FINANCIAL PERFORMANCE ANALYSIS OF NEPALESE MICROFINANCE COMPANIES

A Thesis

Submitted By:
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RECOMMENDATION

This is to certify that the Thesis

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

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VIVA-VOCE SHEET

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and found the thesis to be the original work of the student and written according to the prescribed format. We recommend the thesis to be accepted as the partial fulfillment of the requirements for

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

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DECLARATION

I hereby declare that the thesis **FINANCIAL PERFORMANCE ANALYSIS OF NEPALESE MICROFINANCE COMPANIES** submitted to Shanker Dev Campus the Faculty of Management, Tribhuvan University is my original work done for the partial fulfillment of requirements for the Master of Business Studies (M.B.S.) under the supervision of Keshar Singh Khati of Shanker Dev Campus.

Date…… **…….....…….**

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Thank You.

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Madhav Belbase

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ABBREVIATIONS

CAR	:	Capital Adequacy Ratio
CR	:	Credit Risk
DER	:	Debt Equity Ratio
DTAR	:	Debt to Total Assets Ratio
FY	:	Fiscal Year
IER	:	Income Expenses Ratio
LAR	:	Loans to Assets Ratio
LDR	:	Loan to Deposit Ratio
LR	:	Liquidity Risk
NIM	:	Net Interest Margin
NITA	:	Non-Interest Income to Total Assets
NPM	:	Net Profit Margin
OC	:	Operation Cost
OER	:	Operating Efficiency Ratio
PER	:	Profit to Expenses Ratio
ROA	:	Return on Assets
ROE	:	Return on Equity
Sig	:	Significant
SPSS	:	Statistical Package for Social Science
TU	:	Tribhuvan University

CHAPTER - I

INTRODUCTION

The introduction, literature review, research methods, analysis and discussion, and summary and conclusion are the five chapters that will make up this study. The introductory portion of the course will be covered in the first chapter. It will include the following: the study's history, problem statement, goals, theories, justification, and limitations.

1.1 Background of the Study

The assessment and measurement of a person's or an organization's financial outcomes and achievements is known as financial performance. It is evaluating several financial measurements, ratios, and indicators to determine how profitable, successful, and efficient financial operations and management are. Financial performance analysis sheds light on how effectively resources are used, income is produced, expenses are controlled, and value is created for stakeholders. To evaluate an entity's financial health and performance, key metrics including revenue, profitability, return on investment, liquidity, solvency, efficiency, and cash flow are examined. To obtain a thorough grasp of a person's or an organization's financial operations and overall success, financial performance can be assessed, compared over time, or benchmarked against industry peers by analyzing these indicators and other pertinent financial data (Sangmi & Nazir, 2010).

Both internal and external variables may have an impact on the effectiveness of microfinance organizations. These elements fall into two categories: microeconomic variables and internal, bank-specific characteristics. The performance of the bank is influenced by internal variables, which are specific features of the bank. Basically, the board and management's internal decisions have an impact on these elements. The external variables that impact the profitability of banks are those that are sector- or nation-wide, beyond the company's control (Ongore & Kusa, 2013). The majority of research on bank performance has concentrated on industry-specific elements that influence the overall performance of the banking industry. Nonetheless, the microeconomic factors must be taken into account. As a result, the analysis in this paper includes two important macroeconomic variables: GDP and inflation (Ongore

& Kusa, 2013). This research also looked at the possibility that ownership identity has an impact on the correlation between bank performance and its factors.

1.2 Statement of the Problem

Many difficulties in gathering disparate monies and allocating them to areas of productivity. Not every educated person can find job in the public or private sectors. The requirements of individuals are increasing as a result of liberalization and globalization. However, Nepalese industries are not able to provide Nepalese goods. Then, our nation's capital is leaving. Thus, how can one make investments in our nation (Shrestha, 2010)? Numerous opportunities exist for investing and saving. To get opportunities for saving and investing, it must learn about the topic of saving and investing. Microfinance is expanding at an increasingly rapid pace while making use of its greatest resources and methods (Jha & Hui, 2012).

The majority of distant regions are not included in microfinance studies. The market is now lacking in liquidity. Political parties and industrial labor are on strike. Economic sectors are impacted by these actions. Every year, the government has been unable to use the whole development money. There are a lot of microloans in the economy. The government has not been able to guarantee security at schools, colleges, or other locations. It perceives a lack of stability in the government and its investment-related policies in our nation (Pradhan, 2004). Therefore, our government and the relevant industry should focus on removing the investment-related concerns in order to create solid investment policies.

The financial performance of microfinance firms will be the primary focus of this study, which primarily addresses the following research issues with respect to a subset of microfinance organizations.

- How do the sample microfinance firms' credit risk, liquidity risk, operational costs, capital sufficiency, and profitability ratios stand?
- Is there a connection between the sample microfinance firms' capital sufficiency, profitability ratio, operational costs, and credit risk and liquidity risk?
- How do operational costs, capital sufficiency, credit risk, and liquidity risk affect the sample microfinance firms' financial performance?

1.3 Objectives of the Study

This study's main goal is to identify the key factors that affect financial performance and how they affect the financial performance of microfinance firms in Nepal. The researcher additionally adds the following particular goals in order to fulfill the overall aim.

- To assess the current status of credit risk, liquidity risk, operating cost, capital adequacy and profitability ratio of sample microfinance companies.
- To analyze the relationship between credit risk, liquidity risk, operating cost, capital adequacy and profitability ratio of sample microfinance companies.
- To examine the impact of credit risk, liquidity risk, operating cost, capital adequacy on financial performance of sample microfinance companies.

1.4 Hypothesis

The null and alternative hypotheses are as follows: in formulating the hypothesis, our primary objective is to determine whether there is a significant relationship between each independent variable and the dependent variables, as well as to evaluate the significance of the effect of the independent variables taken together on the dependent variables.

H_1: There is significant impact of credit risk on financial performance of sample microfinance companies.

H_2: There is significant impact of liquidity risk on financial performance of sample microfinance companies.

H_3: There is significant impact of operating cost on financial performance of sample microfinance companies.

H_4: There is significant impact of capital adequacy on financial performance of sample microfinance companies.

1.5 Significance of the Study

The research demonstrates the extent of characteristics unique to microfinance and how they affect the financial performance of microfinance firms in Nepal. The research illustrates the profitability of microlending firms as well as the impact of determinants on their financial performance. According to academics, the research

will contribute to the body of information already in existence since it offers suggestions for how to make the financial industry better. The research will pinpoint the variables that have a major impact on microfinance enterprises' financial success. Consequently, it will serve as a signal to policy makers and microfinance management to take into account the primary elements influencing microfinance's financial performance. This will enable them to enhance their intermediary efficiency and achieve effective financial performance.

1.6 Limitations of the Study

The main limitations of the study are as follows:

- Since the research is dependent on secondary data, its limitations may have an impact on its findings.
- The annual reports of the microfinance firms in the sample were the source of the secondary data. It's probable that the concept presented in the yearly reports is window dressing and doesn't really reflect the state of microfinance.
- Among other things, the researcher employed return on assets (ROA) and net profit margin (NPM) as dependent variables and management efficiency (ME), liquidity (LIQ), credit risk (CR), and asset quality (AQ) as independent variables to assess the financial performance of microfinance enterprises.

1.8 Organization of the Study

There are five chapters in the research on the trade-off between microfinance profitability and liquidity.

Introduction to Chapter I

The backdrop of the study, the problem description, the research's aims, its importance, its limits, and its structure are all covered in the introductory chapter.

Chapter II: Literature Review

The relevant and important literature as well as several research have been evaluated in the second chapter. The theoretical underpinnings of banking concepts that are pertinent to this research project have been reviewed.

Research Methodologies in Chapter III

The research approach utilized to assess the liquidity and profitability status of the

microfinance under examination is briefly explained in the third chapter. Research design, sample and population, data sources, statistical and financial tools and procedures are all covered in this chapter.

Data Presentation and Analysis in Chapter IV

The study's primary conclusions are included in the fourth chapter, which also presents, analyzes, and interprets the data needed for the investigation utilizing a variety of methods.

Summary, Conclusion, and Recommendations of Chapter V

This chapter seeks to summarize the study's findings and provide a number of recommendations and ideas for enhancing the bank's performance going forward.

A reference list is a list of the original sources that are consulted when creating a work or that are mentioned within the text.

Appendix: additional information at the conclusion of a book, article, or other section of a computation connected to the annual report on microfinance.

CHAPTER - II

REVIEW OF LITERATURE

2.1 Conceptual Review

The fundamental theories and ideas pertaining to the financial performance of microfinance organizations are covered in this part.

2.1.1 Financial Statement Analysis

Written reports that provide a quantitative assessment of a company's financial health are called financial statements. This comprises a cash flow statement in addition to the balance sheet and income statement. Typically, quarterly and yearly financial statements are prepared.

When evaluating the state and efficacy of a person's or an organization's financial management and operations, financial performance is an essential component. It includes assessing and measuring a range of financial measures, ratios, and indicators in order to ascertain the effectiveness, profitability, and general performance of financial operations. Financial performance offers important insights into resource usage, revenue generation, cost management, and value creation for stakeholders via the analysis of financial statements and key performance indicators. Evaluating financial performance entails looking at things like revenue, which is the entire amount of money made from selling products or services. The capacity to turn a profit is gauged by profitability measures including net profit margin, operational profit margin, and gross profit margin. While return on assets (ROA) assesses how well assets are used to create profits, return on investment (ROI) measures the return received in relation to the cost of the investment. According to Liargovas and Skandalis (2008), return on equity (ROE) is a metric that quantifies the profit created for shareholders' equity, indicating the profitability of their investment.

It is possible to evaluate, compare across time, or benchmark financial performance against peers in the sector by analyzing and interpreting these financial indicators together with other pertinent financial data. Understanding the financial well-being, sustainability, profitability, and efficiency of a person or an organization's financial operations is made easier with the help of this study. It helps all parties involved—investors, creditors, managers, and regulators—to monitor performance, see

opportunities for development, and make educated choices. In general, risk management, strategic decision-making, and reaching financial objectives all heavily depend on the analysis of financial performance. They cannot afford any loss or decline in the value of securities due to their small equity buffer. As previously mentioned, in addition to credit risk, money rate risk may affect investments in securities (Shrestha, 2010).

The fluctuation of interest rates and market prices are components of the money rate risk. Bond prices fluctuate at a significantly less amplitude than share prices, primarily because share values are determined by a wide range of circumstances and do not have a fixed dividend rate. For a banker, changes in the value of securities are quite important. When an investor purchases, he or she accepts the market's existing yield. The yield that the investor got when he purchased the assets is higher than the current rate in the event that the interest rate changes (Almazari, 2011). By formulating funds for deficit spending units, microfinance firms play a crucial role in mitigating issues such as trade deficits, inflation and deflation of the monetary trade, and budget deficits resulting from economic challenges. In order to assist the underprivileged, they also provide funding for small cottage businesses and the agricultural sector via priority sector investment schemes (Jha & Hui, 2012).

