objectives:

The main objective of this study is appraising Standard Chartered Bank Nepal Ltd. Thus the major objectives are:

- To highlight the current profit planning premises adopted and its effectiveness in SCBNL.
- To analyze the variance of budgeted and actual achievements.
- To study the growth of the Bank over the period.
- To provide suggestions and recommendations for improvements of the overall profitability of the bank.

Findings:

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

Loudari (2003) has conducted a study on “*A Study on Investment Policy of Nepal Indosuez Bank Ltd. in Comparison to Nepal SBI Bank Ltd.*”

Epal

Objectives:

- To examine the liquidity, asset management and profitability position and investment policy of Nepal Indosuez Bank Ltd in comparison to NSBI Ltd.
- To study the growth ratios of loans and advances and investment to total deposit and net profit of Nepal Indosuez Bank Ltd in comparison to NSBI Ltd.
- To analyze relationship between deposit and investment, deposits and loan & advances, net profit and outside assets of Nepal Indosuez Bank Ltd. in comparison to NSBI Ltd.

Findings:

The research findings of the study are as follows:

- Current ratios for both the banks are satisfactory.
- NSBI Ltd. has increased investment in government securities whereas Nepal Indosuez Bank Ltd has decreased.
- Nepal Indosuez Bank Ltd. has maintained both current ratio and cash reserve ratio better than NSBI Ltd. But its cash and bank balance, investment in government securities and loan and advances in comparison to current assets are lower than that of NSBI Ltd.
- Deposit utilization of Nepal Indosuez Bank Ltd. is less effective than that of NSBI Ltd.
- Indosuez Bank Ltd. did a better performance in return on total assets and loan and advances and interest earning, but it paid lower interest amount to working fund.
- The analysis of growth ratios shows that growth ratios of total deposit, loan and advances, total investment and net profit of Nepal Indosuez Bank are less than that of NSBI Ltd.
- The trend value of loan and advances to total deposits ratio is decreasing in case of both banks. The trend value of total investment to total deposits ratio is also decreasing in case of both banks.

Lamsal (2004) made “*A Comparative Financial Statements Analysis of HBL and NGBL*”. He used financial tools like ratio analysis and statistical tools like CV, SD, trend analysis, hypothesis tests in his study.

Objectives:

- To make comparative study on financial performance of the selected banks.
- To evaluate the liquidity position of these selected banks.
- To analyze the resource position of these banks.

Findings:

- The liquidity position of the HBL is better than NGBL.
- HBL has sufficient cash and bank balance to meet its current and fixed deposits.
- HBL has better turnover than NGBL in terms of loan and advances to total deposits ratios.
- Investment to total deposit ratio of NGBL is better than HBL.

Shrestha (2004) conducted thesis entitled on “*Role of Rastriya Banijya Bank in Priority Sector Credit & its Recovery.*”

Objectives:

- To identify the compliance of the target loan limit to be invested in priority sector credit as prescribed by NRB.
- To analyze the relationship of credit (loan & advances) with total deposit & also with Priority Sector Credit of RBB.
- To examine the situation of deprived sector credit of RBB.
- To analyze the disbursement, recovery status & NPA position under Priority Sector Credit of RBB purpose wise.

Findings:

- Bank’s total no. of borrowers in PSC is about 76 % to 78 % whereas borrowers under DSC are about 28 % to 29 %.
- RBB is very much success in complying the NRB policy.
- Bank is not able to fully utilize the collected deposits in a proper way.
- The study reveals that the disbursement & recovery under DSC is in decreasing trend. However, the ratio of repayment to disbursement is in increasing trend. Loan repayment under DSC is more satisfactory from industry sector, agriculture sector & services sector.
- The trend values of recovery of RBB under PSC shows that the recovery position of the bank is in downward sloping whereas its overdue loan under PSC is in increasing trend which brings no return to the bank.

Shrestha (2005), in his thesis "*Financial Performance Analysis of Nepal Bangladesh Bank ltd*", has used various financial research and statistical tools to achieve the objective of the study. The analysis of data will be done according to the pattern of data available. Likewise, some financial tools such as ratio analysis and trend analysis have also been accomplished.

Objectives:

- To analyze the functions, objectives procedure and activities of the Nepal Bangladesh bank Ltd.
- To analyze the lending practices and resources utilizations of Nepal Bangladesh bank.
- To determine the impact of growth in deposit on liquidity and lending practices.
- To examine the lending efficiency and its contribution to profit.
- To make suitable suggestions based on the findings of this study. The financial and statistical tools are used.

Findings:

- The researcher found that Nepal Bangladesh bank has sufficient liquidity. It shows that bank has not got investment sectors to utilize their liquid money.
- Nepal Bangladesh bank has utilized most funds in the form of credit and advances. More than 75% of total deposits of the bank have been forwarded to customers as a credit and advances.
- The major part of utilizing deposits and income generating sectors. If the bank has high deposits, bank can provide money to its customers as credit and advances. Therefore, there is highly positive correlation between total deposits and credit and advances of Nepal Bangladesh bank.
- Bank is providing different schemes to attract good customers. After

attracting deposits from the customers, bank has issued the deposits to the needy area to make profit for the bank.

Gautam (2006) has conducted research on "*A Comparative Study on Financial Performance of Standard Chartered Bank Nepal Limited and Nepal Bangladesh Bank Limited*". He analyzes financial performance with two important tools. These tools are the financial tools which include ratio analysis and other is statistical tools.

Objectives:

- To study the existing capital structure of financial position of selected joint venture commercial banks and to analyze its impact on the profitability.
- To access the debt servicing of the joint venture commercial bank.
- To examine the correlation and the signification of their relationship between different ratios related to capital structure.
- To provide suggestions and recommendations for the optimal capital structure of the joint venture commercial bank.
- To obtain the objectives, some financial, statistical and accounting tools.

He has found that the joint venture banks are operating in Nepal as commercial merchant banks. The growth is still going on as so many new banks are coming into existence after this study.

JVBs are operating with higher technology and new efficient methods in banking sector. However, this study has undertaken only few JVBs to examine and evaluation the financial data.

Findings:

- The research sample JVBs has used is high percentage of total debt in raising the assets. The higher ratio constitutes that the outsider's claim in

total assets of the bank is owner's claim. On an average, NBBL bank constitutes 16.27 times of P/E ratio, which should be reduced as quickly as possible. NBBL average degree of financial leverage constitutes 3.73 times which indicates the higher degree of financial risks.

- The average ROE of JVBs i.e. SCBNL and NBBL are 37.36% and 21.75% respectively.

Joshi (2007) has conducted thesis on "*A Comparative Study on Financial Performance of Nabil Bank Ltd. and Nepal Bangladesh Bank Ltd.*" The main objective of the study is to know the financial condition, financial performance and financial growth of Nabil and NBBL.

Objectives:

- To examine the EPS and DPS of Nabil and NBBL.
- To analyze the efficiency of Nabil and NBBL in utilizing the assets.
- To evaluate the trend of net profit of the concerned banks.

Findings:

- The overall liquidity position of NBBL is stronger than that of Nabil.
- Similarly, capital adequacy position of Nabil is found to be better than that of NBBL.
- According to profitability analysis, Nabil is found sound profitability due to its higher ratio. Also, other indicators, as EPS and DPS, are found sharply higher in Nabil.
- Nabil should keep only the reasonable amount of liquidity, which will save the bank from creating low return; NBBL should improve its capital adequacy by investing the assets and deposits in highly returnable sector; Nabil should invest its deposit in profit generating sectors.

Luitel (2007) has conducted research on “*A comparative Analysis of Financial Performance of the Joint Venture Banks*” with the objectives:

Objectives:

- To emphasize about the growth, objectives, functions and role of the commercial JVBs.
- To inform about the major regulations, such as NRB Directives, Govt. policy and other policies that govern these Banks.
- To evaluate whether the selected JVBs are efficient to face the challenges.

Findings:

- Though the Loan Loss Provisions are under the standard norms, Nabil & HBL are with excessive loan loss provisions as compared to SCBNL. Therefore, they are suggested to evaluate the financial positions of their borrowers in a more proficient way thereby identifying possibilities of risks prior granting the loans.
- Higher costs to income ratio in case of HBL and Nabil are the primary cause for the lower profit before tax. So, they should reduce operating costs to achieve the operational efficiency.
- As Loans & Advances of HBL & Nabil are in the higher volume as compared to SCBNL, SCBNL should try to increase its credit portfolio by exploring the productive sectors.
- In case of all three, JVBs, debt financing has always almost exceeded 90 % of the Total Assets over the review period, which indicates the excessively geared capital structure of these banks. This shows the excessive use of debt to finance Total Assets.
- Financial figures should show a consistency in their respective growths. The financial records observed in all these chosen JVBs are rather erratic. Therefore, all these banks are suggested to predict a more accurate data in order to remain in the same position and to advance ahead.

- In order to generate more capital for the development of the economy, more deposit needs to be collected by the financial institutions. For this, the selected JVBs are suggested to quote higher deposit interest rate as far as possible.

Pandey (2008) has studied on “*A Study on Profit Planning of Commercial Bank*” as comparative study of Bank of Kathmandu and Himalayan Bank Ltd.

Objectives:

- To highlight the current profit planning premises adopted and its effectiveness in HBL and BOK.
- To analyze the variance of budgeted and actual achievements.
- To study the growth of the business of the Banks over the period.
- To provide suggestions and recommendations for improvements of the overall profitability of the banks.

Findings:

Various analyses have been done, and the findings of this study are as follows:

A) In the management part:

- Job description and responsibility assignment should be clearly mentioned.
- Employee training at advance level should be given.
- Manpower should be updated with the changing practice and the technologies.
- Form a specific planning and research department.
- Objectives of both banks should be clearly defined.

B) In the business part:

- The deposit collection of HBL is not satisfactory.
- The average cost of deposit of BOK is higher than HBL.
- Correlation between interest expenses and deposit of HBL is negative.

- Expenses should be optimized and should be related with income generating activities of the banks. The banks have to put more focus on the other kind of non-funded activities.
- The liquidity positions in terms of current ratio of both banks are below normal standard.
- Net profit of the HBL is higher than BOK during the study period.
- Profitability position of HBL in term of net profit to total assets, net profit to shareholder equity and net profit to loan & advance are better than BOK.
- It is essential to exercise a suitable mechanism through which the overdue loan can be recovered within time.

Bhattacharai (2010) has conducted a research on '*Financial Performance Analysis of Commercial Banks*' with reference to Kumari Bank Ltd and Nepal Bangladesh Bank Ltd.

Objectives:

- To analyze the firm performance through the use of appropriate financial tools.
- To highlight various aspects related to the both Banks for a period of 5 years.
- To solve the course of change in cash position of these two banks at two balance data.
- To suggest and recommend with the banks to improve their firm performance.

Findings:

- Both banks have very low liquidity position because the current ratios are below the standard.

- The investment positions of KBL and NBBL, out of its total deposit are not satisfactory.
- Both banks have provided more loans and advance from it's saving, fixed, and total deposit.
- Steps should be step forwarded to develop satisfied and well-trained employees.
- Rules and regulations are the guidelines.

Hamal(2010) has conducted her study on “*Comparative Financial Performance Analysis of Nepal Investment Bank Ltd and Himalayan Bank Ltd.*”

Objectives:

- To compare and analyze various ratios between NIBL and HBL.
- To examine the relative financial performance of both Banks.
- To perform trend analysis of these Banks and make a projection of these banks for 5 years.
- To provide meaningful suggestions for improvement in financial performance.

Findings:

- The current ratio of the two banks, NIBL and HBL is considerable. This can be regarded as good liquidity position.
- It has been found that loan & advances to total deposit ratio of HBL is lower than that of NIBL. It means NIBL has not properly used their existing fund as loan & advances.
- NIBL and HBL have a possible risk because there is large amount of doubtful loan & advances and risky investment.
- Both the banks are recommended to formulate and implement the sound and effective investment portfolio to increase volume of total investment and loan & advances.

- Both companies have earned more income from interest income. So both have to increase their revenue through other banking activity for long-term survival and to avoid bad debt risk.
- Both banks should be careful in increasing profit of the shareholders, depositors and all its customers.
- Both banks have to expand its services in the rural area so that the people in the rural areas will also be able to have the facilities provided by the bank. The banks are suggested to improve its management structure to increase the efficiency. In order to win the heart of the client. They should be given desired facility and deal with maximum courtesy.
- NRB has given directives to financial institution to invest their certain percentage of investment in deprived and priority sector.

Keeping all these in consideration, the HBL has little less performance than that of NIBL. Therefore, in the future ahead, the HBL should improve its weaknesses by adopting the innovative approach to marketing. In the light of growing competition in the banking sector both banks NIBL and HBL should be customer oriented. It should strengthen and activate its marketing function by providing new facilities to the customers at competitive prices.

Research Gap

The previous researchers have covered the liquidity position, leverage ratio, profitability ratio, activity ratio, trend analysis, financial situation as their main objectives. Some researchers have also examined the existing financial situation. They have used the tools like trend analysis to compare sales and net profit etc. and other tools. But some of them have left or missed the tools like correlation analysis.

The present researcher has focused on various objectives like correlation analysis with sales and profit to evaluate liquidity management and profitability

position, risk position to examine the existing financial situation, and also to evaluate coefficient of correlation, probable error ratio of sales and net profit. So this research is completely my original work.

CHAPTER-III

RESEARCH METHODOLOGY

Research methodology deals with the road map of the study. It deals with the way the data are being collected, analyzed, figured out and necessary conclusion and recommendation is made. It is a way of systematic, organized database, critical scientific enquiry or investigation into a specific problem and finding solution. The research work will use different methods. The data used for the study will be secondary in nature and collected through bank annual reports, profit and loss account and balance sheets of the bank.

3.1 Research Design

Before examining the types of research designs, it is important to be clear about the role and purpose of research design. We need to understand what research design is and what it is not. We need to know where design fit into the whole research process from framing a question to finally analyzing and reporting data.

There are two types of research problems: those which relate to states of nature and those which relate to relationships between variables. The research problems have been formulated in clear cut terms; we are required to prepare a research design. Research design is concerned with the collection and analysis of data that are relevant towards meaningful findings of the study.

Descriptive, exploratory and analytical research designs have been used in this study. Collected data is simply explored by using selected financial as well as statistical tools.

3.2 Population and Sample

The population or the universe of the study is 31 banks in Nepal with 966 branches till Nov-2010. The 31 numbers of banks are as follows:

- Nepal Bank Ltd.
- Rastriya Banijya Bank.
- Nabil Bank Ltd.
- Nepal Investment Bank Ltd.
- Standard Chartered Bank Nepal Ltd.
- Himlayan Bank Ltd.
- Nepal SBI Bank Ltd.
- Nepal Bangladesh Bank Ltd.
- Everest Bank Ltd.
- Bank of Kathmandu Ltd.
- Nepal Credit and Commerce Bank Ltd.
- Nepal Industrial and Commerce Bank Ltd.
- Lumbini Bank Ltd.
- Machhapuchchhre Bank Ltd.
- Kumari Bank Ltd.
- Laxmi Bank Ltd.
- Siddhartha Bank Ltd.
- Agricultural Development Bank Ltd.
- Global Bank Ltd.
- Citizens Bank Ltd.
- Prime Commercial Bank Ltd.
- Sunrise Bank Ltd.
- Bank of Asia Nepal Ltd.
- Development Credit Bank Ltd.
- NMB Bank Ltd.
- Kist Bank Ltd.