The banking industry has a big influence on the health of the economy and is crucial to the survival of the financial markets. A bank's sound financial standing provides a guarantee to its depositors as well as to its shareholders, staff, and the whole economy. In response to this dictum, attempts have sometimes been made to assess each bank's financial standing and administer it in an efficient and effective manner (Sangmi & Nazir, 2010). Microfinance firms are institutions that provide related services, provide business loans, and receive deposits. A range of deposit accounts, including checking, savings, and time deposits, are also accepted by the bank. These organizations are owned by a group of people and are operated for financial gain. Although microfinance institutions provide services to private clients, their main focus is on accepting deposits from and lending to businesses. Because microfinance organizations provide the widest variety of financial services required by the economy, they are sometimes referred to as the financial department store. Microfinance enterprises are the most prominent privately held financial institution in Nepal and the economy of most major nations. Along with a growing number of more

recent and cutting-edge services, the institution provides the general public with deposit and credit services as well as investment advising, security underwriting, insurance policy sales, and financial planning (Thapa, 2018). One of the world's earliest microfinance organizations was Bank of Venice, founded in 1157. The only things a commercial bank could do at first were take deposits and provide loans. But these days, their roles have multiplied. There are microfinance businesses functioning all over the globe. Nepal Bank Limited was founded on April 30, 1994, B.S. is one of Nepal's first microfinance firms. On July 12, 1984, NUBL Finance was founded as the first joint venture bank in Nepal under a technical service agreement with Dubai Bank Ltd (Thapa, 2018).

Following the nation's adoption of liberalization measures in 1980, the financial sector in Nepal saw tremendous expansion. This expansion was seen in the number of businesses as well as in the range of goods and services offered and the use of more recent technology. This expansion even penetrated international borders and became a part of the global financial system. Other signs of the expanding banking sector include the rise in remittances via official channels, cards and financial services that are globally usable, and representative offices that operate beyond national borders. The previous five years have seen a slowdown in the decade-long fast expansion, and a steady process of consolidation has begun. The NRB is promoting mergers and acquisitions in order to accelerate the pace of consolidation. The number of institutions in the financial sector has significantly decreased in recent years. NRB, 2016).

A prevalent presumption that serves as the foundation for a large portion of financial performance research and discourse is that better financial performance would enhance organizational operations and activities. The financial performance of businesses has garnered a lot of interest, discussion, and private management of microfinance organizations on a worldwide scale. A company's profitability, dividend growth, sales turnover ratio, and return on investment are a few metrics that may be used to evaluate its financial success. Still up for contention, nevertheless, are the appropriate metrics for gauging a company's success and the variables influencing a company's financial performance (Liargovas & Skandalis, 2008).

Examining historical and present financial data allows financial statement analysts to assess a company's performance, financial status, and potential for growth and risk in

the future. The quality of a company's profits, its financial position's strengths and weaknesses, and trends and linkages may all be learned via the examination of financial statements.

The process of identifying a company's operational and financial features from accounting information and financial statements is known as financial analysis. Determining the effectiveness and performance of the company's management as shown in the financial reports and records is the aim of such. The analyst is making an effort to gauge the company's liquidity, profitability, and other signs that it is operating in a logical and systematic manner. Analysts flag deviations when a company fails to meet industry-standard financial benchmarks or acceptable correlations between data points. Management may thus be forced to shoulder the burden of explaining the seeming issues (Sangmi & Nazir, 2010).

Financial analysis is the process of identifying the financial strengths and weaknesses of the company by correctly establishing relationships between the items of the balance sheet and profit and loss account. Financial statement analysis includes the study of relationships within a set of financial at a point in time and with trends in these relationships over time (Pradhan, 2004).

A variety of financial statements are used in financial analysis. The balance sheet is the first and provides a moment in time view of a company's financial situation. The income statement, on the other hand, shows a summary of the company's profitability over time. One of the most popular methods for analyzing financial statements and assessing management effectiveness is ratio analysis. The examination highlights the issues. If any areas of company operations exist, this serves as a foundation for the necessary remedial measures. Many people use financial ratios often to monitor the success of their investments or for other personal reasons (Pradhan, 2004).

Prior to making any trading or investment decisions, the important aspects should be carefully examined in a bank's financial statement. The yield curve and the business cycle are two concepts that investors should be well-versed in since they both significantly affect the financial success of microfinance. Since a bank's financial success is based on the yield curve, the two main elements to take into account are interest rate risk and credit risk. Boards, managers, payers, lenders, and other decision-makers who assess an organization's financial health value financial

statement analysis. The goal of financial statement analysis is to examine past and current financial data in order to evaluate a company's performance and financial position and estimate future risk and potential. Ratio analysis is one commonly used method of assessing financial statements; it uses data from the income statement and balance sheet to produce values that have easily interpreted financial meaning. The quality of a company's earnings, its financial position's strengths and weaknesses, and trends and linkages may all be learned via the study of financial statements (Zergaw, 2010).

2.1.2 Role of Financial Analysis

Financial analysis is helpful because it shows how different financial components have historically been linked. Let's say that the senior management decides to aim for a twenty percent growth in net income in the next year. Linking sales and profit. We can calculate the extra turnover needed to reach the objective. Knowing increased turnover enables us to determine the amount of more assets—fixed and current assets in the case of manufacturing companies—that are needed, as well as the additional money needed to purchase those assets. Accordingly, financial planning requires financial analysis (Zergaw, 2010).

Nowadays, a variety of financial statement users do financial analysis. Financial analysis is done by investors and management to determine how productively or profitably the company's assets are employed. Lenders and suppliers of quality consider a company's capacity to pay back debts on schedule. As an example, if you were a bank depositor, you would be concerned about the liquidity of the bank and would anticipate receiving your money when you needed it. In order to get ongoing assistance, the customer would prefer to know the bank's long-term solvency. As a borrower, for instance, you want your bank to remain profitable and in good health since you will be reliant on it for future requirements. Naturally, workers would be interested in the bank's profitability and liquidity.

In addition to creating financial statements, financial managers also evaluate them to get more understanding of the organization's performance. In order to meet the demands of several stakeholders and adhere to their requirements, they must evaluate the organization from the viewpoints of multiple users. While managers' attempts to meet the needs of different stakeholders may sometimes have an impact on

profitability, an excessive concentration on profitability may have unintended consequences for the firm. For example, we anticipate that the holders of our deposits will need liquidity. Profitability may be impacted if we budget for more liquidity (Zergaw, 2010).

2.1.3 Financial Ratio

One effective method for financial analysis is ratio analysis. A ratio may be described as the connection between two additional variables or as the stated quotient of two mathematical expressions. A ratio is a benchmark in financial analysis that is used to assess the performance and financial status (Kumbirai & Webb, 2010).

The act of identifying and deciphering numerical correlations from financial accounts is known as ratio analysis. A ratio is a metric used in statistics that shows how two variables and figures relate to each other. According to Said and Tumin (2007), there are two ways to describe this relationship: as a quotient (current assets as a particular number of times the current liabilities) or as present (cost of products sold as a percentage of sales).

There are four categories of financial ratios: coverage, profitability, debt, and liquidity. For the financial analyst, each of these kinds has a unique use. These measures also aid in management oversight and provide a clearer picture of the financial performance and condition that external capital providers anticipate.

The creativity and knowledge of the financial analyst using the ratio determines its usefulness. Financial ratios, in their opinion, are essentially worthless and should only be examined in comparison.

An analysis of the same firm's ratio over time is crucial for identifying patterns and changes in the company's profitability and financial standing. There's a chance that this comparison is historical. It could be predicated on anticipated financial statements. Ratios may also be evaluated by contrasting them with those of other companies in the same industry and, where applicable, with the industry average. A careful examination of financial numbers may reveal a lot. Financial ratio analysis is expected to become more objective and scientific than it was in the past with empirical testing of its prediction capacity (Tarawneh, 2006).

i. Profitability Ratios

The first concern of every company is its profitability. Profitability ratios are an often used technique in financial ratio analysis, serving as an indicator of the company's overall performance. Profitability metrics have significance for both business owners and management. The principal proprietor of a small firm must undoubtedly demonstrate success to outside investors who have contributed their own funds (Nedunchezhian & Premalatha, 2013).

Return on Assets (ROA)

Because it gauges how well a business is managing its asset investment and using it to generate overall profit, the Return on Assets ratio is a crucial profitability metric. It calculates the profit margin in relation to the firm's overall asset investment level. According to Tarawneh (2006), the assets management category of financial ratios is connected to the return on assets ratio.

Return on Equity (ROE)

Among all the financial statistics, the return on equity ratio is perhaps the most significant to the company's investors. It calculates the yield on the capital that investors have invested in the business. When considering whether or not to invest in the firm, prospective investors consider this ratio (Tarawneh, 2006).

Profit to Expenses Ratio (PER)

It gauges the bank's operational profitability in relation to its overall operating costs. The ratio calculates how much operational profit is made for every dollar spent on operations. The ratio shows how well the bank is able to manage its operational costs. According to Said and Tumin (2007), a bank that has a greater profit to expenditure ratio is more profitable and operates at a lower cost.

Net Interest Margin (NIM)

Because little changes in a bank's lending margin may result in significant changes to its bottom line, analysts place a lot of emphasis on the net interest margin ratio. The cheaper the money or the larger the margin the bank is getting, the higher the ratio.

One important performance metric that influences ROA of a bank is its net interest margin. The difference between interest revenue and interest costs is known as net interest income. According to Zergaw (2010), it is the gross margin on a bank's lending and investing activity.

Non-interest Income to Total Assets (NITA)

An indication of the operation's success is the ratio of non-interest income to total assets. It shows the percentage of fees and other revenue relative to the banks' total assets. As a metric of profitability, this ratio is used (Said & Tumin, 2007).

Return on Deposit (ROD)

Return on Deposit is regarded by the majority of financial experts as one of the most accurate indicators of bank profitability. This ratio shows how well bank management is able to turn a profit on the deposits made by consumers (Zergaw, 2010).

ii. Liquidity Ratio

The liquidity ratio makes an effort to gauge a company's capacity to settle its immediate debt. The most liquid assets of a business are compared to its short-term obligations to achieve this. A higher liquidity ratio indicates a greater margin of safety and the bank's capacity to meet its immediate commitments. High liquidity risk exists for banks and other depository institutions due to the withdrawal flexibility of transaction deposits and savings accounts. Generally speaking, a company's ability to pay off its short-term obligations and continue to support its operations is shown by how much of its liquid assets cover its short-term liabilities. A firm with a poor coverage rate, on the other hand, ought to alarm investors as it might indicate that the business would struggle to pay its debts and operate its operations. Loan to Asset Ratio (LAR) and Loan to Deposit Ratio (LDR) are two indicators of bank liquidity (Said & Tumin, 2007).

Loan to Deposit Ratio (LDR)

This is the ratio of a bank's loan amount to its deposit amount at any particular period. The bank is depending more on borrowed funds—which are often more expensive than most deposit kinds—the greater the ratio. In comparison to a bank with a high LDR, one with a low LDR is seen to have abundant liquidity, maybe lesser earnings, and hence less risk (Zergaw, 2010).

Loans to Assets Ratio (LAR)

The whole amount of outstanding loans is expressed as a proportion of total assets via the loan to asset ratio. The greater this ratio, the more leveraged and less liquid a bank is. A bank may be more vulnerable to increased defaults if the ratio is larger (Zergaw, 2010).

iii. Risk and Solvency Ratios

One of many ratios that assess a company's capacity to fulfill long-term commitments. The solvency ratio compares the amount of a company's total debt obligations to its after-tax revenue, excluding non-cash depreciation charges. It gives an estimate of the probability that a business will keep up its debt payments (Said & Tumin, 2007).

Industry-specific acceptable ratios may differ, but generally speaking, a solvency ratio of more exceeding twenty percent is seen as sound financial management. In general, there is a higher chance that a business may miss payments on its debts if its solvency ratio is smaller (Zergaw, 2010).

Debt-equity Ratio (DER)

The debt-to-equity ratio calculates the maximum amount of money that a business may borrow for extended periods of time without risk. This is accomplished by dividing the overall debt of the business—including both short- and long-term obligations—by the owner equity. This ratio, which compares what is owned to what is owned, shows how leveraged (or in debt) the firm is. A high debt-to-equity ratio might be a sign that the business has to find measures to cut down on its debt since it can be overleveraged. Lenders and investors often utilize the connection between equity and debt, two important financial statement statistics, to assess risk. How healthy your company's finances are may be shown by looking at the ratio of equity to long-term debt. Your company's equity will consist of the products and assets it owns as well as any claims it makes against other organizations. Both current and long-term obligations will be included in the debt (Said & Tumin, 2007).

Debt to Total Assets Ratio (DTAR)

The proportion of total debt financing the company employs divided by the percentage of total assets is known as the debt to asset ratio. It enables you to see the

percentage of your assets that are funded by debt. A company's debt to asset ratio should be as low as possible since high debt levels increase risk. It is a risky situation for a corporation to have two or three times as many assets as liabilities, therefore you should definitely take a close look at any organizations that have more total liabilities than total assets. Anything below this might be a clue that things are not going well for the business (Zergaw, 2010).

Efficiency Ratios

grasp financial accounts requires a grasp of essential ratios, including the efficiency ratios. Our spread sheets for ratio computation save time and effort when computing ratios for decision-making. In addition to helping owners, managers, and consultants boost productivity and company profitability, they lower risk for lenders and investors (Zergaw, 2010).

Assets Utilization Ratio (AUR)

An institution's assets utilization ratio indicates how well it is using all of its resources. If the AU ratio is high, the bank is probably considered to be utilizing its assets as efficiently as possible to generate total revenues. If the bank's asset-to-income ratio is low, it is not making the most of its resources and need to sell off part of its holdings or boost overall revenue. In Zeragaw (2010).

Income Expenses Ratio (IER)

In the banking industry, this ratio is most often and extensively used to evaluate the management effectiveness in producing overall revenue while managing operational expenses. The ratio known as "income to expense" indicates how much money is made for every dollar spent on operational costs. A higher income expense ratio is better than a lower one since it shows how well the bank can generate more overall revenue relative to its total operating expenditures (Almazari, 2011).

Operating Efficiency Ratio (OER)

It gauges how well managers produce operational income and keep operating costs under control. Stated differently, operational efficiency is the ratio that calculates the amount of operating expenditure per dollar of operating revenue, as opposed to income expense ratio, which calculates the amount of money made per dollar of operating cost. Because lower operating expenditures suggest lower operating

revenues, lower operating expenses are preferable over greater operating expenses. In Zeragaw (2010).

2.2 Review of Previous Studies

Numerous research studies have been conducted worldwide about the financial performance of commercial banks. The majority of studies use microeconomic, industrial, and bank variables to assess a bank's performance. The researcher examines financial performance in relation to papers and theses in this part.

Almazari (2011) conducted research on the 2005–2009 financial performance of a few chosen microfinance firms in Jordan. It is an evaluator by nature, obtaining information sources from secondary data. Financial ratios and variables provide the foundation for the analysis of banks' financial performance. In order to evaluate the influence of the independent variables—bank size, asset management, and operational efficiency—on the dependent variable, the financial performance of 20 chosen Jordanian microfinance enterprises was analyzed using simple regression in this research. Return on assets and magnitude of interest income serve as indicators of financial success. It was discovered that banks' financial performance is not necessarily correlated with their total deposits, loans, assets, and shareholders' equity. Additionally, a strong connection was seen between financial performance and asset size, asset utilization, and operational efficiency. Regression analysis further supported the finding that these independent characteristics had a significant impact on financial performance. Bank managers may find this research useful in enhancing their financial performance and developing policies that will support a stable financial system. The report also suggests actions that banks should take to guarantee the stability of their business operations.

Based on their financial features, Jha and Hui (2012) examined the financial performance of various ownership structured microfinance organizations in Nepal and identified the performance factors revealed by the financial ratios, which were based on the CAMEL Model. A financial analysis of eighteen microfinance organizations was conducted between 2005 and 2010. Furthermore, the impact of the capital adequacy ratio, non-performing loan ratio, interest expenses to total loan, net interest margin ratio, and credit to deposit ratio on the financial profitability, or return

on assets and return on equity of these banks, was estimated using an econometric model (multivariate regression analysis) by creating two regression models. The findings indicate that although local private banks are just as efficient as foreign-owned (joint venture) banks, public sector banks are noticeably less efficient than their counterparts. Additionally, the estimate findings show that the capital adequacy ratio had a large impact on return on equity, but it had no effect on return on assets. Interest expenditures to the total loan and net interest margin also had a significant impact.

The financial performance of five Palestinian microfinance firms that are listed on the Palestine Securities Exchange (PEX) was analyzed by Alkhatib (2012). Three indicators have been used to assess the financial performance in this paper: return on assets, which is an internal indicator; Tobin's Q model, which is a market indicator based on price/book value of equity; and economic value add, which is an economic indicator based on performance. In order to determine the effects of bank size, credit risk, operational efficiency, and asset management on the financial performance indicated by the three indicators, the study used correlation and multiple regression analysis of annual time serious data from 2005 to 2010. It also created a well-fitting regression model to forecast the financial performance of these banks in the future. The premise that "bank size, credit risk, operational efficiency, and asset management have a statically insignificant impact on the financial performance of Palestinian microfinance companies" was refuted by the research.

"Determinants of commercial bank profitability in Sub-Saharan Africa" was the subject of research by Francis (2013). An imbalanced panel of 216 microfinance organizations from 42 Sub-Saharan African nations was utilized for the investigation, spanning the years 1999 to 2006. Bank profitability was calculated in a static framework using the panel random effects approach and the cost efficiency model. Along with the macroeconomic variables of GDP and inflation growth, the explanatory factors include growth in bank assets, growth in bank deposits, capital adequacy, operational efficiency (inefficiency), and liquidity ratio. The results unequivocally demonstrate that the variance in commercial bank profitability across the study period is explained by both macroeconomic and bank-specific variables.

These results highlight the significance of macroeconomic and bank-level variables in elucidating Sub-Saharan African commercial bank profitability. This paper's policy implications include that macroeconomic variables and bank levels both matter if banks are to increase their profitability.

According to Nedunchezhian and Premalatha (2013), the banks have achieved performance efficiency in the areas of capital adequacy ratio, management efficiency ratio, earnings and profitability ratio, and leverage ratio during the post-merger period. Basically, two techniques were used to compare performance before and after the merger: First, the performance of local banks is compared using ratio analysis and comparison between the pre-merger (2003-2006) and post-merger (2008-2011) periods. The significance of the changes in financial performance before and after the merging activity is then ascertained using a paired sample t-test. The research discovered that, when examining the increase in the debt-to-equity ratio, all the chosen banks—aside from an Indian foreign bank—show less improvement after mergers. With the exception of India, international banks exhibit less improvement after mergers when it comes to the growth rate of total loans to total assets. When it comes to the equity capital to total assets ratio, all of the chosen banks perform worse after mergers. Following the merger, the combined banks' asset growth rates and total deposit rates all exhibit improved performance. With the exception of Indian foreign banks, the dividend payout ratio has not improved much after the merger. With the exception of Indian foreign banks, growth rates, return on assets ratios, and other income to total income show less improvement after mergers. All of the chosen banks' current ratios and quick ratios demonstrated improved performance after the merger. The performance of the chosen banks after the merger has generally improved in the majority of categories.

There is a clear lack of research to close this gap, with just Ongore and Kusa's (2013) study on the moderating influence of ownership structure on bank performance. The authors estimated the parameters in this important field of research using panel data and a linear multiple regression model with modified least squares. With the exception of the liquidity variable, the results demonstrated that bank-specific characteristics had a considerable impact on the success of microfinance enterprises in Kenya. However, at the 5% significance level, the total impact of the

microeconomic factors was deemed inconclusive. The financial performance of microfinance enterprises was not significantly affected by the ownership identity moderating effect. Thus, it can be said that management and board choices mostly influence the financial performance of Kenyan commercial banks, with macroeconomic considerations playing a minor role.

The factors that determine bank performance that Nassreddine et al. (2013) researched may be divided into two categories: internal and external. External determinants are factors that represent the economic and regulatory context in which the bank functions, while internal determinants are also referred to as intrinsic performance or microeconomic determinants. This research used a cognitive method to accomplish its goals. This study looks at the factors that affect banks' performance in the banking sector in Tunisia.in an effort to pinpoint the factors and provide helpful recommendations for enhancing profitability performance. Based on our findings, the key factors that affect a bank's success are its size, control, and credit quality.

According to a 2014 study by Rahman et al., banks—which are among the top financial institutions—have a significant role in Bangladesh's financial and economic growth. The performance of Bangladesh's banking industry has drawn a lot of attention lately. It is unquestionably a significant issue. The three main factors used to assess a bank's success are profitability, productivity, and the risks related to these two factors. The goal of this research was to determine NCB performance in a relatively short amount of time (2008 to 2012). In Bangladesh, there are four commercially nationalized banks. Three banks have been selected for this research study's convenience. The research uses data from secondary sources.

In their 2017 study, Daoud and Kammoun examined the Tunisian Islamic banking industry's financial results from 2010 to 2014. In Tunisia, Islamic banking is relatively recent compared to traditional banking. The performance was classified using the descriptive statistical measures of mean, standard deviation, and coefficient of variation, which reflect the variability and dispersion of these ratios. The outcome shows that over the examined time, both banks maintained a strong financial performance position in the banking sector. In contrast, Baraka Bank's profitability and risk management are somewhat higher than ZBL Bank's. Both Islamic banks are

generally financially sound, however in terms of stability, Al Baraka Bank is in a better position than ZBL Bank.