- Janata Bank Nepal Ltd.
- Mega Bank Nepal Ltd
- Commerz and Trust Bank Ltd.
- Civil Bank Ltd.
- Century Commercial Bank Ltd.

Among them, Machhapuchchhare Bank Ltd. and Nepal Investment Bank Ltd. have been selected for comparative study. The sampling technique used in this study is the judgmental. Thus, financial statements of these banks for five years (2005/ 06 to 2009/10) have been taken as samples for the same purpose.

3.3 Sources of Data

Data collection could be done either by using primary source or secondary source or the optimum combination of both sources. Both primary and secondary sources of data collection methods are used in this study. The data collection sources are described in the upcoming section.

For the purpose of study only the secondary data are used. The required data and information for analysis are collected from the annual reports of the respective banks. Some other supplementary data are also collected from various sources as mentioned below,

- Published reports of the bank.
- Published and unpublished bulletins, reports of the Nepal Stock Exchange.
- Previous studies and reports.
- Unpublished official records.
- “Banking and Financial Statistics” report of Nepal Rastra Bank Magazines.

- Journals and other related documents and reports from the Central Library of T. U., Library of Shanker Dev Campus, Library of Nepal Commerce Campus and Library of Nepal Rastra Bank.
- Various Internet Websites.

3.4 Method of Data Analysis

Mainly financial methods are applied for the purpose of this study. Appropriate statistical tools like, correlation analysis, has been used as a major tools for the study. To make the study more specific and reliable, the researcher uses two types of tool for analysis.

- a) Financial tools
- b) Statistical tools

For the purpose of analysis, financial statements like profit and loss account, balance sheet and cash flow statement of the concerned banks have been taken.

3.4.1 Financial Tools

Various financial tools have been used for the study. The main tools used are ratio analysis, total investment and total income analysis.

Ratio Analysis

Ratio analysis is a tool used by individuals to conduct a quantitative analysis of information in a company's financial statements. Ratios are calculated from current and previous year's numbers to judge the performance of the company. Ratio Analysis compares significant numbers from financial statements.

Ratio analysis is a widely used tool for financial analysis. It is defined as the systematic use of ratio to interpret the financial analysis statements so that the strengths and weaknesses of a firm as well as its historical performance and current financial condition can be determined.

The following financial ratios are used in this research.

i. Liquidity Ratio

A liquidity ratio measures bank's ability to meet short term liabilities. The denominator of a liquidity ratio is the company's current liabilities, i.e., obligations that the company must meet soon, usually within one year. These ratios are mainly used to evaluate the financial position of the banks. Because current assets are expected to be converted to cash within one year, this liquidity ratio includes assets and liabilities of equal longevity.

The most common liquidity ratio is the current ratio, Cash and bank balance to total deposit ratio, Cash and Bank Balance to Current Assets Ratio.

a. Current Ratio

The current ratio is the most commonly used measures of short term solvency, since it indicates the extent to which the claims of short term creditors are covered by the assets that are expected to be converted to cash in a period roughly corresponding to the maturity of the claims. The current ratio is quantitative relationship between current assets to current liabilities.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} \text{ (times)}$$

The two basic components of this ratio are current assets and current liabilities. Current assets include cash and those assets which can be easily converted into cash within a short period of time, generally, one year, such as marketable securities or readily realizable investments, bills receivables, sundry debtors, (excluding bad debts or provisions), inventories, work in progress, etc. Prepaid expenses should also be included in current assets because they represent payments made in advance which will not have to be paid in near future.

Current liabilities are those obligations which are payable within a short period of time, generally, one year and include outstanding expenses, bills payable, sundry creditors, bank overdraft, accrued expenses, short term advances, income tax payable, dividend payable, etc.

b. Cash and bank balance to total deposit ratio

Cash and bank balances are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositor. Cash and Bank Balance to Total Deposit Ratio indicates the bank ability to meet their daily requirement of depositors. Higher ratio shows the greater ability of the firms to meet customer demands on their deposits. This ratio can be computed by dividing cash and bank balance by total deposit, and can be presented as:

Cash & Bank Balance to Total Deposit Ratio

$$= \frac{\text{Cash \& Bank Balance}}{\text{Total Deposit}} \text{ (times)}$$

Cash and bank balance includes cash in hand, foreign cash in hand, cheques and other cash items, balance with domestic and foreign banks. The total deposit includes deposits made by customers through different accounts like current (demand deposit), saving, fixed deposit, call deposit and other deposit accounts.

c. Cash and Bank Balance to Current Assets Ratio

It is represented by cash and near cash items. It is a ratio of absolute liquid assets to total current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositor. In the computation of this ratio only the absolute liquid assets are compared with the liquid liabilities. The absolute liquid assets are cash, bank and marketable securities. It is to be observed that receivables e.g. debtors/accounts receivables

and bills receivables are eliminated from the list of liquid assets in order to obtain absolute liquid assets since there may be some doubt in their liquidity.

$$\text{Cash \& Bank Balance to Current Assets} = \frac{\text{Cash \& Bank Balance}}{\text{Current Assets}} \text{ (times)}$$

Cash and Bank Balance are the most liquid or quick assets. Cash and bank balance to current assets ratio represents the liquidity capacity of the firms as per cash and bank balance. Higher the ratios, better the ability of the firms to meet the daily cash requirement of their customers. But high ratio is not so preferred to the firms because firms have to manage the cash and bank balance to current asset ratio in such manner that firm may not be paid interest on deposits and may not have liquidity crisis.

ii. Assets Management Ratio or Activity Ratio or Turnover Ratio

Asset Management Ratios attempt to measure the firm's success in managing its assets. For example, these ratios can provide insight into the success of the firm's credit policy and inventory management. In another word, asset management ratio measures the proportion of various assets and liabilities in balance sheet. The proper management of assets and liability ensures its effective utilization. The banking business converts the liability into assets by way of its lending and investing functions.

a. Loans and Advances to Total Deposit Ratio

This ratio shows the bank how they invested in loans and advances to total deposit. This ratio can be calculated in this way. Greater ratio implies better utilization of total deposits. This ratio is also known as credit deposit ratio. This ratio can be obtained by dividing loans and advances by total deposit as under;

$$\text{Loans \& Advances to Total Deposit Ratio} = \frac{\text{Loans \& Advances}}{\text{Total Deposit}} \text{ (times)}$$

This ratio actually measures the extent to which the banks are successful to mobilize the total deposit on loans & advances for the purpose of profit generation. A higher ratio of loans & advances indicates better mobilization of collection deposit and vice-versa. But it should be noted that too high ratio might not be better from its liquidity point of view.

b. Total Investment to Total Deposit Ratio

Investment is one of the major forms of credit creation to earn income. This implies the utilization of firm's deposit on investment on government securities, shares and debentures of other companies and banks. This ratio can be calculated by total investment divided by total deposit as:

$$\text{Total Investment to Total Deposit Ratio} = \frac{\text{Total Investment}}{\text{Total Deposit}} \text{ (times)}$$

Commercial banks and financial companies invest their collected funds in various governments' securities and other financial or non-financial companies. This ratio measures how successfully and efficiently the banks are mobilizing their funds on investment in various securities.

c. Loans & Advances to Total Assets Ratio

It indicates the part of total assets which has been utilized as loans and advances. Loans and advances is the major component in the total assets, which indicates the ability of bank to utilize its deposits in the form of loans and advances to earn high return. This ratio is calculated:

$$\text{Loans & Advances to Total Asset Ratio} = \frac{\text{Loans & Advances}}{\text{Total Asset}} \text{ (times)}$$

A commercial bank's working fund plays very active role in profit generation through fund mobilization. This ratio reflects the extent to which the banks are successful in mobilizing their total assets on loans & advances for the purpose

of income generation. A high ratio indicates better mobilization of funds as loans and advances and vice-versa.

iii. Profitability Ratio

It is a financial metrics that help investors assess a business's ability to generate earnings compared with its expenses and other relevant costs incurred during a specific period. When these ratios are higher than a competitor's ratio or than the company's ratio from a previous period, this is a sign that the company is doing well.

Every firm is most concerned with its profitability. One of the most frequently used tools of financial ratio analysis is profitability ratios which are used to determine the company's bottom line. Profitability measures are important to company managers and owners alike. If a small business has outside investors who have put their own money into the company, the primary owner certainly has to show profitability to those equity investors. Profitability ratios show a company's overall efficiency and performance.

The profitability of the bank should also be evaluated in term of its investment in assets and in term of capital contributed by creditors.

a. Return on Loans & Advances

Return on Loans and Advances measures a bank's net operating profit as a percentage of the leverage that they are using. This ratio helps to measure the earning capacity of selected banks.

The bank has to mobilize its resources in the form of loans and advances to make profit. To measure how efficiently a bank has utilized its fund, return on loans and advances ratio is calculated. This ratio also measures the earning capacity of its loans and advances. This ratio is computed by dividing net profit/loss by loans and advances as shown below.

$$\text{Return on Loans \& Advances} = \frac{\text{Net Profit(Loss)}}{\text{Loans \& Advances}} (\%)$$

b. Return on Total Assets Ratio (ROTA)

Return on Total Assets Ratio measures the profitability with respect to the total assets. This ratio is calculated to measure the profitability of all the financial resources invested in the Bank's Assets. The higher 'Return on Assets' ratio reflects the efficiency of the bank in utilizing its overall resources. A higher ratio also indicates the lower volume of nonperforming assets employed by the bank. Nonperforming assets are very harmful for the bank, so they should try to reduce their proportion in the assets structure. Return on Total Assets measures a company's EBIT against its total net assets. The ratio is considered as an indicator of how effectively a company is using its assets to generate earnings before contractual obligations is to be met. The greater a company's earnings in proportion to its assets (and the greater the coefficient from this calculation), the more effectively that company is said to be using its assets.

This ratio can be calculated as

$$\text{Return on Total Asset} = \frac{\text{Net Profit(Loss)}}{\text{Total Assets (Working Fund)}} (\%)$$

This ratio shows the relationship between bank's net profit and assets.

c. Return on Net worth or Equity Ratio

This ratio represents the relationship of net profit and assets, and this ratio shows that the investments in the banks are favorable or unfavorable. The Return on Net worth/Equity ratio is one of the most important of all the financial ratios for the companies. It reflects the extent to which the bank has been successful to mobilize or utilize its equity capital. A higher ratio indicates

higher successful mobilization of its owned capital and vice-versa, as it shows that the bank is doing a good job using the investors' money.

Any firm or bank must maximize shareholders' wealth by earning an adequate return on the shareholder's fund. Return on Net worth ratio expresses the capacity of the banks to utilize its owner's fund. This ratio is a strong indicator as it judges whether the firm has earned a satisfactory return for its equity-holders or not. It reveals how well the firm has deployed the resources of the owners to earn profit. So, higher the ratio, the more favorable it is for the stockholders which represents the sound management and efficient mobilization of the owners' equity.

The ratio can be calculated in this way

$$\text{Return on Equity} = \frac{\text{Net Profit(Loss)}}{\text{Total Equity Capital}} (\%)$$

d. Total Interest Earned to Total Assets Ratio

Income from interest is the major portion for a bank's revenue. To find out up to what extent a bank has been able to earn interest on its total assets (working fund). Higher ratio implies better performance by the banks in terms of interest earning on its total working funds. This ratio is computed by dividing total interest earned by the total assets of the bank and expressed as follow.

$$\text{Interest Earned on Total Assets} = \frac{\text{Interest Income}}{\text{Total Assets}} (\text{Times})$$

Total interest earned to total assets ratio evaluates how successful the selected banks are mobilizing their total assets to achieve high amount of interest. Higher the ratio indicates, higher the interest income.

e. Return on Total Deposit Ratio

This ratio is computed by net profit after tax divided by total deposits. This ratio indicates the relation & net profit earned by bank with the total deposits accumulated. Since deposits collected by the bank are the major resource of funds, these collected deposits have to be mobilized into loans and advances in the efficient way so as to maximize their return on deposits. It evaluates the bank in proper mobilization and utilization of deposits in generating profit. This ratio can be calculated as:

$$\text{Return on Total Deposit} = \frac{\text{Net Profit(Loss)}}{\text{Total Deposit}} (\%)$$

The ratio of commercial bank measures the degree of NPAT earned by using the total deposit. This ratio shows how efficiently the management is utilizing its deposit in profit generating activities. This ratio is a mirror for bank's overall financial performance as well as its success in profit generation. The deposits made by its customers are the major source of earning of the commercial banks by efficient and effective utilization.

iv. Capital Structure Ratio (Solvency Ratio)

Capital structure ratio measures bank's capacity of borrowings as a means of capital accumulation. It measures a long term solvency of a bank. The combination of capital structure is debt and equity of banks. The ratio indicates the long term financial position.

a. Debt to Equity Ratio

This ratio represents the relationship between debt capital and equity capital. This ratio reflects the relative claims of creditors and shareholders against the assets of the firm. The higher ratio indicates risk to the bank.

This ratio is calculated in this way

$$\text{Debt to Equity Ratio} = \frac{\text{Total Debts}}{\text{Shareholder's Equity}} \text{ (Times)}$$

b. Total Debt to Total Assets Ratio

This ratio shows the portion of capital assets that are financed by outside funds on total assets. A high ratio implies a bank's success in exploiting debt to more profitable and riskier capital structure. It is calculated by dividing total debts by total assets.

$$\text{Debt to Total Assets Ratio} = \frac{\text{Total Debts}}{\text{Total Assets}} \text{ (Times)}$$

c. Interest Coverage Ratio

This ratio is calculated by dividing earnings before interest and tax by interest. This ratio shows the bank can pay the interest easily.

$$\text{Interest Coverage Ratio} = \frac{\text{Earning Before Interest and Taxes}}{\text{Interest}} \text{ (times)}$$

v. Other Ratios

In addition to above described ratios, some other ratios have also been computed which are outlined as below.

a. Earnings per Share (EPS)

Earnings per Share are the portion of a company's profit allocated to each outstanding share of common stock. Earnings per share serve as an indicator of a company's profitability. Shareholders are concerned about the earning that will eventually be available to pay them dividends of that are used to expand their interest in the firm because the firm retains the earning. This ratio is calculated the following formula

$$\text{EPS} = \frac{\text{Earning available to Common Shareholders}}{\text{No of Outstanding Share of Common Stock}} \text{ (Rs.)}$$

b. Dividend per Share (DPS)

Dividend means that portion of net profit, which is allocated to shareholders as their return in term of cash. EPS implies what the owners are theoretically entitled to get from the company. Dividend per Share is the sum of declared dividends for every ordinary share issued. Dividend per share is the total dividends paid out over an entire year (including interim dividends but not including special dividends) divided by the number of outstanding ordinary shares issued.