Between 2015 and 2019, Akber and Dey (2020) conducted an analysis and evaluation of the performance of Islamic banks and traditional private microfinance organizations in Bangladesh. The CAMEL test served as the foundation for the analysis in this work. Every pertinent piece of information was gathered from the bank's websites. This article employed a sample of five Islamic banks and five conventional private microfinance organizations to assess and evaluate the performance. It took each year's average ratio into account. Islamic and conventional private microfinance organizations have had their performance examined using a common test structure called the CAMELS tests. T-tests have been utilized in this study to support the data's dependability. Based on the CAMEL test, the paper's conclusion is that, other from management quality, there is no discernible difference between the performance of Islamic banks and conventional private microfinance firms in Bangladesh. When it comes to asset quality and managerial caliber, traditional private microfinance firms outperform Islamic banks in Bangladesh in terms of capital adequacy and liquidity.

Gazi et al. (2022) used the established CAMELS grading method to determine the position based on each individual's financial performance both before to and throughout the COVID-19 period. During both eras, AIBL, SKBBL, and BBL performed almost independently better. Regarding bank profitability, our article found that high rates of non-performing loans, retaining more liquid assets, having a large amount of capital put aside for hedging, and having an inappropriately small bank all reduced the profitability of the banks during the COVID-19 epidemic. By contrast, the bank's profits during this time was boosted by a low inflation rate and debt situation. The study's findings will assist bank regulators in identifying weak points and implementing preventative actions that will increase banks' profitability during a crisis like COVID-19. The portfolios of depositors and investors in banks are precisely customizable.

In Kithandi's analysis from 2022, the impact of reserve ratio requirements, repo rates, and changes in central bank rates on the financial performance of microfinance companies in Kenya were all examined. A descriptive longitudinal research approach

was adopted in the study. The forty-two microfinance organizations that have been granted operating licenses in Kenya by the Central Bank of Kenya comprised the entire population. The study used a variety of research tests; the normalcy test, quantile-quantile plot, and Durbin-Watson tests were used to analyze the research findings. The research discovered a negative correlation between the Central Bank rate, the need for a cash reserve ratio, and the return on equity (financial performance) of Kenyan microfinance enterprises. The study's conclusions also demonstrated a favorable correlation between the repo rate and the return on equity, or financial success, of Kenyan microfinance firms. The study's conclusion was that Kenyan microfinance enterprises' financial performance and profitability are impacted by monetary policy. The research suggests that the central bank should monitor and maintain a low central bank rate in order to boost economic development.

2.3 Summary of Literature Review

Author	Titles	Year	Methodology	Major Findings
Said, R.M., & Tumin, M.H.	Performance and Financial Ratios of Microfinance Companies in Malaysia and China	2007	Ratio analysis and regression analysis	The results imply that the ratios employed in this study have different effects on the performance of banks in both countries, except for credit and capital ratios.
Sangmi, M., & Nazir, T.	Analyzing Financial Performance of Microfinance	2010	CAMEL parameters model	The position of the banks under study is sound and satisfactory

	Companies in India: Application of CAMEL Model			in terms of capital adequacy, asset quality, management capability, and liquidity.
Kumbirai, M., & Webb, R.	A Financial Ratio Analysis of Commercial Banks	2010	Descriptive financial ratio analysis	Overall bank performance increased considerably in the first two years of the analysis. A significant change in trend was noticed at the onset of the global financial crisis in 2007.
Shrestha, B	A Comparative Analysis of Financial Performance of Banks	2010	Comparative research approach	SKBBL (Siddhartha Bank) demonstrated better solvency than HBL (Himalayan Bank) and Nepal SBI. SKBBL's earnings per share also outperformed

				other selected joint venture banks.
Zergaw, L.N	Financial Performance Analysis: The Case of Bank of Abyssinia Versus Other Private Microfinance Companies in Ethiopia	2010	Comparative analysis	Weak performance was consistently reported across all financial ratios (profitability, liquidity, risk, solvency efficiency, and credit quality) analyzed.
Almazari, A. A.	Financial Performance Evaluation of Some Selected Jordanian Banks	2011	Simple regression method	Higher total deposits, credits, assets, and shareholders' equity did not always correlate with better profitability performance. However, there was a positive correlation between financial performance and asset size, utilization, and

				operational efficiency.
Jha, S., & Hui, X.	A Comparison of Financial Performance of Microfinance Companies	2012	Multivariate regression analysis	Public sector banks were significantly less efficient than their domestic private counterparts, but equally efficient compared to foreign-owned (joint venture) banks. Return on assets was significantly influenced by capital adequacy ratio, which had a considerable effect on return on equity.
Francis, M.E	Determinants of Commercial Bank Performance in Sub-Saharan Africa	2013	Panel Random Effects Method	Both bank-specific and macroeconomic factors influenced bank total factor productivity growth over the study period.

Alkhatib, A.	Financial Performance of Palestinian Microfinance Companies	2012	Correlation and multiple regression analysis	Asset size, credit risk, operational efficiency, and asset management had varying impacts on market financial performance, measured by ROA and Tobin's Q Model.
Nedunchezhiyan, D. V., & Premalatha, M. K.	Analysis and Impact of Financial Performance of Commercial Banks After Merger in India	2013	Ratio analysis and T-test methodology	While analyzing the growth of debt-equity ratio, all selections except India Overseas Banks showed less improvement after mergers. The current ratio and quick ratio of all selected banks exhibited better performance post-merger.

Ongore, V.O., & Kusa, G.B.	Determinants of Financial Performance of Microfinance Companies in Kenya	2013	Linear multiple regression model and Generalized Least Squares on panel data	Banks' specific factors played a significant role in determining financial performance.
Nassreddine, G., Fatma, S., and Anis, J.	Determinants of Banks Performance: Viewing Test by Cognitive Mapping Technique	2013	Cognitive approach	Result, size, control, and credit quality are important variables that determine bank performance.
Rahman1, M.I., Adhakary, D., & Yousuf, S.	Productivity and Profitability Analysis of Nationalized Commercial Banks (NCB) in Bangladesh	2014	Comparative and descriptive research design	General public confidence in the soundness of NCBs remains unimpaired, contributing to increased financial strength.
Daoud, Y., & Kammoun, A.	Financial Performance Analysis of Islamic Banks in Tunisia	2017	Comparative analysis	No significant difference in profitability levels between Islamic banks.
Shrestha, A	Financial Performance of Microfinance	2018	Descriptive and analytical research	SCBL efficiently controls

	Companies		designs	expenses and maintains an appropriate service policy. SCBL performs better in operations and profit maximization.
Akber, S. M., & Dey, A.	Evaluation of the Financial Performance Between Traditional Private Microfinance Companies and Islamic Banks in Bangladesh	2020	CAMEL tests	Apart from management quality, no significant difference exists between the performance of Islamic banks and traditional private microfinance companies in Bangladesh. Islamic banks excel in capital adequacy and liquidity.
Yusuf, M., & Ichsan, R. N.	Analysis of Banking Performance in the Aftermath of the Merger of Bank Syariah	2021	Statistical descriptive test, ROA analysis	Variables (NPF, FDR, BOPO, and CAR) significantly impact the financial

	Indonesia During COVID-19			performance of Sharia microfinance companies in Indonesia during the period 2011-2020.
Kithandi, C.K.	Monetary Policy and Financial Performance of Microfinance Companies in Kenya	2022	Descriptive longitudinal research design	Negative relationship between Central Bank rate, cash reserve ratio requirement, and return on equity for microfinance companies in Kenya. Positive relationship between repo rate and return on equity.
Gazi, M. A. I., Nahiduzzaman, M., Harymawan, I., Masud, A. A., & Dhar, B. K.	Impact of COVID-19 on Financial Performance and Profitability of Banking Sector in Bangladesh	2022	Standardized CAMELS rating system, fixed-effect regression model	During the pandemic, high non-performing loan rates, more liquid assets, and excessive hedging capital reduced bank profitability. Low leverage position and

				inflation rate enhanced profitability.

2.4 Research Gap

This section shows the gaps between this study and the study that done in previous. Empirical review for this research provides background information of microfinance companies performance in general and concentrates specifically on profitability and total factor productivity measures. There is sample evidence of comprehensive account of microfinance companies performance in developed countries and a few of the emerging ones, but less of Nepal, signifying the requirement for further research on the sub- region. There is extensive literature on bank profitability and total factor productivity growth measurements which provide support that these measures are influenced by both internal, sector specific as well as microeconomic factors. Whereas extensive research has been done in developed countries using larger scope and robust econometric methods and regression analysis, such studied in Nepalese financial system are lacking. On this topic Information on Nepalese banking system seems to be scantly and limiting in terms of scope and type correlation regression to adequately study banking system improvement in Nepal. There is various study on comparative analysis of financial performance of microfinance companies but less study on determinants of financial performance of microfinance companies in Nepal. In light of these knowledge gaps and methodological requirements, the thesis sought to provide additional empirical evidence using a three sample microfinance companies drawn from 26 microfinance companies and applying descriptive research methods.

CHAPTER - III

RESEARCH METHODOLOGY

The research approach used in this thesis is covered in this chapter. This chapter also includes a description of the procedures used in the data collection and analysis processes. The specifics of the research approach used for this study are listed below.

3.1 Research Design

It is the investigation's strategy and structure that are created in a manner that allows a researcher to find the answers to research questions. The entire research program is outlined in the plan. According to Adhikari and Pandey (2020), the process involves a series of steps, including issue identification, data collecting, measurement, analysis, and selection of data analysis methodologies, followed by conclusion and generalization of results depending on available resources and tools. Descriptive and causal comparative research designs form the basis of this investigation. Using descriptive analysis, the facts and behaviors of the variables under investigation have been examined. Correlation study design is also used to investigate the direction and strength of the link between the financial performance of Nepalese microfinance organizations and variables influencing it. Lastly, the explanatory power of bank-specific characteristics for explaining the financial performance of Nepalese microfinance enterprises is assessed using the causal comparative study methodology.

3.2 Population and Sample and Sampling Design

Population refers to all observations or units that are within the purview of the investigation (Adhikari & Pandey, 2020). The population of our research consists of the 57 microfinance organizations that exist in Nepal at the moment. A sample is a segment of the population that is typical of the whole population and has all of the features of the population (Adhikari & Pandey, 2020). Based on the largest paid-up capital, a sample of three microfinance firms is chosen from among the 57 microfinance companies that are currently operating in the nation and are registered with Nepal Rastra Bank. Purposive sampling was used in the selection of the three samples, which are Sana Kisan Bikas Laghubitta Bittiya Sanstha Limited, Chhimek Laghubitta Bittiya Sanstha Limited, and Nirdhan Utthan Laghubitta Bittiya Sanstha

Limited. These microfinance institutions are chosen as a sample based on capitalization.

3.3 Sources of Data

This research used secondary sources for its data. Secondary data sources included the audited financial reports of the microfinance organizations in the sample, academic thesis papers, books, journals, and websites. Also, some information is gathered from the NRB oversight report.

3.4 Data Collection & Processing Procedure

The secondary data used in the research was supplied by the banks SKBBL, CBBL, and NUBL. Included in it is the annual financial statement, which is given as an annual report. In addition, the NRB's annual report on the supervision of microfinance enterprises is also consulted.

3.5 Data Analysis Tools and Techniques

The nature of the issue statement, or more precisely, the research goals, dictates the technique that will be used in any given research project. The data from 2013–14 to 2022–23 will be analyzed in this research in order to assess the relationship and effect of the independent variable on the dependent variable of sample microfinance enterprises' profitability. For analytical purposes, the sample microfinance organizations' audited financial records spanning ten years are collected. When evaluating financial performance, a descriptive and correlation regression analysis is used to gauge the profitability, capital sufficiency, operational efficiency, liquidity, and credit quality. To ascertain if dependent variables have a significant association with the independent variable, a two-tailed test with a 0.05 threshold of significance is computed. The broad patterns of the data across the sample period will be analyzed using descriptive statistics for the variables. Furthermore, the link between the explained and explanatory factors will be investigated using a correlation matrix. We will employ a multiple linear regression model and t-statistic to ascertain the relative contribution of each independent variable on profitability. The following financial and statistical methods will be used in this research in order to meet its goals:

Statistical Tools

Statistics are measurement, enumerations or estimates of natural phenomenon usually systematically arranged, analyzed and presented as to exhibit important interrelationships among them (Acharya et al., 2076). In this research we use various statistical tools such as mean, standard deviation, percentage, correlation analysis and regression analysis.

Arithmetic Mean (A.M.)

Arithmetic mean is obtained by adding together all the items and by dividing this total by the number of items. It is also called average. Mean has been calculated to describe the position of debt ratio, debt to equity ratio, Interest coverage ratio, liquidity ratio, TETA ratio, market debt ratio, ROA, ROE and ROIC (Middleton, 2022). It is denoted by $\bar{X}$.

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

Where, $\sum X$ denotes sum of numerical values

'n' denotes number of observations

Standard Deviation

The standard deviation is a measure of how much the data in a set differs from the mean, or average, of the set. It is calculated by finding the difference between each data point and the mean, squaring those differences, and then taking the square root of the sum of these squared differences. A small standard deviation indicates that the data is concentrated closely around the mean, while a large standard deviation means that the data is more spread out and less consistent. Standard deviation is often used to understand how much variation or dispersion there is in a set of data.

Coefficient of Variation

Coefficient of Variation (CV) is a relative measure. To compare the variability between two or more series, CV is more appropriate statistical tool.

Mathematically,

$$CV = \frac{\sigma}{\bar{X}} \times 100$$

Correlation Analysis

Correlation analysis is a statistical method used to examine the relationship between two variables. It helps researchers understand whether there is a relationship between the variables and, if so, the strength and direction of that relationship. Correlation analysis can be used to determine whether there is a relationship between variables such as income and education level, or whether there is a relationship between variables such as stress and illness. In research, correlation analysis is often used to understand the relationship between different variables and to make predictions about one variable based on the values of another variable (Godfrey,1980).

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

Interpretation

If calculated r is equal to +1 there is perfect Positive Correlation between two variables and If r is equal to -1 there is perfect Negative Correlation between two variables. If r is equal 0 there is no correlation between two variables or uncorrelated. If r lies between 0.001 to 0.499 there is low degree of Positive Correlation. If r lies between 0.5 to 0.699 there is moderate Positive Correlation. If r lies between 0.70 to 0.999 high degree Positive Correlation. If r lies between -0.499 to -0.001 there is low degree of Negative Correlation. If r lies between -0.699 to -0.5 there is moderate Negative Correlation. If r lies between -0.999 to -0.7 high degree Negative Correlation.

Regression Analysis

Regression analysis is a statistical method used to understand the relationship between two variables. It involves examining the relationship between a dependent variable and one or more independent variables. The goal of regression analysis is to understand how changes in the independent variables are related to changes in the dependent variable. For example, regression analysis might be used to understand how changes in the price of a product are related to changes in the demand for the product. In this case, the dependent variable would be demand, and the independent variable would be price. Regression analysis can be used to make predictions about the dependent variable based on the values of the independent variables (Freund et al., 2006).

In order to accomplish the goals of this research, there are four independent variables and one dependent variable. This study's main goal is to identify correlations between variables and determine how determinant variables affect profitability. The following is the research model:

$$ROA_{it} = \beta 0 + \beta 1ME_{it} + \beta 2LIQ_{it} + \beta 3CR_{it} + \beta 4AQ_{it} + e_{it} \quad \ldots\ldots\ldots (1)$$

Where,

ROA_{it} = the return on assets of the bank i for year t,

βi = the coefficient of bank specific variable to be estimated,

ME_{it} = the management efficiency of the bank i for year t,

LIQ_{it} = the liquidity of the bank i for year t,

CR_{it} = the credit risk of the bank i for year t,

AQ_{it} = the assets quality of the bank i for year t,

e_{it} = the residual error term.

$\beta 1$ - $\beta 4$= Beta coefficient of four independent variable one to four respective

3.6 Research Framework and Definition of Variables

A condensed conceptual framework that postulates the connection between financial performance and its factors is presented in this section. The financial ratio approach is often used to evaluate a company's performance as it offers a concise summary of the company's financial performance relative to prior periods and enhances managerial performance. The dependent variable in this research was the return on assets (ROA), which is a measure of the financial success of microfinance enterprises in Nepal. Finding out how bank-specific variables affect Nepalese microfinance enterprises' financial success is the goal of this research. Therefore, the explanatory factors in this research were bank-specific variables, which are determined by credit risk (CR), liquidity (LIQ), management efficiency (ME), and asset quality (AQ).

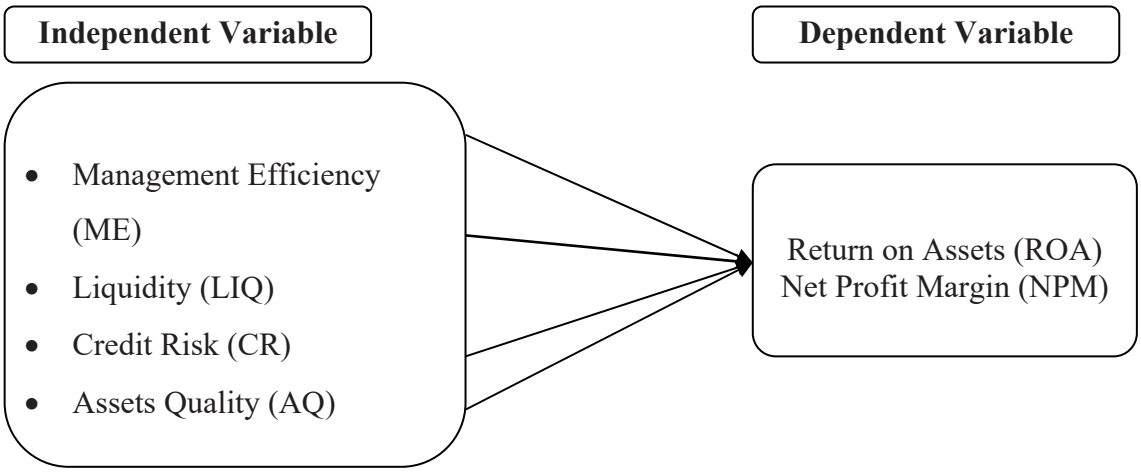

Figure 1: Theoretical Framework

Source: Akber and Dey (2020)

3.6.1 Definition of Variable

Return on Assets

Return on assets (ROA) has been employed in this research as a stand-in for financial performance of Nepalese microfinance institutions. ROA is a commonly utilized metric to assess the financial performance of businesses as it serves as an indication of profitability. It just compares the company's earnings with its total assets. Return on assets, then, demonstrates how well a company uses its resources to produce revenue. Put differently, it demonstrates how effectively management generates revenue from the organization's assets (Alkhatib, 2012).

Management Efficiency

Management efficiency (ME) is the ratio of an organization's production to its capital and assets as determined by the management team. It is among the key elements influencing the bank's financial performance. The management system, organizational discipline, cost control system, staff quality, etc. are often used to monitor it. The effectiveness of the organization's management may also be assessed using a variety of metrics, including growth in assets, earnings, profit, etc., despite the fact that this is a highly complicated and qualitative phenomena. The management efficiency in this research is determined by dividing net income by total revenue (Rahman et al., 2014).

Liquidity

Liquidity (LIQ) ratio is another significant bank-specific factor that influences the bank's financial performance. The loan to deposit ratio is often used to gauge a bank's liquidity. Customers' deposits are used by microfinance firms to provide loans. If the bank uses a large quantity of deposits to create loans, this will result in a high liquidity ratio, which may not be sufficient to support customers' unforeseen future withdrawals. Therefore, a bank with significant liquidity also has a high credit risk, which raises the bank's profitability. The ratio of total loans to total deposits is used in this research to determine the bank's liquidity (Francis, 2013).

Credit Risk

Credit Risk Bank has reserves on hand to cover losses resulting from non-performing loans. Credit risk (CR) is always linked to the loan that the bank has approved. Therefore, the bank keeps what is known as a loan loss provision in order to mitigate this kind of credit risk. According to Nassreddine et al. (2013), the ratio of loan loss provision to total loan is used in this research as a stand-in for credit risk.

Assets Quality

Asset quality (AQ) is a crucial factor that significantly affects the bank's financial performance. The bank's portfolio of loans, investments, current assets, and fixed assets made up its assets. The portfolio of loans is the primary source of income for the bank among these assets. As a result, the bank's asset quality is determined by the quality of its loan portfolio, or earning assets. A loan of poor quality has a greater chance of being non-performing. According to Alkhatib (2012), the ratio of non-performing loans to total loans is the most accurate indicator of the quality of a bank's assets.

CHAPTER- IV

DATA PRESENTATION AND ANALYSIS

4.1 Data Presentation and Analysis

In order to make the study effort more understandable, this chapter deals with the presentation, analysis, and interpretation of statistical data and facts. Multiple regression models, correlation analysis, and descriptive statistics were used to examine the data. Tables and appropriate graphs are also used to display the data and findings.

Table 1

Return on Assets of SKBBL, CBBL and NUBL

Year	SKBBL	CBBL	NUBL
2013/14	2.11	1.60	2.80
2014/15	2.39	2.60	3.25
2015/16	2.25	2.30	2.65
2016/17	1.85	1.90	2.06
2017/18	1.85	2.00	2.32
2018/19	1.83	2.10	2.69
2019/20	1.97	2.13	2.61
2020/21	1.94	1.79	2.11
2021/22	1.42	1.19	1.58
2022/23	0.89	1.56	1.71
Mean	1.79	1.91	2.32
SD	0.43	0.41	0.52
CV (%)	23.87	21.59	22.32

Sources: Annual report of sample microfinance companies from fiscal year 2013/14 to 2022/23

Table 1 displays the sample microfinance enterprises' returns on assets. From 2013–14 to 2022–23, the sample microfinance organizations' average return on assets was 1.79%, 1.91%, and 2.32% for SKBBL, CBBL, and NUBL, respectively.