This ratio is calculated as:

$$\text{DPS} = \frac{\text{Earning paid to Shareholders}}{\text{No of Outstanding Share of Common Stock}} \text{ (Rs.)}$$

c. Earnings Ratio

It is a ratio of earning per share to market value per share. The earnings ratio can be used to compare the earnings of a stock, sector or the whole market against bond yields. Generally, the earnings yields of equities are higher than the yield of risk-free treasury bonds reflecting the additional risk involved in equity investments.

$$\text{Earning Ratio} = \frac{\text{Earning Share}}{\text{Market Value per Share}} \text{ (Times)}$$

Earnings ratio is the earning per share for the most recent 12-month period divided by the current market price per share. The ratio is also known as earning price ratio.

d. Divided Yield

Divided Yield is a financial ratio that shows how much a company pays out in dividends each year relative to its share price. In the absence of any capital gains, the dividend yield is the return on investment for a stock. The dividend yield or the dividend-price ratio on a bank's stock is the company's annual

dividend payments divided by its market value, or the dividend per share, divided by the price per share. It is often expressed as a percentage. This can be calculated as:

$$\text{Dividend Yield} = \frac{\text{Dividend Per Share}}{\text{Market Value per Share}} (\%)$$

e. Price Earnings Ratio (P/E Ratio)

The PE ratio (price-earnings ratio) of a stock is a measure of the price paid for a share relative to the annual net income or profit earned by the bank per share. PE is a financial ratio used for valuation: a higher PE ratio means that investors are paying more for each unit of net income, so the stock is more expensive compared to one with lower PE ratio. In other words, PE ratio shows current investor demand for a company share. The reciprocal of the PE ratio is known as the earnings yield. It is a valuation ratio of a company's current share price compared to its per-share earnings.

$$\text{Price Earning Ratio} = \frac{\text{Market Value of Share}}{\text{Earning Per Share}} (\text{times})$$

A high PE suggests that investors are expecting higher earnings growth in the future compared to companies with a lower PE. However, the PE ratio doesn't tell us the whole story by itself. It's usually more useful to compare the PE ratios of one company to other companies in the same industry, to the market in general or against the company's own historical PE.

3.4.2 Statistical Tools

To analyze the data, various statistical tools can be used. Every researcher has to choose the most important and suitable tools to reach the financial decision. In this study the following statistical tools have been used

- i) Co-efficient of variance
- ii) Least square liner trend

i. Co-efficient of Variance

Co-efficient of variance is the relative measure of dispersion comparable across distribution, which is defined as the ratio of the standard deviation to the mean express in percent (*Levin, and Rubin; 1994:144*)

Co-efficient of variance denotes by C.V. is given by:

$$CV = \frac{\sigma}{\bar{x}}$$

$$SD(\sigma) = \sqrt{\frac{\sum(x - \bar{x})^2}{N}}$$

\bar{x} = Arithmetic mean is an average value of the data series.

s = Standard deviation; defined as positive square root of the arithmetic mean of the square of the deviations of the given observations from their arithmetic mean.

ii. Least Square Linear Trend

The straight line trend implies that irrespective of the seasonal and cyclical swings and irregular function. The trend values increases or decreases by absolute amount per unit of time. The linear trend values from a series in arithmetic progression, it is computed by following notations.

$$y=a+bx$$

where, y = Estimated value of ‘y’ for any given value of independent variable ‘x’

a = y-intercept or value of y when x = 0

b = slope of the trend line or amount of change in ‘y’ per unit change in ‘x’

In order to determine the values of the constants ‘a’ and ‘b’, the following two normal equations are to be solved.

$$\Sigma y = Na + b\Sigma x$$

$$\Sigma xy = a\Sigma x + b\Sigma x^2$$

Where N represents number of years (months or any other period) for which data are given. It should be noted that the first equation is merely the summation of the given function; the second is the summation of x multiplied by the given function.

We can measure the variable x from any point of time in origin such as the first year. But the calculations are very much simplified when the mid-point in time is taken as the origin because in that case the negative values in the first half of the series balance out the positive values in the second half so that $\Sigma x = 0$. In other words, the time variable is measured as a deviation from its mean.

Since $\Sigma x = 0$ the above two normal equations would take the form-

$$\Sigma y = Na \quad \dots\dots\dots (i)$$

$$\Sigma xy = b\Sigma x^2 \dots\dots\dots (ii)$$

The values of 'a' and 'b' can now be determined easily.

$$a = \frac{\Sigma y}{N}$$

$$b = \frac{\Sigma xy}{\Sigma x^2}$$

The constant 'a' is simply equal to the mean of y values and the constant 'b' gives the rate of change. It should be noted that in case of odd number of years,

when the deviations are taken from the middle year Σx would always be zero provided that there is no gap in the data given. However, in case of even years also Σx will be zero if the x origin is placed midway between the two middle years.

CHAPTER-IV

DATA PRESENTATION AND ANALYSIS

This chapter presents analysis of data collected and their presentation. Detail data of Machhapuchchhre Bank Limited (MBL) and Nepal Investment Bank Limited (NIBL) are analyzed and presented. The computations of ratios from the financial year 2005/06 to 2009/10 as well as their trend analysis are covered. Tables are prepared in such a way to make the presentation of result simple and understandable.

4.1 Financial Tools

Financial analysis is the starting point for making plans before using any sophisticated forecasting and planning procedures. Understanding the past is prerequisite for anticipating future. Some of the important tools are used for the computation of ratios and its' analysis.

4.1.1 Analysis of Different Ratios

The study focuses the financial performance of MBL and NIBL and their comparison, hence, various ratios are calculated and compared for the both the banks. Ratio analysis shows the mathematical relationship between two accounting figures. It helps to analyze the financial strengths and weaknesses of the banks. It is also inevitable for the quantitative judgment with which the financial performance of banks can be presented properly. Ratio analysis is also concerned with output and credit decision. Four main categories of ratios have been taken in this study that is mainly related to financial performance of banks.

i. Liquidity Ratio

a. Current Ratio

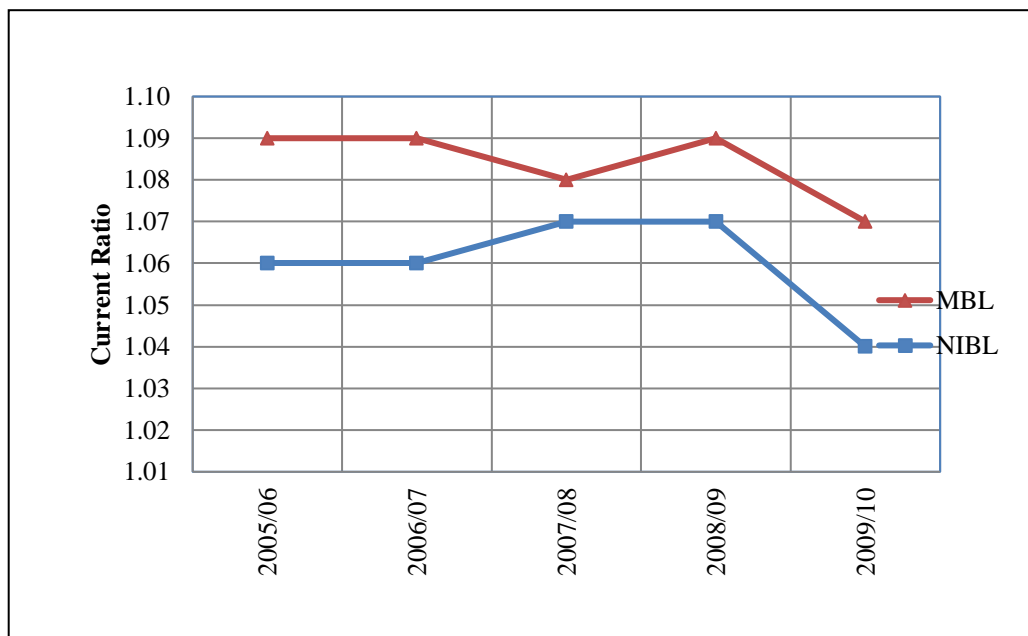
Table 4.1
Current Ratios for MBL and NIBL

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	1.09	1.09	1.08	1.09	1.07	1.08	0.009	0.008
NIBL	1.06	1.06	1.07	1.07	1.04	1.06	0.011	0.01

Sources: Appendix 1

The mean current ratio for MBL and NIBL are 1.08 and 1.06 respectively. Both the banks have current ratio almost constant for the five years. In general it can be stated that the both the banks have sound ability to meet short-term obligations. Liquidity position for MBL is slightly greater than NIBL. Similarly, standard deviation and covariance for MBL and NIBL are 0.009, 0.008 and 0.011, 0.01 respectively. The current ratios are presented graphically as follows:

Figure 4.1
Current Ratios for MBL and NIBL



The above plot shows that despite of maintaining a sound ability to meet short term obligation, both the banks have decreasing current ratio in the present year, however, that doesn't mean a critical problem. The decreasing current

ratio in the present year may be an indication that the banks are investing their deposits more than in previous years.

b. Cash and Bank Balance to Total Deposit Ratio

Higher value of this ratio shows greater ability of the firms to meet customer demands on their deposits. The following table shows the cash and bank balance to total deposit ratio.

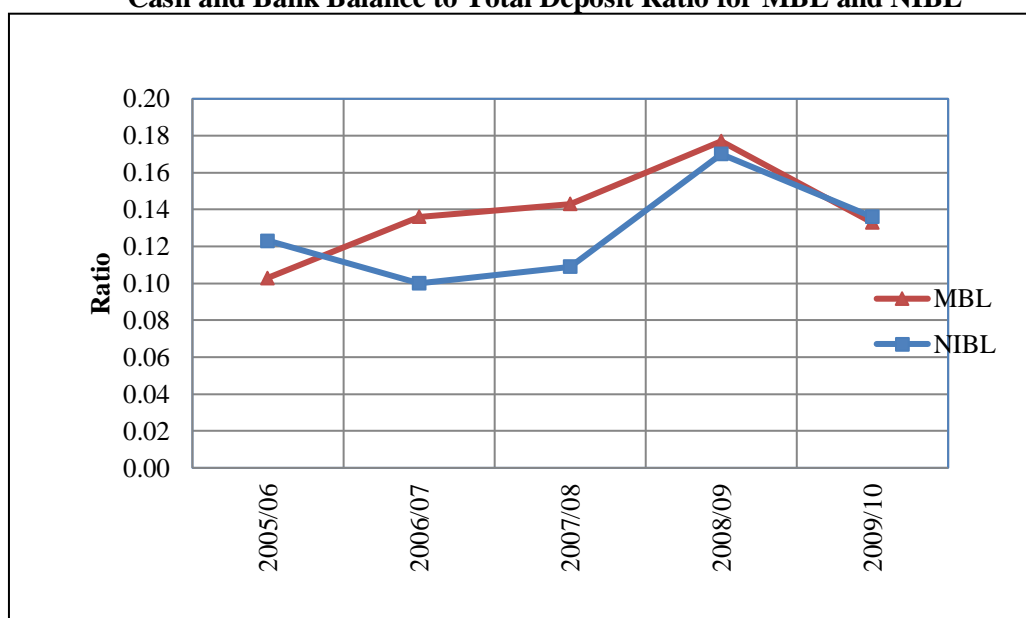
Table 4.2
Cash & Bank Balance to Total Deposit

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.103	0.136	0.143	0.177	0.133	0.138	0.024	0.171
NIBL	0.123	0.100	0.109	0.170	0.136	0.128	0.024	0.191

Sources: Appendix 1

The analysis result shows that both the banks have a fluctuating trend. The highest ratio of MBL 0.177 in F/Y 2008/09 and lowest is 0.103 in F/Y 2005/06. Similarly, the highest ratio of NIBL is 0.170 in F/Y 2008/09 and lowest in 0.10 in 2006/07. The mean ratio of MBL and NIBL are 0.138 and 0.128 respectively. MBL has slightly better covariance than NIBL; however, both the banks have similar standard deviation. The ratios are presented graphically as follows:

Figure 4.2
Cash and Bank Balance to Total Deposit Ratio for MBL and NIBL



It is concluded that the cash and bank balance position of MBL with respect to NIBL is better in order to serve its customer's deposits. It implies the better liquidity position of MBL from the view point of depositor demand. In contrast, a high ratio of cash and bank balance may be undesirable which indicates the bank's inability to invest its funds income generating areas.

Thus, MBL should invest in more productive sectors like short-term marketable securities insuring enough liquidity which will help the bank to improve its profitability.

c. Cash and Bank Balance to Current Assets Ratio

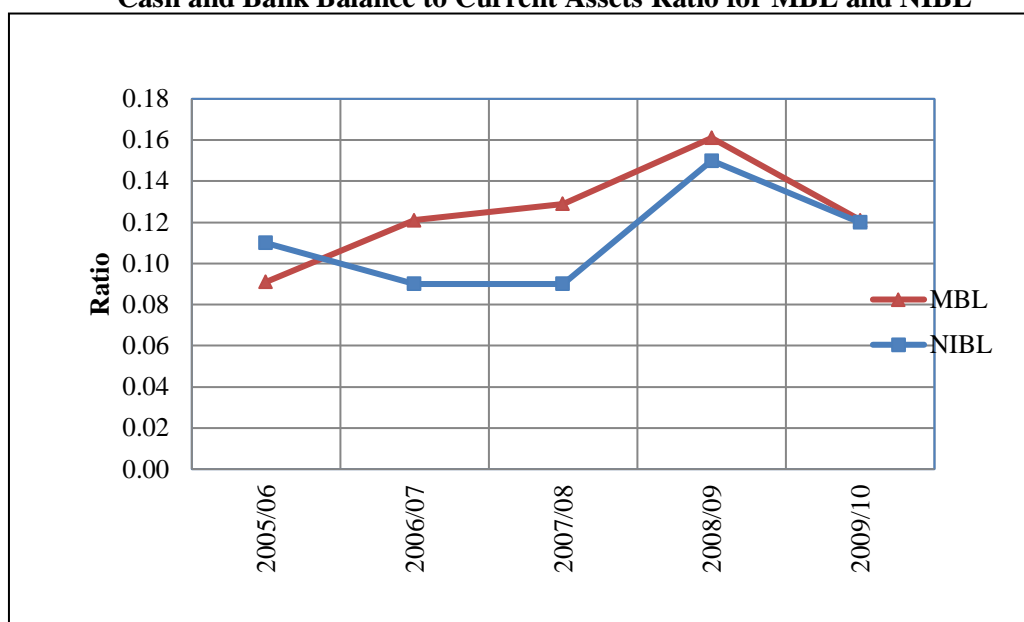
Table 4.3
Cash & Bank Balance to Current Asset Ratio

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.091	0.121	0.129	0.161	0.121	0.125	0.022	0.176
NIBL	0.111	0.089	0.097	0.150	0.120	0.113	0.021	0.203

Sources: Appendix 1

Both the bank has fluctuating trend regarding cash and bank balance to current assets ratio. The mean ratios for MBL and NIBL are 0.125 and 0.113 respectively. The higher mean ratio of MBL shows that it's better ability to meet total cash requirements of their customers. In other word, it shows that MBL has more liquidity due to low investment opportunities. The cash and bank balance to current assets ratios are presented graphically as follows:

Figure 4.3
Cash and Bank Balance to Current Assets Ratio for MBL and NIBL



The above plot shows that MBL has higher cash and bank balance to total asset which indicates MBL is paying interest on deposits. MBL is maintaining a higher liquidity at hand, which in terms of financing deposit is not satisfactory. MBL shall invest more of its deposit, maintaining a good liquidity position. NIBL, in other hand, is investing its' deposit in more lucrative way.