Additionally demonstrates how microfinance firms' success is represented by ROA, which decreased from 2013–14 to 2016–17. After seeming steady at 2.17% in 2017–18, ROA showed a growing tendency there. From 2017–19, it showed a little increase, and in 2018–19, it performed better at a high return on assets across ten-year periods. The ROA of the sample microfinance firms seems to be declining from 2019–20 to 2022–2023.

Table 2

Net Profit Margin of SKBBL, CBBL and NUBL

Year	SKBBL	CBBL	NUBL
2013/14	19.80	15.50	23.74
2014/15	26.45	28.30	32.66
2015/16	26.63	27.80	33.49
2016/17	27.20	28.10	29.93
2017/18	28.88	31.00	37.30
2018/19	25.75	47.10	39.22
2019/20	22.86	46.10	31.12
2020/21	21.13	39.82	24.25
2021/22	16.25	30.00	18.55
2022/23	13.54	42.39	21.72
Mean	22.27	34.83	28.44
SD	5.09	8.13	6.87
CV (%)	22.87	23.36	24.15

Source: Annual report of sample microfinance companies, 2013/14 to 2022/23.

According to Table 2, from 2013–14 to 2022–23, the average net profit margin (NPM) of microfinance enterprises was 22.27%, 34.83%, and 28.44% of SKBBL, CBBL, and NUBL, respectively. Additionally, it exhibits a little increase in 2015–16 and a slight decrease in 2016–17. The remarkable rise in microfinance company performance in 2017–18 is followed by a gradual decline in 2018–19, 2019–20, and a declining trend in 2022–2023.

Table 3

Credit Risk of SKBBL, CBBL and NUBL

Year	SKBBL	CBBL	NUBL
2013/14	0.84	3.32	2.33
2014/15	0.62	1.91	2.13
2015/16	0.97	1.77	2.23
2016/17	0.66	1.25	1.82
2017/18	0.38	0.68	1.14
2018/19	0.25	0.83	0.80
2019/20	0.20	1.36	0.55
2020/21	0.16	2.78	0.74
2021/22	0.22	2.91	0.98
2022/23	0.12	2.46	0.84
Mean	0.35	1.71	1.20
SD	0.31	0.91	0.69
CV (%)	87.98	53.31	57.77

Source: Annual report of sample microfinance companies, 2013/14 to 2022/23.

Table 3 displays the credit risk of the sample microfinance enterprises. According to Table 3, from 2013–14 to 2022–23, the average credit risk of microfinance enterprises was 0.35%, 1.71%, and 1.20% of SKBBL, CBBL, and NUBL, respectively.

Table 4

Liquidity Risk of SKBBL, CBBL and NUBL

Year	SKBBL	CBBL	NUBL
2013/14	73.22	77.60	77.91
2014/15	76.57	74.70	74.90
2015/16	78.01	71.97	74.55
2016/17	66.63	72.93	64.43
2017/18	73.52	75.12	70.49
2018/19	84.05	75.30	65.38
2019/20	81.86	76.40	82.66
2020/21	87.01	72.40	81.96
2021/22	83.52	74.70	79.72
2022/23	85.30	80.10	89.84
Mean	78.72	74.81	75.81
SD	6.51	2.46	7.95
CV (%)	8.27	3.28	10.49

Source: Annual report of sample microfinance companies, 2013/14 to 2022/23.

Liquidity risk of sample microfinance companies are presented on the table 4. The average liquidity risk of sample microfinance companies is 78.72%, 74.81%, and 75.81% of SKBBL, CBBL and NUBL respectively on 2013/14 to 2022/23.

Table 5

Operating Cost (OC) of SKBBL, CBBL and NUBL

Year	SKBBL	CBBL	NUBL
2013/14	6.62	1.23	6.73
2014/15	4.79	1.22	4.84
2015/16	4.71	1.13	3.56
2016/17	3.39	1.01	3.53
2017/18	2.75	0.95	2.64
2018/19	4.15	0.90	3.40
2019/20	5.16	1.30	4.93
2020/21	5.86	1.40	5.49
2021/22	6.14	1.30	5.80
2022/23	4.85	1.20	5.22
Mean	5.18	1.15	4.44
SD	0.80	0.16	1.28
CV (%)	15.38	14.22	28.88

Source: Annual report of sample microfinance companies, 2013/14 to 2022/23.

Operating cost of sample microfinance companies are presented on the table 5. The average operating cost of sample microfinance companies are 5.18%, 1.15%, and 4.44% of SKBBL, CBBL and NUBL respectively on 2013/14 to 2022/23.

Table 6

Capital Adequacy Ratio of SKBBL, CBBL and NUBL

Year	SKBBL	CBBL	NUBL
2013/14	11.02	11.49	11.01
2014/15	11.59	11.27	11.59
2015/16	11.31	11.90	11.18
2016/17	13.33	14.92	11.57
2017/18	12.66	13.02	11.73
2018/19	14.54	13.02	12.90
2019/20	14.20	12.66	13.00
2020/21	13.74	13.26	12.50
2021/22	13.38	13.54	13.07
2022/23	12.47	14.71	12.77
Mean	12.77	12.93	12.11
SD	1.22	1.23	0.80
CV (%)	9.58	9.50	6.57

Source: Annual report of sample microfinance companies from fiscal year 2013/14 to 2022/23

Capital adequacy of sample microfinance companies are presented on the table 6. The average capital adequacy of sample microfinance companies with in ten-year periods are 12.77%, 12.93%, and 12.11% of SKBBL, CBBL and NUBL respectively on 2013/14 to 2022/23.

4.2 Descriptive Statistics

The variable used in this study's descriptive statistics are shown in Table 7. The variables' computations are done using ratios and percentage points. In order to assess the financial performance of microfinance companies in Nepal, this study looked at return on assets and net profit margin as dependent variables. Credit risk, liquidity risk, operating costs, and capital adequacy ratio were considered independent

variables that determine financial performance. This research takes into account the mean, minimum, maximum, and standard deviation of each variable. Table No. 4.7 displays the descriptive findings results.

Table 7

Descriptive Statistics of PM, CR, LR, OC, CAR and ROA

	N	Minimum	Maximum	Mean	Std. Deviation
PM	30	13.54	47.10	28.5527	8.58395
CR	30	.12	3.32	1.2417	.90728
LR	30	64.43	89.84	76.7583	6.11449
OC	30	.90	6.73	3.5400	1.97376
CAR	30	11.01	14.92	12.6450	1.12646
ROA	30	.89	3.25	2.0483	.49814
Valid N (listwise) 30					

Table 7 shows that there were 21 observations from three sample microfinance organizations for each variable. The ratio of net income to total asset is used to calculate return on asset. The ROIA (return on average) is 2.04%. This indicates that there is, on average, a 0.0204 rupee return for every rupee invested in the asset. The annual return on assets has a maximum value of 3.25% and a minimum value of 0.89%. Additionally, there is variance from the mean as shown by the standard deviation, which is 0.498.

Additionally, the profit margin—which reveals pricing tactics and cost-control measures—is included in the descriptive statistics. A net profit of 0.2855 rupees is earned for every rupee of revenue, according to the mean PM value of 28.552%. There is variance in NPM from its mean, as seen by the lowest and highest values of 13.54% and 47.10%, respectively, with a standard deviation of 8.58.

The percentage of non-performance loans to total loans serves as a proxy for credit risk. The studied microfinance organizations had an average credit risk of 1.2417%. This shows that, on average, 1.2417% of all loans invested are non-performance loans. While banks confront a minimum credit risk of 0.12%, microfinance

enterprises have a maximum credit risk of 3.32%, indicating inferior asset quality. The standard deviation of this difference is 0.907, indicating a divergence from the mean value.

According to the descriptive data for liquidity risk, the average annual percentage rate of loan availability and total deposit for client loans is 76.76%. This indicates that 76.76% of deposits in the majority of microfinance firms in the market are used to fund consumer loans. The liquidity deposit ratio has maximum and lowest values of 89.84% and 64.43%, respectively. Its standard deviation is 6.114, indicating that there are significant deviations from the mean. This suggests that the average liquidity to deposit position of Nepalese microfinance enterprises is greater.

In addition, the average ratio of operating costs to total assets is 3.54%. This suggests that in order to deliver their financial services, the majority of the microfinance in the sample had operational expenditures of 3.54%. Stated otherwise, the bank's operational expenditures for providing its financial service came to a total of.0354 rupees. Operating costs for the most efficient microfinance were 0.90%, while those for the least efficient microfinance were 6.73%. This suggests that effective microfinance has an advantage over inefficient microfinance in terms of cost control. There is variance from the mean, as shown by the standard deviation of 1.973.

The total risk weighted assets should be the foundation for maintaining capital adequacy. D class microfinance enterprises are required by the Nepal Rastra bank to maintain a capital fund of 19% of their total risk-weighted assets. Table 7 illustrates that the average capital adequacy of the sample microfinance firms is 12.64%, indicating that the majority of microfinance companies meet the capital adequacy ratio criterion. The departure from the averages is shown by the standard deviation of 1.126, which is between the maximum and lowest capital adequacy of 14.92% and 11.01%. This result demonstrates that the majority of typical microfinance has met the capital adequacy minimal requirements.

4.3 Correlation Analysis of the Profitability and Explanatory Variables

The linear link between two variables is measured by the correlation coefficient. good relationships have an upward slope, and negative relationships have a downward slope. The nature of the connection might be either good or negative. The degree of correlation between the independent and dependent variables is ascertained for this

study using Pearson correlation. To ascertain if there is a significant link between the dependent and independent variables, two-tailed tests with a 0.05 threshold of significance will be computed.

4.3.1 Correlation Analysis of ROA among Independent Variables.

Table 8

Correlation Matrix between ROA and Independent Variables

		ROA	CR	LR	OC	CAR
ROA	Pearson Correlation	1				
	Sig. (2-tailed)					
CR	Pearson Correlation	-.353	1			
	Sig. (2-tailed)	.117				
LR	Pearson Correlation	-.287	-.141	1		
	Sig. (2-tailed)	.207	.543			
OC	Pearson Correlation	.432*	.212	-.103	1	
	Sig. (2-tailed)	.05	.355	.658		
CAR	Pearson Correlation	-.126	-.166	.624**	-.507*	1
	Sig. (2-tailed)	.587	.472	.003	.019	

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

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

Table 8 shows that the variable that has the most positive correlation with return on assets is operational cost. This association demonstrates unequivocally that return on assets improves in tandem with those variables. Given that the significant value of the variables is equal to or less than the significance value of 0.05, a connection is considered significant if it is more than 0.05. Operating cost has a positive significant association with return on assets, as shown by the table, and is significant at the level of 0.05, which is lower than the significance threshold. Whether the significant value of capital sufficiency, credit risk, and liquidity risk is more than 0.05. Return on assets and these variables have a negative, negligible connection, respectively. This

implies that return on assets will rise in tandem with the decrease in the capital adequacy ratio, credit risk, and liquidity risk.

4.3.2 Correlation Analysis

Table 9

Correlation Matrix Between NPM and Independent Variable

		NPM	CR	LR	OC	CAR
NPM	Pearson Correlation	1				
	Sig. (2-tailed)					
CR	Pearson Correlation	-.410	1			
	Sig. (2-tailed)	.065				
LR	Pearson Correlation	-.468*	-.141	1		
	Sig. (2-tailed)	.032	.543			
OC	Pearson Correlation	.315	.212	-.103	1	
	Sig. (2-tailed)	.164	.355	.658		
CAR	Pearson Correlation	-.492*	-.166	.624**	-.507*	1
	Sig. (2-tailed)	.023	.472	.003	.019	

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

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

Table 9 illustrates that the variables that have the most positive correlation with net profit margin are capital sufficiency and liquidity risk. However, there seems to be a negative association between the measurements of net profit margin and credit risk and operational costs. This means that when these variables rise, net profit margin moves in the other way, and an increase in CAR and LR raises NPM and vice versa. The variables have a significant value of equal to or less than 0.05; a value greater than 0.05 is considered inconsequential. The table indicates that the significant values of 0.023 and 0.032 for CAR and LR are below the significance threshold. Additionally, the significant value for variables OC and CR is higher than 0.05. This indicates that these variables and NPM have a negative insignificance relationship.

4.4 Regression Analysis

The link between profitability and the variables influencing the financial performance of microfinance firms in Nepal has been investigated using multiple regression analysis. The purpose of regression analysis is to determine how independent variables, or predictors, affect the dependent variables. With the use of regression, one may determine which linear equation incorporating one or more independent variables has the best coefficients for predicting the values of the dependent variables. The coefficient of determination may be defined as the proportion of variance in the dependent variables (ROA, NPM) that can be explained by the independent variables (CR, LR, OC, CAR) or as the change in the independent variables.

Table 10

Model Summary of Return on Assets

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.669[a]	.448	.310	.41680

a. Predictors: (Constant), CAR, OC, LR, CR

Table 10 displays the model 1 fitness indicators. The correlation coefficient (R) between the independent variables and ROA is 0.669, indicating a strong positive association. With an R-squared of 0.448, the model is able to account for 44.8% of the variables or changes in the dependent variables of ROA. Put otherwise, operational expenses, capital sufficiency, credit risk, and liquidity risk combined may account for 44.8% of the variation in ROA, with additional factors not included in this research accounting for the remaining 44.8%.

Table 11

ANOVA Result of Return on Assets

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.256	4	.564	3.247	.000[b]
	Residual	2.779	25	.174		
	Total	5.035	29			

a. Dependent Variable: ROA

b. Predictors: (Constant), CAR, OC, LR, CR

The likelihood that the observed F-value would occur by chance if there was no true association between the independent and dependent variables is shown by this p-value. The model is considered statistically significant at the 0.05 level if the significance threshold is set at 0.000. This indicates that ROA is significantly impacted by the independent factors taken as a whole.

Table 12

Regression Analysis Result of ROA and Independent Variable

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	5.118	1.138		4.497	.000
	CR	-.200	.121	-.32	-1.65	.119
	LR	-.010	.016	-.16	-.64	.529
	OC	-.026	.011	-.57	-2.45	.026
	CAR	-.134	.106	-.36	-1.26	.023

a. Dependent Variable: ROA

Model 1

$ROA = \alpha + \beta1\ (CAR) + \beta2\ (CR) + \beta3\ (LR) + \beta4\ (OC) + e$

Become to Model 1

ROA= 5.118 -0.134(CAR) -0.200(CR) -0.01(LR) -0.026(OC)

The findings of a regression study evaluating the influence of many independent factors on Return on Assets (ROA) are shown in Table 12. The Capital Adequacy Ratio (CAR), Operating Cost (OC), Liquidity Ratio (LR), and Current Ratio (CR) are the independent variables. The results of the regression model include t-values, significance levels (Sig.), and both standardized and unstandardized coefficients.

Since the unstandardized coefficient for the CR is -0.200, it may be inferred that a unit rise in CR causes a 0.200 drop in ROA. The impact of CR on ROA is not statistically significant at the traditional 0.05 level, as shown by the t-value of -1.65 at a significance level of 0.119.

The LR has a somewhat negative effect on ROA, with an unstandardized value of -0.010 and a standardized coefficient of -0.16. There is no statistically significant evidence for this influence, according to the t-value of -0.64 and a significance level of 0.529.

On the other hand, OC has a reasonably large negative influence on ROA, with an unstandardized value of -0.026 and a standardized coefficient of -0.57. The effect of OC on ROA is statistically significant at the 0.05 level, as shown by the t-value of -2.45 and the significance level of 0.026.

Lastly, the standardized coefficient for CAR is -0.36 while the unstandardized coefficient is -0.134. This points to a somewhat detrimental effect on ROA. The impact of CAR on ROA is statistically significant at the 0.05 level, according to the t-value of -1.26 and the significance level of 0.023.

Table 13

Model Summary of Net Profit Margin

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
2	.776[a]	.603	.503	5.86854

a. Predictors: (Constant), CAR, OC, LR, CR

The model 2 fitness indicators are shown in Table 13. The correlation coefficient (R) between the independent variables and NPM is 0.776, indicating a significant positive link. A coefficient of determination (R-square) of 0.603 suggests that 60.3% of the variables or changes in the NPM dependent variables can be explained by the model. Put otherwise, the combination of credit risk, liquidity risk, capital sufficiency, and operational expenses may account for 60.3% of the variation in NPM. The remaining 39.7% can be explained by factors not included in this research.

Table 14

ANOVA Result of Net Profit Margin

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	836.167	4	209.042	6.070	.000b
	Residual	551.036	25	34.440		
	Total	1387.203	29			

a. Dependent Variable: NPM

b. Predictors: (Constant), CAR, OC, LR, CR

The analysis of variance (ANOVA) on how CR, LR, OC, and CAR affect ROA and NPM is shown in Table 14. The model is statistically significant in describing the relationship between operational costs, credit risk, liquidity risk, and capital adequacy ratio and the profitability of microfinance enterprises in Nepal, according to the findings of sign value 0.000. This indicates that, at the 0.05 level of significance, the ANOVA findings show that the combined influence of CAR, CR, OC, and LR is statistically significant in explaining the financial success of microfinance enterprises.

Table 15

Regression Analysis Result of NPM and Independent Variables

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	82.488	16.03		5.15	.000
	CR	-5.889	1.71	-.56	-3.45	.003
	LR	-.419	.22	-.40	-1.89	.078
	OC	.231	.15	.30	1.54	.143
	CAR	-1.104	1.49	-.18	-.74	.472

a. Dependent Variable: NPM

And Model 2

$NPM = \alpha + \beta1\ (CAR) + \beta2\ (CR) + \beta3\ (LR) + \beta4\ (OC) + e$

Model 2

$NPM = 82.488 - 1.104(CAR) - 5.889(CR) - 0.419(LR) + 0.231(OC)$

The findings of a regression study that looked at how numerous independent factors affected Net Profit Margin (NPM) are shown in Table 15. The capital adequacy ratio (CAR), operating cost (OC), liquidity ratio (LR), and current ratio (CR) are the independent variables taken into account in this model. T-values, significance levels (Sig.), and unstandardized and standardized coefficients are all included in the table.

With a p-value of 0.000, the unstandardized coefficient, which begins with the constant term, is 82.488. This result is very significant. This suggests that the NPM would be 82.488 if all of the independent variables were zero.

An increase of one unit in the CR is thought to cause a 5.889 fall in NPM, according to the CR's unstandardized coefficient of -5.8889. The effect of CR on NPM is statistically significant at the 0.01 level, as shown by the t-value of -3.45 and the significance level of 0.003.

The LR has a somewhat negative impact on NPM, as seen by its standardized coefficient of -0.40 and unstandardized coefficient of -0.419. This influence is marginally significant, but not statistically significant at the 0.05 level, with a t-value of -1.89 and a significance level of 0.078.

On the other hand, OC has a positive impact on NPM with an unstandardized value of 0.231 and a standardized coefficient of 0.30. The impact of OC on NPM is not statistically significant, according to the t-value of 1.54 and the significance threshold of 0.143.

Lastly, CAR indicates a marginally negative effect on NPM with an unstandardized value of -1.104 and a standardized coefficient of -0.18. The influence of CAR on NPM is not statistically significant, according to the t-value of -0.74 and the significance threshold of 0.472.

4.5 Findings

The chapter also included an examination of statistical tests, such as t-tests and two-way Anova tests, and this part has offered descriptive data analysis utilizing means, maximum, and minimum Standard deviations, Pearson correlations, and regressions. The following are the study's primary results, which may be seen in the chapters above:

- The study's model, which takes into account the independent variables credit risk (CR), liquidity risk (LR), operating cost (OC), and capital adequacy ratio (CAR), can account for 60.3% of changes in the dependent variable of net profit margin (NPM) and 44.8% of variations in return on assets (ROA). Thus, it may be said that the primary determinants of financial performance are the capital adequacy ratio (CAR), credit risk (CR), operational cost (OC), and liquidity risk (LR).
- Pearson correlation reveals that operating cost (OC) has a significant value less than 0.05, indicating a statistically significant correlation with return on assets (ROA), and the capital adequacy ratio (CAR), credit risk (CR), and liquidity risk (LR) have significant values greater than 0.05, indicating an insignificant relationship with ROA. Conversely, if the capital adequacy ratio (CAR) and liquidity risk (LR) have a significant value smaller than 0.05, it indicates a substantial association with net profit margin (NPM). When the significant values for credit risk (CR) and operating cost (OC) are more than 0.05, it indicates that there is no significant relationship between these variables and net profit margin (NPM).
- The results of the regression demonstrate that the independent variables related to operating cost (OC), with a beta of -0.026, have a statistically significant positive impact on return on assets (ROA), while the independent variables related to capital adequacy ratio (CAR), credit risk (CR), and liquidity risk (LR), with betas of -0.134, -0.26, and -0.10, have a statistically negative insignificant impact on ROA.