ii.Assets Management Ratio or Activity ratio

A commercial bank must be able to manage its assets very well to earn high profit, so to satisfy its customers and for own existence. Assets management ratio measures how efficiently the bank manages the resources at its commands. Through following ratios, assets management ability of banks has been measured.

a. Loans and Advances to Total Deposit Ratio

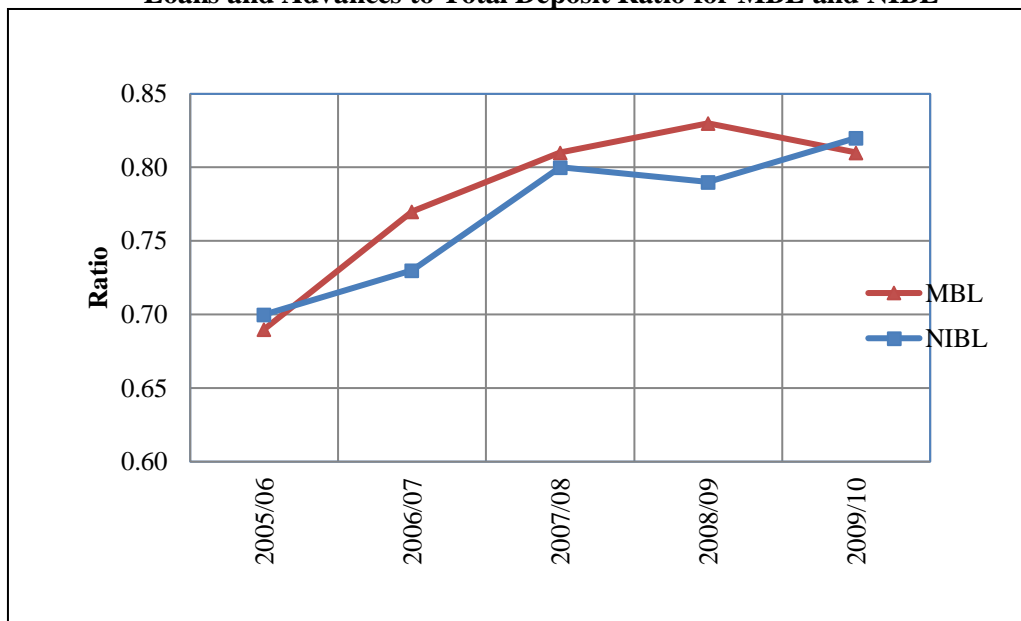
Table 4.4
Loans and Advances to Total Deposit Ratio

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.69	0.77	0.81	0.83	0.81	0.78	0.049	0.064
NIBL	0.70	0.73	0.80	0.79	0.82	0.77	0.045	0.059

Sources: Appendix 1

The above table shows both the banks have a fluctuating trend for Loans and Advances to Total Deposit ratio. It indicates the better mobilization of deposit by NIBL. The mean ratios for MBL and NIBL are 0.78 and 0.77 respectively. MBL has a slightly higher ratio than that of NIBL. The deposits of MBL will be quickly converted into loans and advances to earn income. Since the mean ratios for both the banks are between 0.7 and 0.9, the banks are in better position in mobilizing its' collected deposits as loans and advances. The loans and advances to total deposit ratios are presented graphically as follows:

Figure 4.4
Loans and Advances to Total Deposit Ratio for MBL and NIBL



From above plot it is evident that both the banks are maintaining a higher loans and advances to total deposit, which means they are good in mobilization of collected deposit. In this regard both the banks are doing a good investment.

b.Total Investment to Total Deposit Ratio

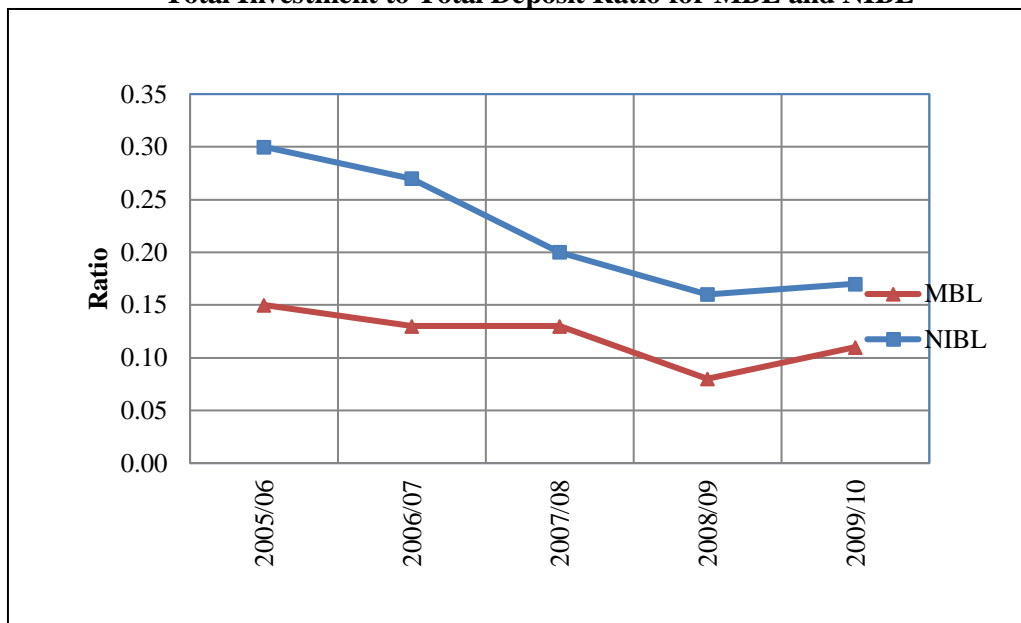
Table 4.5
Total Investment to Total Deposit Ratio

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.15	0.13	0.13	0.08	0.11	0.12	0.024	0.197
NIBL	0.3	0.27	0.20	0.16	0.17	0.22	0.055	0.252

Sources: Appendix 1

MBL has a decreasing trend of total investment to total deposit ratio from 2005/06 to 2008/09 and again the ratio increases but not reaching to its initial ratio value. MBL shows a maximum ratio in 2005/06 which is 0.15 and a minimum of 0.08 in 2008/09. Similarly, NIBL also has a decreasing trend up to 2008/09 and then the ratio slightly improves in 2009/10. The maximum value of this ratio for NIBL is 0.3 in 2005/06 and a minimum value of 0.16 in 2008/09.

Figure 4.5
Total Investment to Total Deposit Ratio for MBL and NIBL



A comparative study shows, despite of both banks decreasing trends, NIBL still has a better performance regarding investing its' deposit. Investment in the recent years for both banks may not be adequate. This may be correlated with the global recession during this period. It will be more advisable for both the banks to reorganize and rework out its investment plan so that they could come up again in the years to come. However, NIBL has a higher standard deviation and larger co variance, which indicates a higher risk for the bank.

c.Loans & Advances to Total Assets Ratio

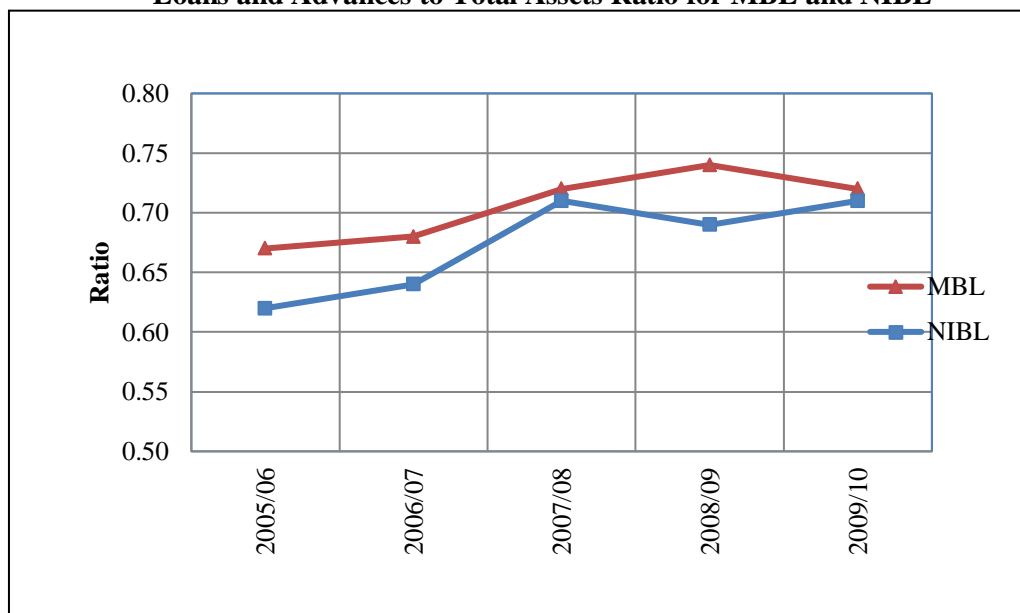
Table 4.6
Loans and Advances to Total Assets Ratio

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.67	0.68	0.72	0.74	0.72	0.69	0.051	0.072
NIBL	0.62	0.64	0.71	0.69	0.71	0.68	0.038	0.055

Sources: Appendix 1

The above table shows almost equal mean values for Loans & Advances to Asset ratio, which means both the banks, have similar performance regarding its loans and advances. However, both the banks show an increasing trend. MBL's loan and advance performance is better in 2008/09, while in 2009/10, the ratio decreases. In 2005/06, MBL has a minimum ratio of 0.67 and maximum of 0.74 in 2008/09. Similarly, in 2007/08 and 2009/10, NIBL has maximum loans and advances ratio of 0.71 and a minimum of 0.62 in 2005/06.

Figure 4.6
Loans and Advances to Total Assets Ratio for MBL and NIBL



The above plot indicates that both the banks are maintaining a good loans and advances to total asset ratio. Moreover, the trend is increasing towards present year. The banks are becoming more investment oriented.

iii. Profitability Ratio

Profitability ratios measure a company's financial performance and its ability to increase its shareholders value and generate profits. Profitability ratios provide insight into the profits made by the company in relation to its size, assets, and sales and also measure the company's performance in relation to itself. Having past data as a benchmark, the firm can start to make conclusions as to why profitability is increasing or decreasing.

a. Return on Loans & Advances

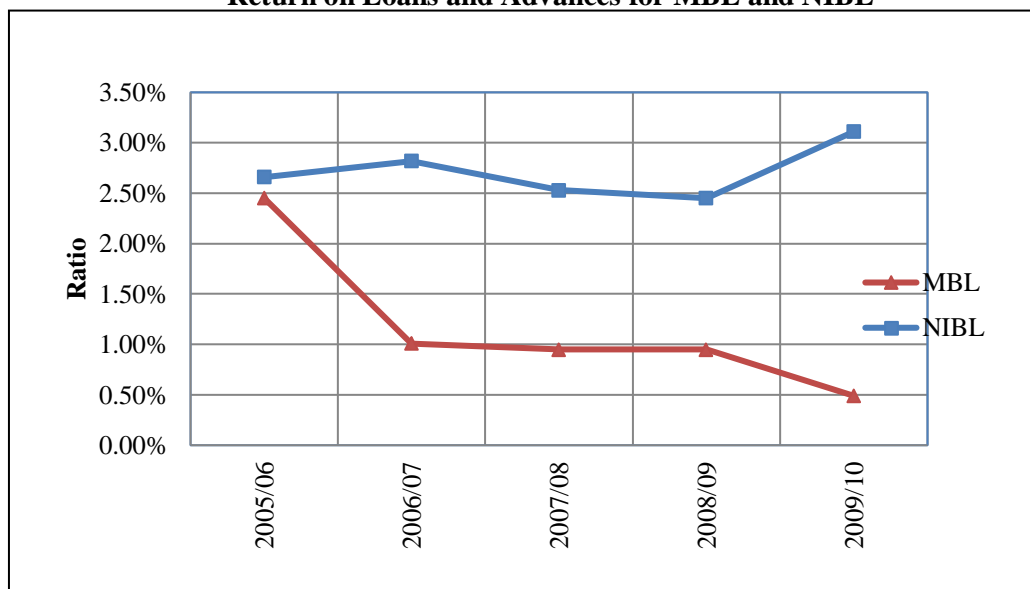
Table 4.7
Return on Loans and Advances

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	2.45%	1.01%	0.95%	0.95%	0.49%	1.17%	0.01	0.835
NIBL	2.66%	2.82%	2.53%	2.45%	3.11%	2.71%	0.015	0.541

Sources: Appendix 1

MBL has a fluctuating trend for return on loans and advances while NIBL has somehow a constant ratio for last five years. NIBL has better return ratios on loan and advance compared to MBL. MBL shows its maximum return ratio of 2.45% in 2005/06 and afterwards the trend is declining and in most cases it is equal to one. The maximum return ratio for NIBL is 3.11% in year 2009/10.

Figure 4.7
Return on Loans and Advances for MBL and NIBL



It can be clearly seen that NIBL is gaining more profit on its loans and advances than MBL. NIBL management seems more efficient than MBL to utilize its fund. It shows that NIBL invest more return investment alternative which helps to earn more profit, whereas MBL fails to find alternatives for profit oriented investment.

b.Return on Total Assets Ratio (ROTA)

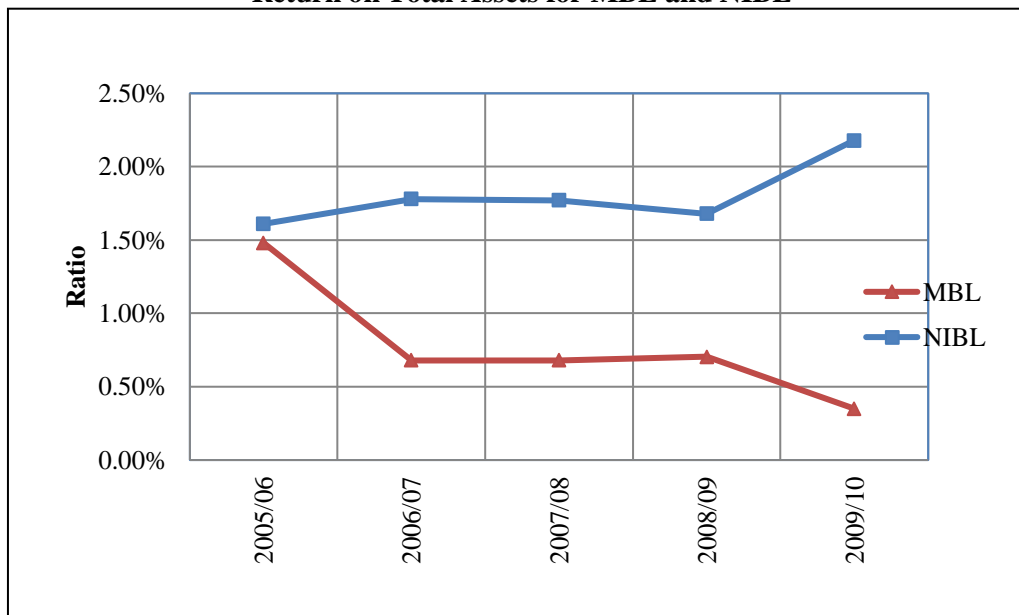
Table 4.8
Return on Total Assets

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	1.48%	0.68%	0.68%	0.7%	0.35%	0.75%	0.004	0.481
NIBL	1.61%	1.78%	1.77%	1.68%	2.18%	1.81%	0.002	0.109

Sources: Appendix 1

The above table shows that both the banks have fluctuating trend for Return on Total Assets ratio. However, NIBL has better ROTA ratio than MBL which implies that NIBL is managing its revenue generating in a better and successful way than MBL. NIBL’s ROTA ratio ranges from 1.61% in 2005/06 to 2.18% in 2009/10 while MBL has it’s ROTA generally below one, ranging from 0.35% in 2009/10 to 1.48% in 2005/06. It can be stated that performance wise MBL is degrading and NIBL is improving.

Figure 4.8
Return on Total Assets for MBL and NIBL



Analysis result shows that NIBL is generating a higher profit, whereas MBL in this regard is not making a significant profit. Moreover, NIBL shows an increasing trend while MBL shows a decreasing trend. MBL seems to have more nonperforming assets which could be harmful for the bank. NIBL in other hand is investing its property in more profit generating venues.

c. Return on Net worth or Equity Ratio

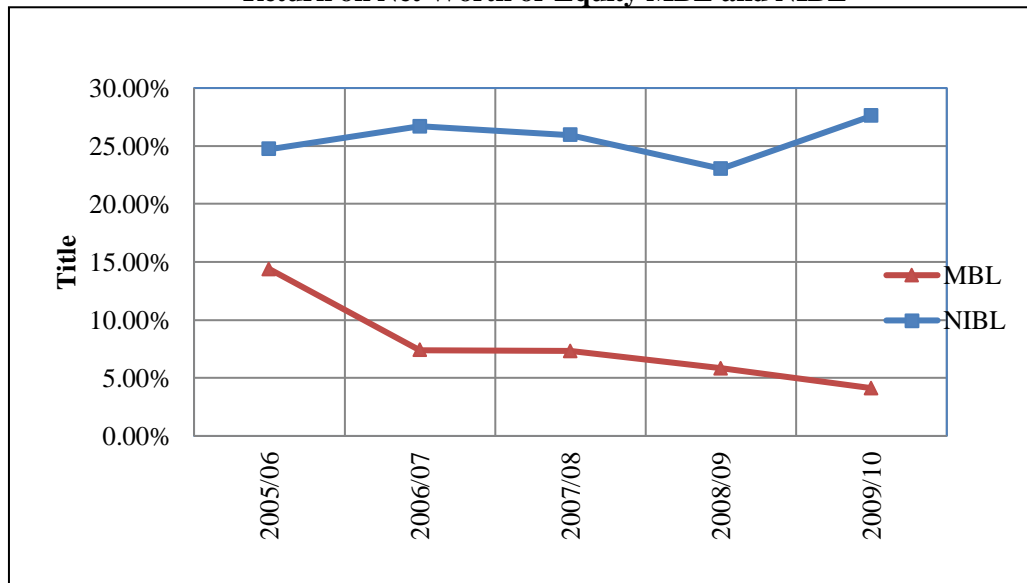
Table 4.9
Return on Net Worth

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	14.39%	7.40%	7.31%	7.23%	4.12%	7.81%	0.035	0.418
NIBL	24.73%	26.68%	25.95%	23.04%	27.59%	25.60%	0.016	0.062

Sources: Appendix 1

The above table shows that NIBL's return on Net Worth ranges from 23.04% in 2008/09 to 27.59% in 2009/10. MBL's return on net worth is 14.39% in 2005/6 and 4.12% in 2009/10, which is in decreasing trend. Compared to MBL's return on Net Worth, NIBL is in a much better position.

Figure 4.9
Return on Net Worth or Equity MBL and NIBL



Despite stiff competition and an adverse macroeconomic environment, NIBL is currently generating higher ROE in comparison to MBL. In brief, it signifies that the shareholders of NIBL are getting higher return but in case of MBL, they are getting lesser. It can be concluded that NIBL has better utilized the

equity for the profit generation. It proves to be a good strength of NIBL in attracting future investment also while MBL shows its weakness regarding efficient utilization of its owner’s equity in comparison to NIBL. NIBL has homogeneous return in each year. It is the strength point of NIBL.

d.Total Interest Earned to Total Assets Ratio

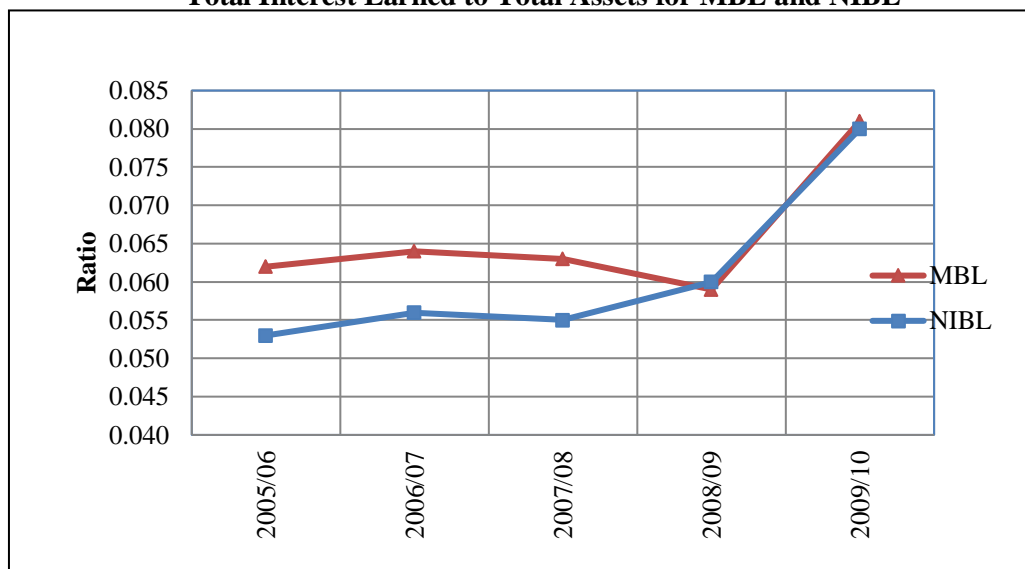
Table 4.10
Total Interest Earned to Total Assets

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.062	0.064	0.063	0.059	0.081	0.0658	0.008	0.118
NIBL	0.053	0.056	0.055	0.06	0.08	0.0608	0.0097	0.162

Sources: Appendix 1

Both the banks have increased trend in total interest earned to total assets ratio. The mean ratios are 0.0658 and 0.0608 for MBL and NIBL. Comparatively MBL seems to be slightly more efficient in earning interest than NIBL. The both banks seem to be managing its assets efficiently to earn interest.

Figure 4.10
Total Interest Earned to Total Assets for MBL and NIBL



A high ratio means that a bank is able to meet its interest obligations because earnings are significantly greater than annual interest obligations. However, a high ratio can also mean that a company has an undesirably low level of leverage or pays down too much debt with earnings that could be used for other

investment opportunities to get higher rate of return.

e.Return on Total Deposit Ratio

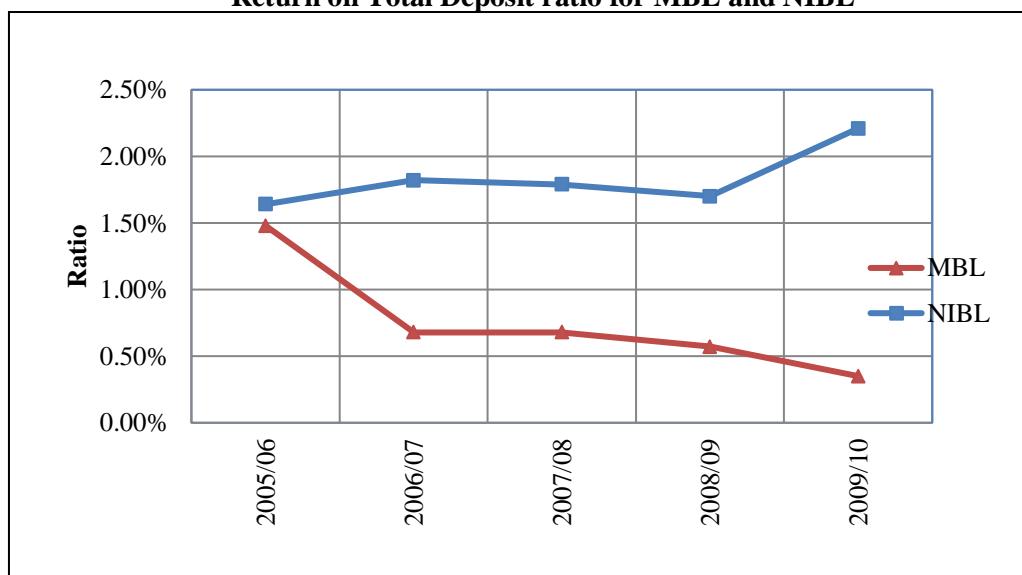
Table 4.11
Return on Total Deposit Ratio

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	1.48%	0.68%	0.68%	0.57%	0.35%	0.75%	0.004	0.511
NIBL	1.64%	1.82%	1.79%	1.70%	2.21%	1.83%	0.002	0.109

Sources: Appendix 1

In most of the cases MBL has a lower return on total deposit for the studied period while NIBL has managed to maintain its return on total deposit by more than one percent. The ratio of MBL is in decreasing trend whereas NIBL in increasing trend. In this regard, it can be stated that the performance of NIBL is better than MBL.

Figure 4.11
Return on Total Deposit ratio for MBL and NIBL



It is evident from above graph that NIBL has better overall financial performance than MBL. NIBL’s performance has been improved over the past five years, whereas MBL has a declining performance for the same period of time.

iv. Capital Structure Ratio or Solvency Ratio or leverage ratio

a. Debt to Equity Ratio

Table 4.12
Debt to Equity Ratio

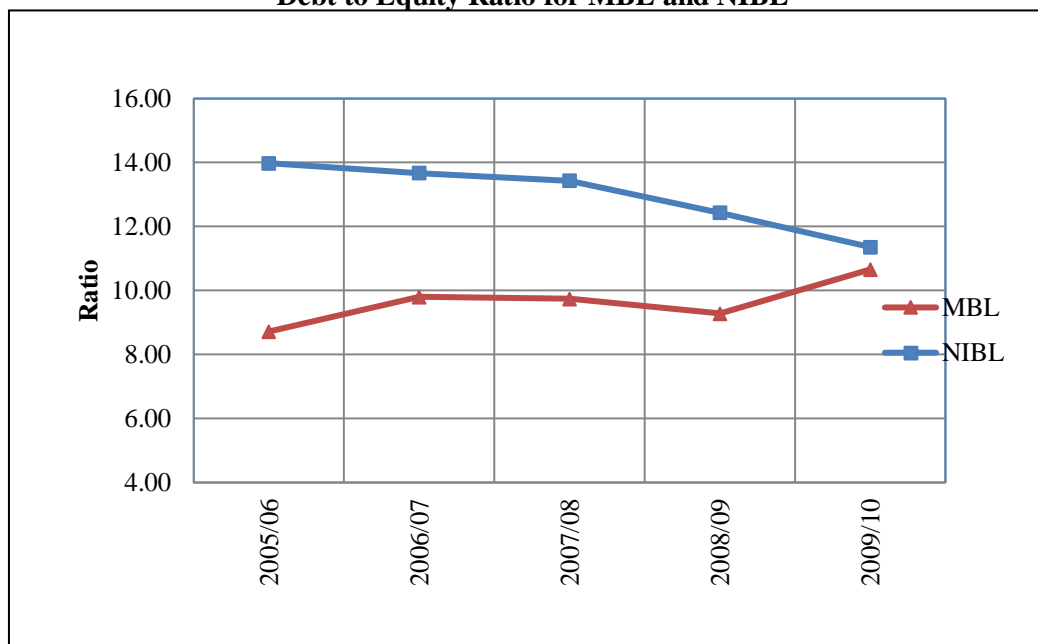
Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	8.72	9.80	9.74	9.28	10.66	9.64	0.641	0.066
NIBL	13.98	13.67	13.43	12.43	11.36	12.97	0.960	0.074

Sources: Appendix 1

The above table shows, for MBL, the trend is somewhat increasing for last five years ranges from 8.72 in the year 2005/06 to 10.66 in the year 2009/10. NIBL has a decreasing trend for debt to equity ratio with a minimum of 11.36 in the year 2009/10 and a maximum of 13.98 in the year 2005/06.

It is important to realize that if the ratio is greater than 1, the majority of assets are financed through debt. If it is smaller than 1, assets are primarily financed through equity.

Figure 4.12
Debt to Equity Ratio for MBL and NIBL



Both the banks have a ratio value higher than 1 which means the banks were aggressively financing its growth with debt. This could result in volatile earnings as a result of the additional interest expenses.

b.Total Debt to Total Assets Ratio

Table 4.13
Total Debt to Total Assets ratio for MBL and NIBL

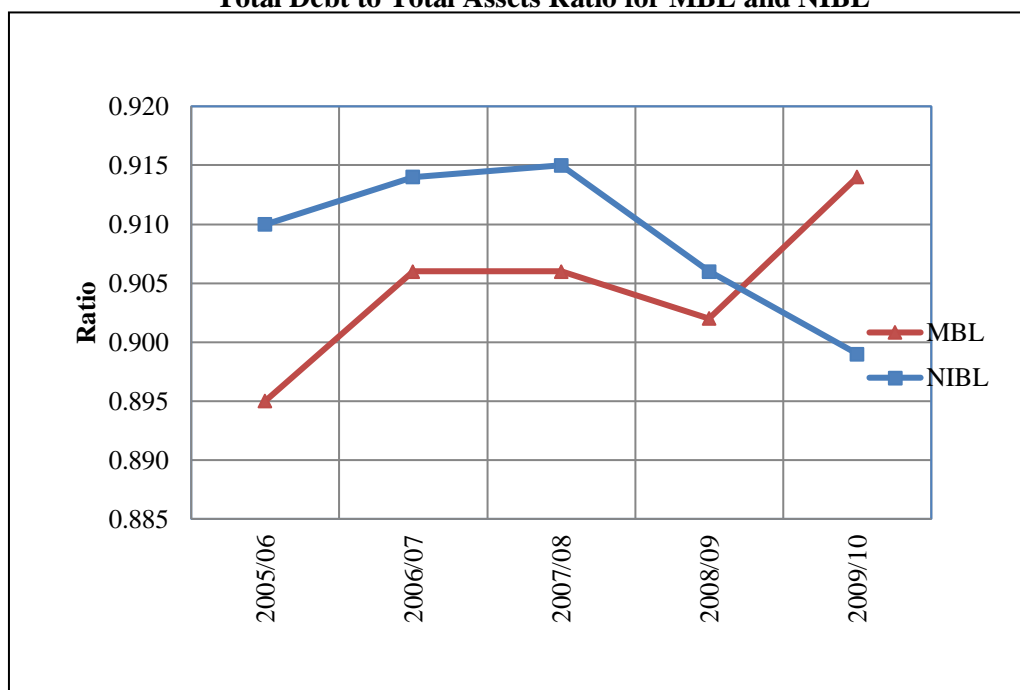
Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.895	0.906	0.905	0.902	0.914	0.905	0.006	0.007
NIBL	0.910	0.914	0.915	0.906	0.899	0.909	0.006	0.006

Sources: Appendix 1

The above table shows that both the banks have fluctuating debt to assets ratio. They have higher debt to asset ratio for the studied period. It means both the companies are financing through debt. This implies that both the banks are highly leveraged and could be in danger if creditors start to demand repayment of debt.

MBL's debt to assets ratio ranges from 0.895 in the year 2005/06 to 0.914 in the year 2009/10. Similarly, for NIBL it is 0.899 in the year 2009/10 and 0.915 in the year 2007/08.

Figure 4.13
Total Debt to Total Assets Ratio for MBL and NIBL



Both the banks have this ratio higher than 0.9 for all the years studied, which means a major amount have been financed through its creditor, not by the

owner. Such a higher ratio indicates more leverage and more risk to both the banks. They should find out ways to finance its investment by itself i.e. owner.

c. Interest Coverage Ratio

Table 4.14
Interest Coverage Ratio for MBL and NIBL

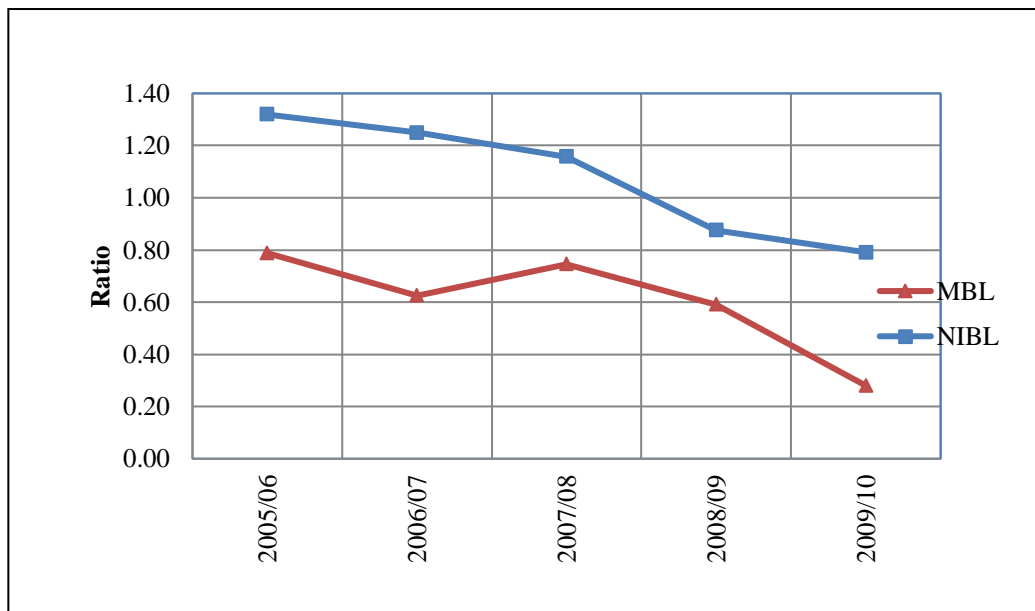
Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.788	0.625	0.745	0.591	0.280	0.606	0.178	0.295
NIBL	1.319	1.249	1.158	0.875	0.791	1.078	0.208	0.193

Sources: Appendix 1

The analysis shows that both the banks have a good interest coverage ratio, however, both the banks have fluctuating trend. It can be stated that both the banks are managing properly to achieve a higher ratio values and minimizing its debt expense burden.

The banks are able to meet interest expenses by generating sufficient revenues. It is to be noted that, the lower the ratio, the more the company is burdened by debt expense. When a company's interest coverage ratio is 1.5 or lower, its ability to meet interest expenses may be questionable. An interest coverage ratio below 1 indicates the company is not generating sufficient revenues to satisfy interest expenses.

Figure 4.14
Interest Coverage Ratio for MBL and NIBL



In the above plot it can be seen that NIBL has fairly good interest coverage ratio, for first three years higher than 1 and less than one for last two years. For MBL its interest coverage ratio is always less than one which means its ability to meet interest expenses may be questionable.

v. Other Ratios

Some other ratios have also been calculated. There are some of the other widely used ratios relating to the financial aspect of the company.

a. Earnings per Share (EPS)

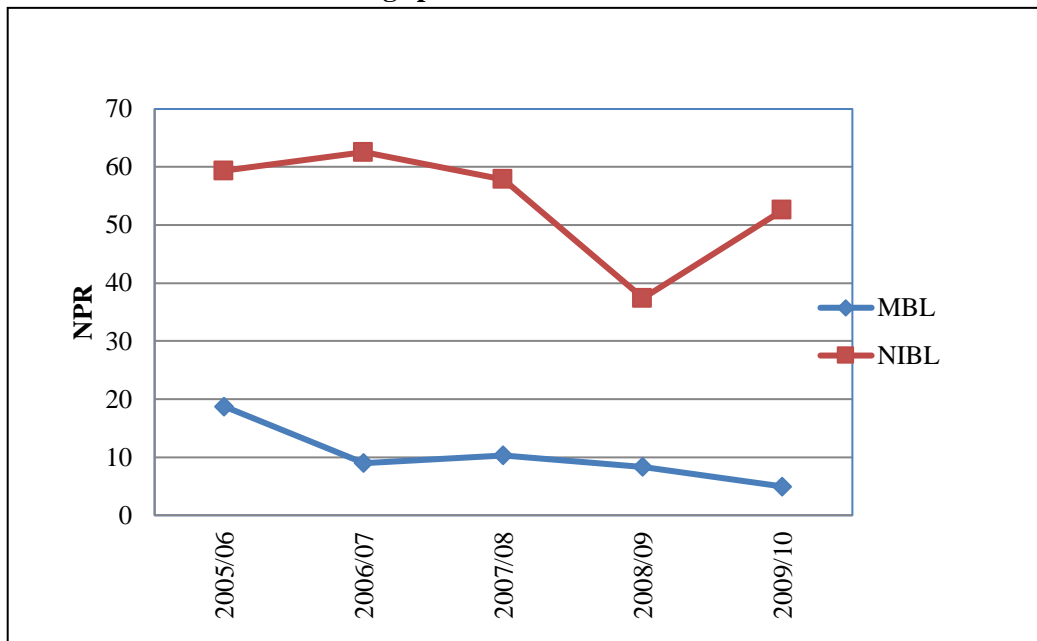
Table 4.15
Earnings per Share for MBL and NIBL

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	18.74	9.02	10.35	8.33	4.96	10.28	4.59	0.446
NIBL	59.35	62.57	57.87	37.42	52.55	53.95	8.88	0.165

Sources: Appendix 1

The above table shows a fluctuating trend for NIBL for EPS, however, it has better EPS value than MBL during the studied period. The EPS for MBL is in decreasing order. From comparison it can be seen that NIBL has better EPS values which means its share is generating more income than MBL. MBL has minimum EPS NPR 4.96 in the year 2009/10 and maximum EPS 18.74 in 2005/06. NIBL has minimum EPS 37.42 in year 2008/09 and maximum EPS 62.57 in year 2006/07.

Figure 4.15
Earnings per Share for MBL and NIBL



The analysis result presented clearly shows that NIBL's share earnings are more than MBL for the studied period.

b.Dividend per Share (DPS)

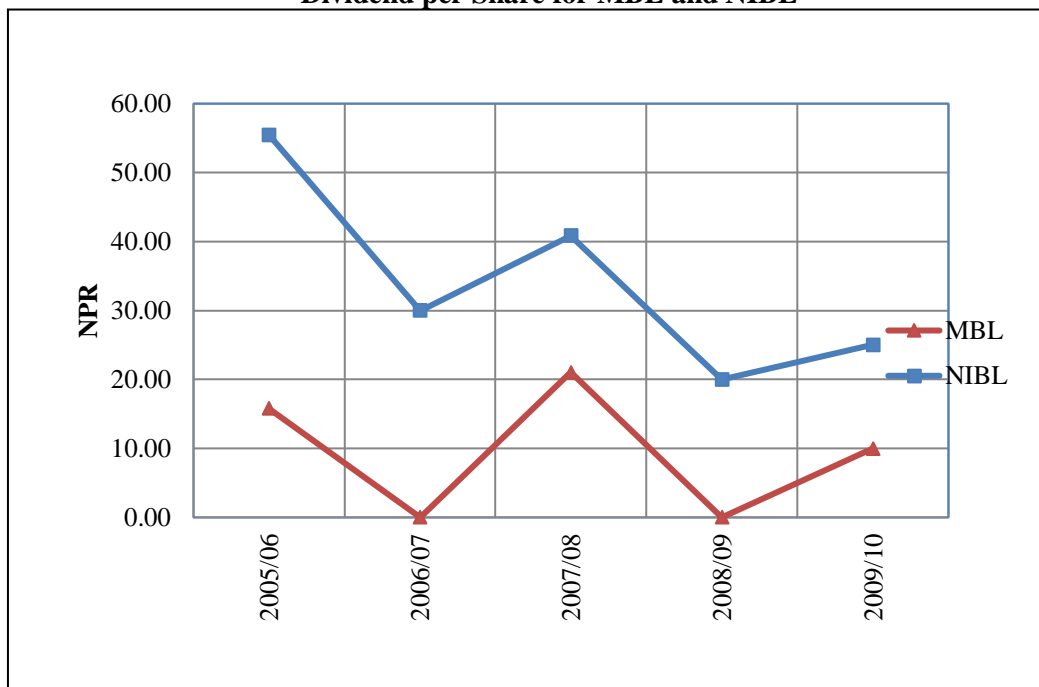
Table 4.16
Dividend per Share for MBL and NIBL

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	15.79	-	21.05	-	10.00	15.61	4.513	0.289
NIBL	55.46	30.00	40.83	20.00	25.00	34.26	12.65	0.369

Sources: Appendix 1

MBL is providing its dividend every alternate year which are 2005/06, 2007/08 and 2009/10 and it has a fluctuating trend. NIBL is distributing dividend every year for the studied period. This shows that NIBL management is more confident about sustainability of its growth. NIBL distributed a higher dividend in 2005/06 at NPR. 55.46 which went down to NPR 20 in the year 2008/09. The fluctuating trend can be realized by calculating its standard deviation which is 4.513 for MBL and 12.65 for NIBL.

Figure 4.16
Dividend per Share for MBL and NIBL



However, both banks show similar fluctuating pattern. NIBL has a greater dividend per share than MBL, Moreover MBL is providing dividend only at one year interval.

c. Earnings Ratio

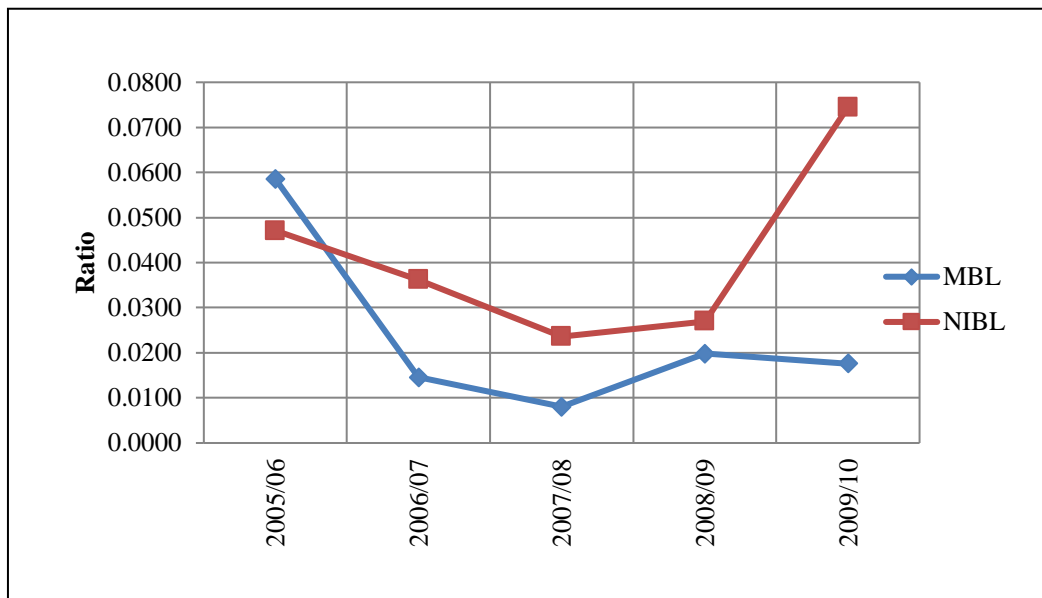
Table 4.17
Earnings Ratio for MBL and NIBL

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	0.0586	0.0145	0.0081	0.0198	0.0176	0.0237	0.018	0.753
NIBL	0.0471	0.0362	0.0236	0.027	0.0745	0.0417	0.018	0.439

Sources: Appendix 1

The above table shows both the bank has a fluctuating trend in earnings ratio. In year 2007/08 MBL has minimum earning and maximum earnings in the year 2009/10. NIBL shows a better earnings ratio in comparison to MBL. NIBL has a maximum earning of 0.0745 in the year 2009/10 and a minimum of 0.023 in the year 2007/08.

Figure 4.17
Earnings Ratio for MBL and NIBL



The trends for earnings ratio for both the banks are similar for the studied period. The trend is declining for first three years and then it rises steeply towards the present year. It can be stated that after a long recession again both the banks are performing better.

d.Dividend Yield

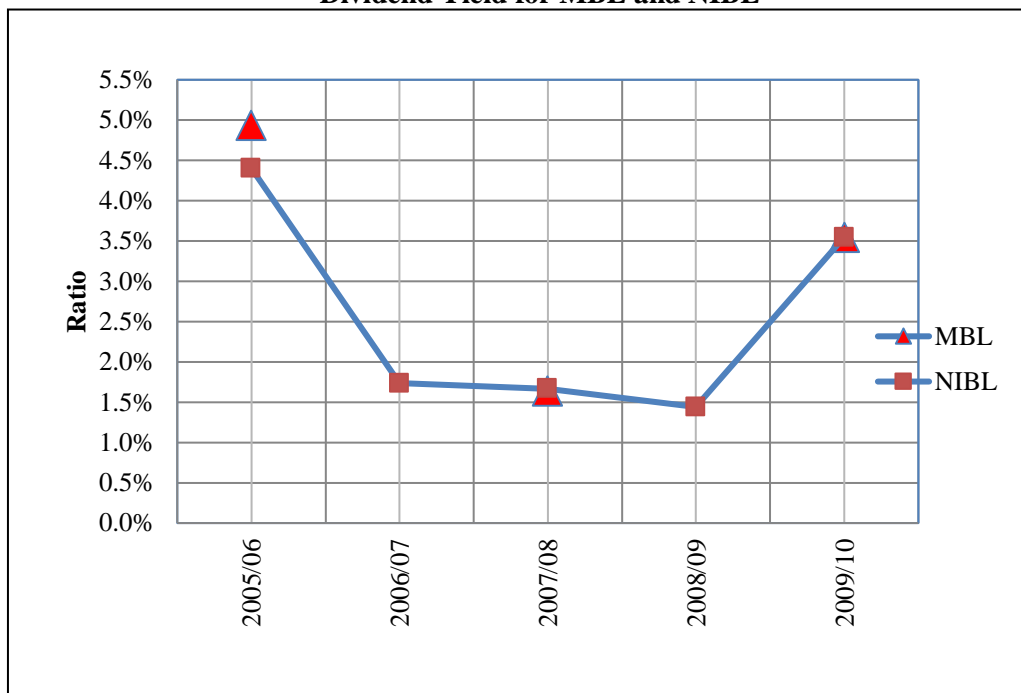
Table 4.18
Dividend Yield for MBL and NIBL

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	4.93%	-	1.64%	-	3.55%	3.37%	0.023	0.707
NIBL	4.40%	1.74%	1.67%	1.44%	3.55%	2.56%	0.012	0.477

Sources: Appendix 1

Dividend yield represents the percentage return by the company that goes to the shareholders in the form of dividends. The mean value for dividend yield is greater for MBL than NIBL, however, it is to be noted that MBL is distributing dividend every alternate year only.

Figure 4.18
Dividend Yield for MBL and NIBL



Except for year 2005/06 both the bank shows very similar dividend yield ratio. The trend for this ratio decreases in 2006/07 and remained constant till 2008/09 and again it increases in 2009/10. A low dividend yield can be considered evidence that the stock is overpriced or that future dividends might be higher.

e. Price Earnings Ratio (P/E Ratio)

Table 4.19
Price Earnings Ratio for MBL and NIBL

Bank	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	Std. Dev.	Co Variance
MBL	17.08	68.74	124.19	50.41	56.9	63.46	34.87	0.549
NIBL	21.23	27.63	42.33	37.1	13.42	28.34	10.45	0.369

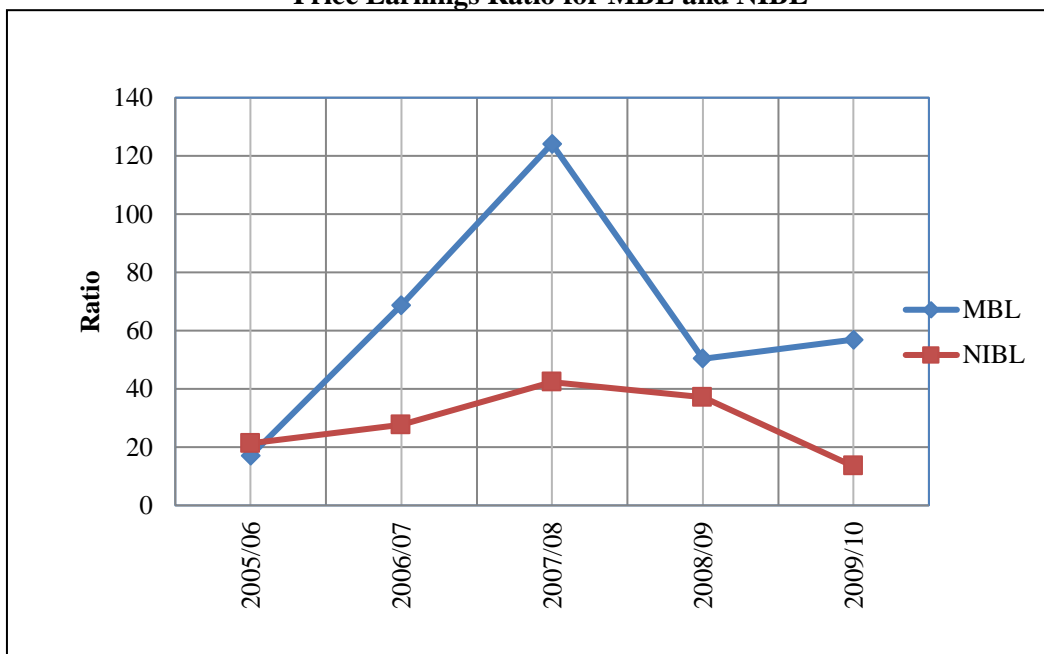
Sources: Appendix 1

The above table shows a fluctuating trend of PE ratio for both the banks. MBL's PE ratio ranges from 17.08 in the year 2005/06 to a maximum of 124.19 in the year 2007/08. NIBL's PE ratio is 42.33 in the year 2007/08 and

13.42 in the year 2009/10. Considering the mean value MBL has better P/E ratio at 63.46 against 28.34 for NIBL.

Since MBL has a higher PE ratio, market is willing to pay for MBL's earnings. Sometimes a high PE means an overpriced stock and that may be the case, however it can also indicate the market has high hopes for this stock's future and has bid up the price.

Figure 4.19
Price Earnings Ratio for MBL and NIBL



Above plot shows MBL having higher P/E ratio so it can be stated that MBL is expecting higher earnings growth in the future compared to NIBL.

4.2 Trend Analysis

It is an aspect of technical analysis that tries to predict the future movement of a stock based on past data. Trend analysis is based on the idea that what has happened in the past gives traders an idea of what will happen in the future. It is a statistical tool used for forecasting.

Various methods are used for trend analysis out of which least square method is one of the popular method used in this study.

Trend analysis is helpful because moving with trends, and not against them, will lead to profit for an investor. It provides degree of safety in the form of financial credit worthiness of the bank in future. On the other hand, for the borrowers, it assures and predicts about the financial capability of the bank to furnish their loans and advances.

In this section, the trends of the three basic financial indicators which are very crucial financial variables and could be related to the financial performance of the banks have been analyzed. These indicators are total deposit, dividend per share and earnings per share.

The trend for previous five years has been analyzed and for future five years, the trend has been predicted for this exercise. The results of such an analysis have been presented in a comparative manner to exhibit the banks performances in future.

The projections are based on the following assumptions.

- The forecast will be true only when the limitation of least square method is carried out.
- The banks will be running present position.
- The economy will remain in the present stage.
- Nepal Rastra Bank will not change its guidelines to commercial banks.

i. Trend Analysis of Total Deposit

The following table shows the trend values for total deposit of MBL and NIBL. The analysis has been carried out based on the previous five years data and projections for upcoming five years have been plotted. The equation for the trend analysis is (Ref 3.4.2 iii above)

$$y = a + bx$$

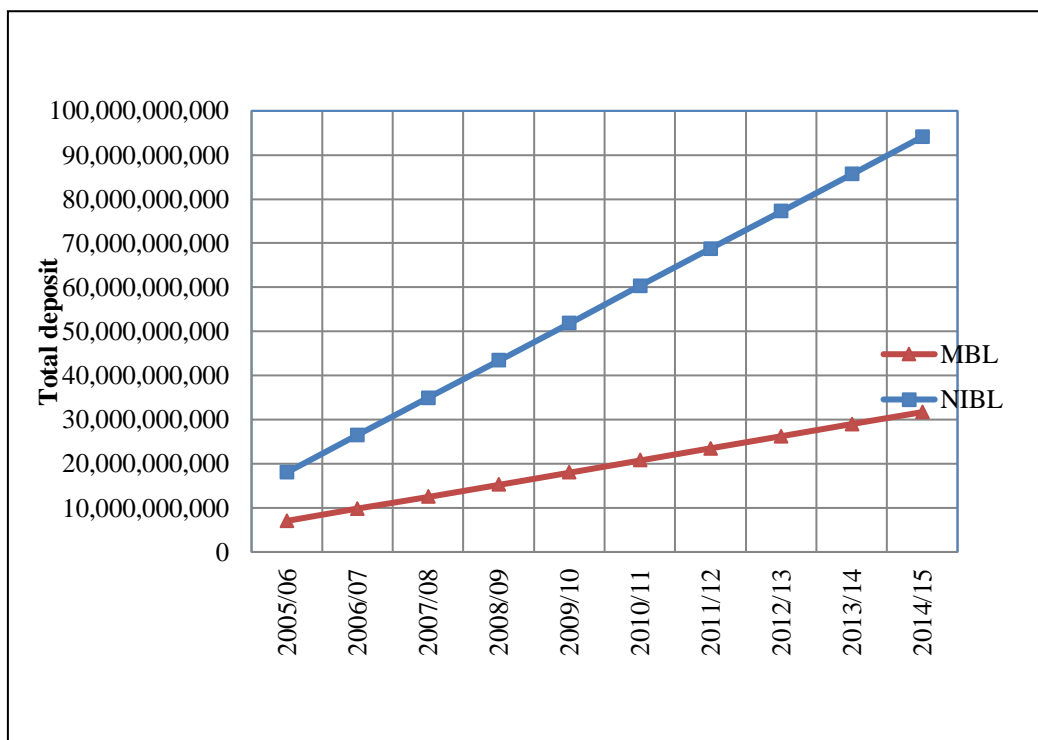
Table 4.20
Trend Analysis of Total deposit (in million)

FY		MBL	NIBL
2005/06	-2	7039	18023
2006/07	-1	9780	26477
2007/08	0	12520	34932
2008/09	1	15261	43386
2009/10	2	18001	51840
2010/11	3	20742	60295
2011/12	4	23482	68749
2012/13	5	26223	77204
2013/14	6	28963	85658
2014/15	7	31704	94112

Sources: Appendix 2z

The analysis shows that both the banks total deposits have been increasing and the trend will follow for next five years. MBL will have highest total deposit of NPR 31,704,000,000 and NIBL will have highest total deposit of NPR 94,112,000,000 in the year 2014/15 if the trend continues.

Figure 4.20
Trend Value for Total Deposit



The above plot shows that NIBL always have a higher amount of deposit compared to MBL. NIBL's total deposit has been increasing very sharply for the studied period; this could be indicator of better performance of the bank and hence gaining a very good will and trust among its customers. On the other hand MBL also has an increasing trend for total deposit; however, it's very gradual.

ii. Trend Analysis of Dividend per Share

The following table shows the trend values for dividend per share for both the banks. An analysis based on previous five year data has been carried out and forecasts for next five years have been done.

The equation for the trend analysis is (Ref 3.4.2 iii above)

$$y = a + bx$$

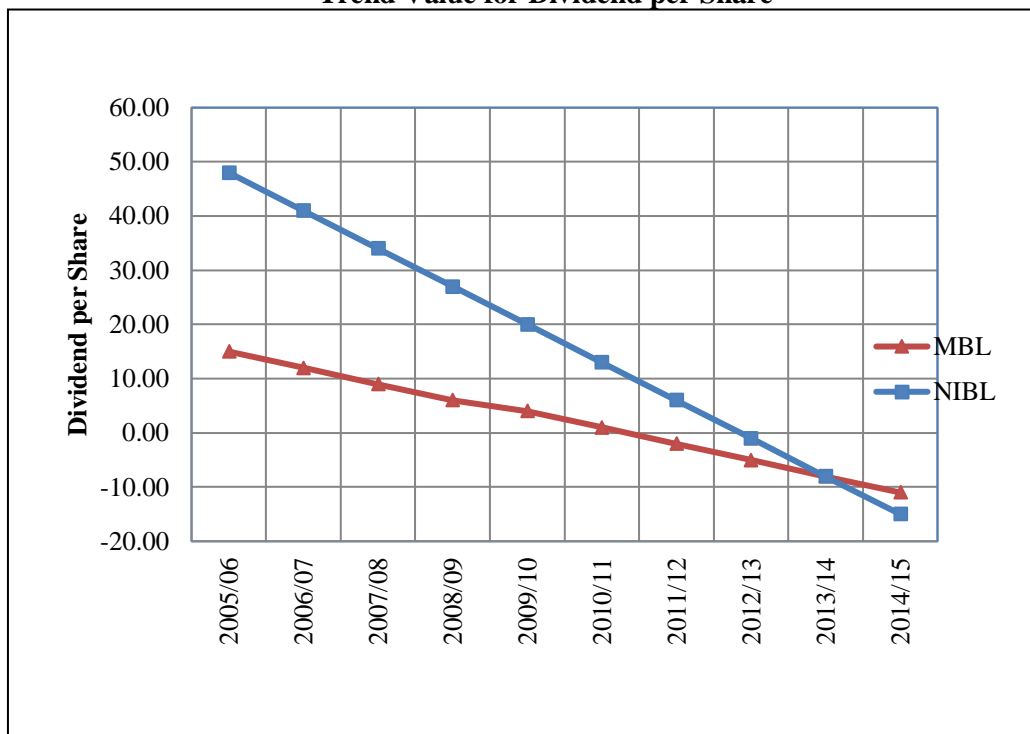
Table 4.21
Trend Analysis of Dividend per Share

FY		MBL	NIBL
2005/06	-2	15	48
2006/07	-1	12	41
2007/08	0	9	34
2008/09	1	6	27
2009/10	2	4	20
2010/11	3	1	13
2011/12	4	-2	6
2012/13	5	-5	-1
2013/14	6	-8	-8
2014/15	7	-11	-15

Sources: Appendix 2

Both the banks have decreasing trend for dividend per share in the last five years and this will even go down if the trend continues. NIBL has a higher dividend per share value, however, it also decreases if the bank doesn't make good profit out of its investment this will even decrease and the value will go below MBL's dividend per share.

Figure 4.21
Trend Value for Dividend per Share



If the trend follows, it will not be very difficult to say that both banks will be unable to provide dividend to its shareholder in the near future. In the beginning of the studied period NIBL has been providing relatively better dividend, however, this value decreases sharply. Trend shows that both the bank will not be in position to pay any dividend at all in the year 2013/14 and onwards. This could be attributed to the global recession in financial sector during this period.

iii. Trend Analysis of Earnings per Share

The following table shows the trend values for earning per share for both the banks. An analysis based on previous five year data has been carried out and forecasts for next five years have been done.

The equation for the trend analysis is (Ref 3.4.2 iii above)

$$y = a + bx$$

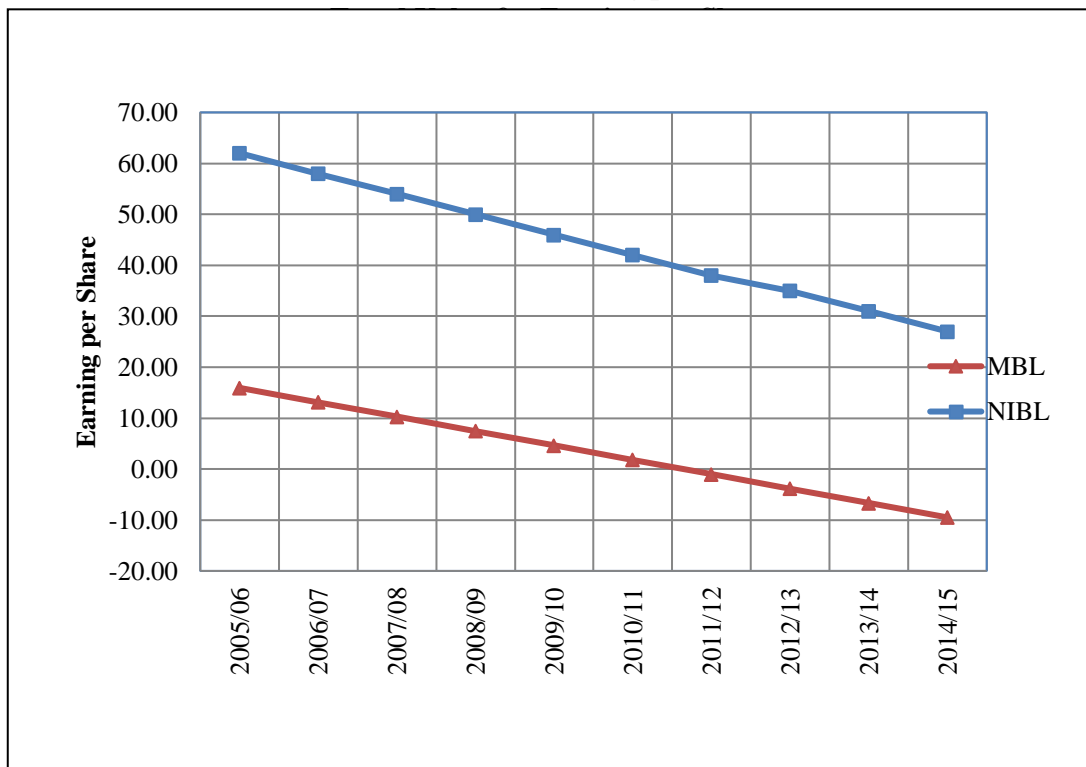
Table 4.22
Trend Value of Earning per Share

FY		MBL	NIBL
2005/06	-2	15.93	62
2006/07	-1	13.105	58
2007/08	0	10.28	54
2008/09	1	7.455	50
2009/10	2	4.63	46
2010/11	3	1.805	42
2011/12	4	-1.02	38
2012/13	5	-3.845	35
2013/14	6	-6.67	31
2014/15	7	-9.495	27

Sources: Appendix 2

NIBL has a better Earning per share value compared to MBL; however, it has a decreasing trend in last five years. MBL has lower earnings per share value and moreover it is following a decreasing trend. If the trend continues MBL may not be able to provide earnings in its share.

Figure 4.22
Trend Value for Earning per Share



In spite of having a better earnings for NIBL compared to MBL throughout the studied period, the declining rate of earning is very similar to that of MBL. This could be a strong indication that during these period, none of the banks were financing for a better profit.

4.3. Major Findings of the Study

The study is based on secondary data. During the study financial and statistical analyses have been carried out. This section presents the major findings from the study which is derived from the analysis of liquidity management of two commercial banks named MBL and NIBL.

- Both the banks are maintaining a good liquidity ratio and in a good position to meet short term demand of its customer. However, this certainly is not always a good factor. A higher liquidity means the banks are not investing its deposit to optimum. The mean current ratio for MBL and NIBL are 1.08 and 1.06 respectively.
- MBL has a better cash and bank balance position than NIBL. So MBL is in a better position to meet short term obligation. NIBL seems to have invested its cash and bank balance more than NIBL. The mean cash and bank balance deposit ratio for MBL and NIBL are 0.138 and 0.128 respectively.
- MBL again shows higher values of cash and bank balance to current asset ratio, however, both banks have shown a fluctuating trend for this ratio. The mean values for MBL and NIBL are 0.125 and 0.113 respectively. This ratio also supports the fact that MBL has more liquidity.
- Both the banks are following similar trend in managing its loans and advances to total deposits. The mean ratios for this ratio are 0.78 and 0.77 respectively. This values shows that both the banks are mobilizing its total deposit in a satisfactory manner.
- As it becomes clear from the liquidity ratio analysis that MBL has more liquidity, the total investment to total deposit also reinforce the fact that

MBL is less investment oriented than NIBL (comparatively). The ratio is always at higher side for NIBL than MBL having an average value of 0.12 and 0.22 respectively.

- The trend for loans and advances to total asset ratio is similar for both the banks, maintain an average ratio for MBL and NIBL to 0.693 and 0.676 respectively. The trend is increasing, so it can be stated that both the banks are increasing its investment in recent years.
- However, both the banks have similar trend in loans and advances, return from such loans and advances are more for NIBL. The ratio for return on loans and advances are always higher for NIBL for the studied period. The average return on loan and advances for MBL and NIBL are 1.17% and 2.71% respectively. NIBL has an increasing trend whereas MBL shows a decreasing trend for return on loan and advances.
- NIBL is always maintaining a higher value of return on total assets than MBL. The mean values for MBL and NIBL are 0.78% and 1.81% respectively. Regarding this value also, NIBL shows an increasing trend and MBL shows a decreasing trend.
- NIBL is always at higher position regarding return in net worth ratio, maintaining 25.60% average, whereas MBL has a lower average value of 8.09%. MBL seems to be very weak in efficiently utilizing its owner's equity.
- MBL is not making a good return on its deposit. NIBL is doing better in this regard and the trend is increasing during the studied period. However, both the banks have very low return on deposits.
- Both the bank's assets are financed through debt. They both have debt to equity ratio more than one with an average of 9.64 for MBL and 12.97 for NIBL.
- Total debt to total assets ratio also supports the fact that both banks have invested through debts. The average value for MBL and NIBL are 0.905 and 0.909 respectively. The banks could be in danger if creditors start to

demand repayment. However, NIBL seems to realize this and it tries to bring down the ratio.

- In spite of having a fluctuating trend in interest coverage ratio, both the banks are managing a good interest coverage ratio. The higher value of interest coverage ratio minimizes the risk of debt expense burden.
- NIBL has more earning per share than MBL.
- NIBL is providing a higher dividend per share to its shareholders whereas MBL is providing dividend every alternate year.
- In this comparative study, it has been found that NIBL is managing its financial performance in a better way than MBL.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

The study has been conducted to evaluate the performance of MBL and NIBL and then make a comparative analysis between them. In the study various financial ratios have been calculated to find out bank's own historical pattern and a future forwarded trend analysis have also been carried out. The main data sources for these analyses were the balance sheet, profit and loss account and some other financial statement. To extract all these data banks' annual reports have been referred. The study is based on the performance analysis of various financial aspects of the bank. The analysis is done through various ratios like liquidity, activity, leverage, capital adequacy, deposits and investments.

The study outlines general background, profile of MBL and NIBL considered essential for the study, statement of the problem, significance, objectives and limitations of the study. An important aspect of the study would be reviewing of literature and various others financial studies regarding the financial performance of the banks have been considered for the study. The importance and relevant aspect of banking, which have been conducted by previous researchers, have been realized in this chapter. The methodology adopted in carrying out the research work includes introduction, research design, sources and nature of data, period covered, research variables and research tools used for the study. A detailed explanation of various analytical tools and techniques has been explained. Data presentation and analysis have been carried out. Analytical analyses have been carried out to find various ratios as explained. Thus results have been presented and interpreted. Some relevant conclusions and recommendations, on the basis of main findings, derived from the analysis of MBL in comparison with NIBL, have been presented. The analysis is

performed with the help of financial tools and statistical tools, and the data have been obtained from secondary sources. During the course of the study various aspects and functions of banks have been realized. Some important functions of banks have been summarized here as follows:

Banks borrow money by accepting funds deposited on current accounts, by accepting term deposits, and by issuing debt securities such as banknotes and bonds. Banks lend money by making advances to customers on current accounts, by making installment loans, and by investing in marketable debt securities and other forms of money lending. At present, the banks adopted many types of saving accounts and schemes.

Banks provide almost all payment services, and a bank account is considered indispensable by most businesses, individuals and governments. Non-banks that provide payment services such as remittance companies are not normally considered an adequate substitute for having a bank account.

Banks borrow most funds from households and non-financial businesses, and lend most funds to households and non-financial businesses, but non-bank lenders provide a significant and in many cases adequate substitute for bank loans, and money market funds, cash management trusts and other non-bank financial institutions in many cases provide an adequate substitute to banks for lending savings too.

Banks act as payment agents by conducting cheques or current accounts for customers, paying cheques drawn by customers on the bank, and collecting cheques deposited to customers' current accounts. Banks also enable customer payments via other payment methods such as telegraphic transfer and ATM.

Both the banks perform certain functions of agency services on behalf of their customers, such as;

- Collect or make payment for bills, cheques, promissory notes, interests, dividends, rents, insurance premium etc.
- Remit funds on behalf of the clients by drafts or mail or telegraphic transfers.

Both the banks usually perform certain general utility services, such as;

- Provide letter of credit, issue travelers cheques, bank drafts, and deal in foreign exchange and foreign trade by accepting or collecting bill of exchange.
- Arrange safe deposit vaults.
- Perform guarantees.
- Collect and provide business information related to trade, commerce and industry.

5.2. Conclusion

The financial system of the country is deepening with the increased number of establishment and operation of banks and financial institutions. The expanding trend of financial sector continued in the current fiscal year as well. Expansion of Commercial Banks and its branches are attributed to the improved peace and security in the nation as well as NRB's additional liberal policy of commercial banks. There have been some improvements on the non-performing loans of commercial banks in recent times due mainly to effective regulations and improved supervision by NRB, and commercial banks own willingness to stand themselves as efficient, capable and competitive entities. But the liquidity fund of commercial banks has decreased in foreign bank balance of Nepal Rastra Banks and commercial banks.

The present study can be concluded as follows:

For the studied period, both the banks have maintained a good liquidity ratio. However, both the banks have invested aggressively during F/Y 2009/10, making a sharp decline in liquidity ratios, which in fact is a good sign for investment banking. Both the bank should be aware of running a liquidity risk.

In all liquidity analysis, it's been observed that MBL is maintaining higher liquidity ratio than NIBL. It makes NIBL a more investment oriented bank than MBL.

MBL and NIBL seem to be mobilizing its deposit in a satisfactory way. They both maintain a similar and a comparable pattern during the studied period. The ratio for both banks is greater than 70% in all samples. However, it can be observed that NIBL is ahead of MBL in investing its deposit to generate profit. Loans and advances to total assets ratio for both banks are similar.

The analysis result for profitability ratio makes it clear and loud that NIBL's financial performance is much better than of MBL. Return on loans and advances, return on total assets, return on net worth ratios and return on total deposit ratio for NIBL is higher than of MBL. All these three parameters indicate a better financial position of NIBL. Whereas total interest earned to total assets ratio follows similar trend for both the bank. This ratio is almost constant for first four years and increases in the present year, which means both the banks finally started more earnings.

The debt/asset ratio shows the proportion of a company's assets which are financed through debt. If the ratio is less than one, most of the company's assets are financed through equity. If the ratio is greater than one, most of the company's assets are financed through debt. Companies with high debt/asset ratios are said to be "highly leveraged," and could be in danger if creditors start to demand repayment of debt. Debt to equity ratio for both the banks are higher than one, which means majorities of assets are being financed through debt.

The interest coverage ratio for NIBL is better than MBL. Both the banks have good interest coverage ratio, and hence, are able to meet interest expenses by generating sufficient revenues.

Similarly, various other ratios have also been analyzed which earnings per share, dividend per share, are earning ratio, dividend yield and price earnings ratio. In all of these ratio analysis NIBL always shows a better ratios than of MBL. NIBL's earning per share is much higher compared to MBL which means NIBL's earnings are more than MBL. Similarly, if we look at dividend per share, NIBL is doing better, whereas MBL is not able to provide dividend every year.

If we compare earnings ratio, NIBL has achieved a better ratio, however, both the banks have decreasing trend for first four years. After a long recession both the banks seems to be earning more toward the fifth year. Despite all above mentioned, MBL still shows high hopes for stock's future, which is evident from its PE ratio.

It can be concluded on the basis of the financial analysis and its' comparisons between two banks, that NIBL in many aspects performing in a better way than MBL. Despite being a smaller bank compared to NIBL, MBL is also fighting against all odds to achieve a higher goal. The effect of global recession could also be observed.

5.3 Recommendations

The financial analysis results have made bank's performance evident and it can be seen that in which regards banks are doing better and where some rectification are necessary to overcome some deficiencies.

A few recommendations have been made based on the study for both the banks which are as follows;

1. The current ratio of the two banks, NIBL and MBL is considerable. This can be regarded as good liquidity position. The liquidity position affects external and internal factors such as prevalent investment situations,

central bank requirements and so on. Considering the growth position of financial market, the lending policy management capabilities, strategic planning and fund flow situation, bank should maintain enough liquid assets to pay short-term obligations. So, it is recommended to maintain sound liquidity position to NIBL and MBL.

2. NIBL and MBL have a possible risk because there is large amount of doubtful loans & advances and risky investment. So it is recommended to evaluate that investment and invest in riskless asset to grab opportunities.
3. EPS and DPS play a vital role to determine the market price of the share and also indicate the financial performance of banks. Higher EPS and DPS indicate the higher performance of banks. NIBL has been able to provide good returns while MBL seems weak in this regard. So MBL shall also invest more to earn.
4. Both the banks are recommended to formulate and implement the sound and effective investment portfolio to increase volume of total investment and loans & advances that helps to meet required level of profitability as well as social responsibility. The banks should consider rural areas in making investment policy.
5. Investment against total deposit has been declining for both the banks, which in general is not acceptable. Both the banks shall invest more for income generating activities.
6. Both banks should be careful in increasing profit of the bank to maintain the confidence of shareholders, depositors and all its customers. The money coming in bank is waning mainly due to loss of confidence. So it

is strongly recommended to utilize risky assets and shareholders fund to gain high amount of profit.

7. It is recommended to all banks to expand its services in the rural areas so that the people in the rural areas will also be able to have the facilities provided by the bank.
8. The banks are suggested to improve its management structure to increase the efficiency. In order to win the heart of the client, they should be given desired facility and deal with maximum courtesy.
9. The bankers have announced many types of saving accounts as saving bonanza, and attractive rates for interest in time deposits. Similarly, some banks have announced different attractive discounts and services on deposits. They provide soft loans to the customers without proper scrutiny of collaterals increasing risk. It is, therefore, collaterals should be properly investigated before providing loans, so that this may not create bad debts. Good governance in financial sector is another way-out for the improvement of banking business.
10. Nepal Rastra Bank has been regularly making public the Annual Monetary Policy since 2002/03. Such Policy includes subject matters such as credit foreign exchange, micro-finance, regulation and supervision of financial system. Monetary Policies announced so far have given high priority especially to internal stability (Price stability and financial sector stability) as well as external stability (favorable balance of payments). Hence, building wider and effective regulatory and supervisory mechanism to monitor the steadily escalating risk has become a challenge. It is also essential to improve corporate governance and self- regulation aspects effective.

11. The commercial banks are obligated to publish their non-audited balance sheet immediately after the end of fiscal year to ensure the transparency in the financial sector. But some of the banks have a nominal difference in their non-audited and audited reports. In fact, records reveal their net profit has marginally increased or decreased in the audited report. Therefore, it is recommended to accomplish their Internal Audit in due time.

12. Man power development is one of the essential jobs of the management to make personnel updated about internal situation and international practices in banking activities with a view to enhance the administrative knowhow.

Keeping all these in consideration, the MBL has little less performance than that of NIBL. Therefore, in the future ahead, the MBL should improve its weaknesses by adopting the innovative approach to marketing. In the light of growing competition in the banking sector both banks, NIBL and MBL should be customer oriented. It should strengthen and activate its marketing function as it is an effective tool to attract and retain the customers. For the purpose, the bank should develop an innovative approach to bank marketing and formulate new strategies of serving customers in a more convenient and satisfactory way by optimally utilizing the modern technology and offering new facilities to the customers at competitive prices. The bank is also required to explore new market areas. Thus, it is recommended to form a strong market department in its central level, which deals with the banking product, place, price and promotion.

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