- The outcome of the regression analysis also reveals that the only variables that have a statistically significant positive impact on net profit margin (NPM) are credit risk (CR), with a beta of -5.889, and capital adequacy ratio (CAR). Liquidity risk (LR), on the other hand, has a statistically insignificant negative impact on NPM, with betas of -1.104 and -0.419, respectively. With a beta of 0.23, OC has a statistically significant yet favorable effect on NPM.
- The regression equation that was developed states that when all variables are taken into consideration, the operating cost (OC), credit risk (CR), liquidity risk (LR), and capital adequacy ratio (CAR)—which is determined by return on assets (ROA) of 5.118 and net present value of 82.488—are.
- When comparing the financial performance of microfinance firms based on net profit margin (NPM) and return on assets (ROA), NUBL ranks first with 2.56 and 32.57, respectively, indicating that its financial performance is more efficient than that of the other sample microfinance companies. LR and CR both score top on the basis of CAR, with 13.66, 86.06, and 1.85, respectively, indicating that their financial performance is the most efficient among the other microfinance organizations in the sample.

4.6 Discussion

The first research goal demonstrates the correlation between microfinance credit risk and return on assets (ROA); however, the credit risk coefficient, as determined by the non-performance loan to total loan ratio, is statistically significant for NPM but statistically insignificant for ROA. In order to offset the possibility of loss, loans and advances are priced lower the greater the credit risk. Thus, based on the results, we may infer that credit risk was a major factor influencing the profitability of Nepali microfinance firms. On the other hand, Daoud and Kammoun (2017) discovered that there is a relationship between microfinance credit risk and return on assets (ROA). Moreover, the credit risk coefficient, which is determined by the non-performance loan to total loan ratio, is statistically significant for both ROA and NPM.

The relationship between liquidity risk and the profitability of microfinance companies is also demonstrated by the first objectives. As predicted, the coefficient of

liquidity risk, which is determined by the ratio of short-term funding to total loan to deposits, is statistically significant for ROA and statistically insignificant for NPM. This indicates that the bank's lower profits are a reflection of its high liquidity premium. This indicates that low ROA and NPM were earned by the bank with a large liquidity risk. Liquidity risk is likewise statistically significant for ROA and statistically insignificant for NPM, according to Gazi et al. (2022) and Rahman et al. (2014).

The second goal of the study demonstrates how operational costs affect microfinance profitability; nevertheless, the coefficient of operating costs, which is determined by the ratio of overhead expenses to total assets, is statistically significant for return on assets (ROA) but statistically insignificant for net present market (NPM). The positive indicator shows that a significant amount of the operational costs of Nepalese microfinance enterprises are passed on to their depositors and borrowers. In summary, the outcome supports the widely acknowledged claim that microfinance may sustain overall profitability even while running at high expenses. The association between operating cost and ROA is statistically significant for NPM, while it is statistically negligible for ROA, according to research by Nedunchezhian and Premalatha (2013) and Kithandi (2022).

In a similar vein, the study's ultimate goals demonstrate how the capital adequacy ratio affects microfinance enterprises' profitability. However, the total capital to total risk weight assets, which was used to calculate the coefficient of capital adequacy, is statistically insignificant for ROA but not for NPM. The data unequivocally demonstrates that microfinance enterprises' profitability declines as capital adequacy increases. Therefore, the bank shouldn't increase its capital to support microfinance enterprises' stable financial performance. On the other hand, capital adequacy ratio was determined to be statistically significant for ROA but statistically insignificant for NPM by Akber and Dey (2020) and Daoud and Kammoun (2017).

CHAPTER V

SUMMARY, CONCLUSIONS AND RECOMMENDATION

Based on the findings and recommendations of the preceding chapter of this research, this chapter offers the discussion.

5.1 Summary

The primary goals of microfinance firms are to lower the difference between interest rates on deposits and loans by reforming microfinance, making the most use of available resources, and increasing the volume of non-cash reserve transactions. Following the nation's adoption of liberalization measures in 1980, the financial sector in Nepal saw tremendous expansion. This expansion was seen in the number of businesses as well as in the range of goods and services offered and the use of more recent technology. This research aims to investigate the variables that influence Nepalese microfinance enterprises' financial success using empirical means. This study used two indicators—internal-based performance measured by return on assets and net profit margin—to measure factors of financial performance in order to meet its goals of examining determinants of financial performance and determining the relationship and impact of determinant variable on financial performance. Therefore, the explanatory factors in this research were bank-specific variables, which are determined by credit risk (CR), liquidity (LIQ), management efficiency (ME), and asset quality (AQ).

Descriptive and causal comparative research designs form the basis of this investigation. Using descriptive analysis, the facts and behaviors of the variables under investigation have been examined. Correlation study design is also used to investigate the direction and strength of the link between the financial performance of Nepalese microfinance organizations and variables influencing it. Lastly, the explanatory power of bank-specific characteristics for explaining the financial performance of Nepalese microfinance enterprises is assessed using the causal comparative study methodology. In order to determine the effects of credit risk, operating costs, capital adequacy, and liquidity risk on the financial performance measured by the two indicators, the study used multiple regression analysis and correlation of annual time series data from 2013–14 to 2022–23. A well-fitting regression model was then developed to forecast the financial performance of microfinance companies in the future. Three microfinance organizations were chosen as a sample from a total of twenty-six microfinance companies that are now operating in the nation, both public and private, and that are registered with Nepal Rastra Bank. SKBBL, CBBL, and NUBL microfinance samples were chosen using the purposive sampling technique. Based on the microfinance with the biggest capital, these loans are selected as a sample. Secondary sources provided the information for this

investigation. SPSS (Statistical Package for the Social Sciences) is used to gather, organize, and show data on tables, in Excel, and in other formats.

60.3% of the variations or change in the dependent variable of net profit margin and 44.8% of the variation in return on assets can be explained by the study's model, which includes the independent variables capital adequacy ratio, credit risk, liquidity risk, and operational cost. Thus, it may be said that the primary determinants of financial performance are the capital adequacy ratio, credit risk, liquidity risk, and operational costs. According to Pearson correlation analysis, operational costs have a positive and statistically significant link with return on assets, whereas the capital adequacy ratio, credit risk, and liquidity risk have a negative and insignificant association with return on assets. Conversely, there is a large and negative correlation between net profit margin and both liquidity risk and the capital adequacy ratio. Credit risk has a negligible negative relationship with net profit margin, but operational costs have a strong positive relationship. When microfinance firms are ranked according to their return on assets and net profit margin, NUBL Microfinance ranks first, indicating that its financial performance is more efficient than that of the other sample microfinance organizations. Furthermore, compared to the other sample microfinance organizations, Citizen Bank has the most efficient financial performance in terms of capital adequacy ratio, liquidity risk, and credit risk.

5.2 Conclusions

Recommendations have been made about the financial performance of microfinance organizations based on the study's results. There has also been discussion of the study's weaknesses and recommendations for more research. The study's conclusion is provided in the section that follows by outlining the key ideas that address the questions.

Examining the connection between determinants and profitability measures on the financial performance of microfinance enterprises was the first goal. The results show that there is a positive link between operational costs and capital adequacy, whereas there is a negative correlation between credit risk and liquidity risk and return on assets. There is a high and negative correlation between the capital adequacy ratio and liquidity risk and net profit margin. Additionally, there is a substantial positive correlation between operational costs and net profit margin and a negligible negative

correlation with credit risk. The positive and high Pearson correlation coefficient suggests that the factors have a statistically significant impact on the bank's financial performance. This suggests that conclusions about the financial success of microfinance companies—represented by their robust and positive correlation coefficient—are drawn primarily from their profitability.

Assessing the effects of credit risk, liquidity risk, operational costs, and capital sufficiency on the financial performance of microfinance enterprises was the second goal of the study. The study's conclusions indicate that although capital adequacy ratio, credit risk, and liquidity risk have negative minor effects on microfinance enterprises' financial performance (ROA), operational costs have a negative substantial influence. The fact that the coefficients for both variables are negative indicates that there is an inverse link between operational costs and return on assets. The explanatory factors liquidity risk, credit risk, and capital adequacy ratio also have an inverse association with spread to the degree that their coefficient is negative, meaning that a rise in these variables will result in a fall in return on assets. The financial performance (NPM) of microfinance enterprises is negatively impacted by credit risk, which also has a negative substantial influence. Liquidity risk, capital adequacy ratio, and operational costs have a negative negligible impact. As long as the correlation variables are negative, it indicates that the capital adequacy ratio, credit risk, liquidity risk, and net profit margin have an inverse connection. Therefore, although the explanatory variable operating cost has a direct link with spread to the degree that its coefficient is positive, increasing these factors will result in a fall in net profit margin.

5.3 Recommendation

Based on the study following recommendation were forwarded;

- The study found that ROA and NPM are the most significant factors influencing financial performance of microfinance companies in Nepal.
- Microfinance generally needs to maintain an optimum level of CAR (or as per regulatory requirement) so that they will not have difficulty meeting their financial obligations, protect their depositors' investment, and thus promote the stability of the financial system. To improve the financial performance of microfinance firms in Nepal, the sample microfinance enterprises should

implement strategies for tracking profitability-related metrics such credit risk, liquidity risk, operational cost, and capital sufficiency.

- The research suggests that Nepalese banks take into account LR, OC, CR, and CAR in their plan to enhance financial performance, since the aggregate findings indicate that these factors have a substantial influence on profitability.
- All microfinance, according to CAR, has completed the NRB-mandated capital adequacy ratio. However, it is less than the 19% global average.In order to comply with international standards, it has improved its tire I and tire II capital.

Suggestion for Future Research

These studies look at the variables that affect Nepali microfinance firms' financial success. Nevertheless, not every factor that could have an impact on the dynamics of Nepalese microfinance profitability was included in the set of variables employed in the statistical study. Future studies may thus take into account other bank-specific variables such as market power, reserve requirements, size, leverage, and macro-economic variables like inflation and the gross domestic product in addition to macro-policy environment elements like reserve requirements and discount rates. The following are some implications for further research:

- The microfinance firms in Nepal are primarily responsible for this outcome. Future research may thus carry out this kind of analysis using other financial entities, such as development banks, financial firms, and so on.Similar to this, further research may be conducted with the use of sophisticated statistical techniques.
- Future research, for instance, may make advantage of causality and non-linear statistical methods.Only secondary data were used in this investigation. Therefore, by using primary sources like surveys, questionnaires, special group discussions, etc., future research may be conducted in a more thorough manner. Further research on the qualitative phenomena might be contemplated.
- These factors may be included in further research, which will provide more study results.

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Appendix

1. Return on Assets

Year	SKBBL	CBBL	NUBL
2013/14	2.11	1.60	2.80
2014/15	2.39	2.60	3.25
2015/16	2.25	2.30	2.65
2016/17	1.85	1.90	2.06
2017/18	1.85	2.00	2.32
2018/19	1.83	2.10	2.69
2019/20	1.97	2.13	2.61
2020/21	1.94	1.79	2.11
2021/22	1.42	1.19	1.58
2022/23	0.89	1.56	1.71

2. Net Profit Margin

Year	SKBBL	CBBL	NUBL
2013/14	19.80	15.50	23.74
2014/15	26.45	28.30	32.66
2015/16	26.63	27.80	33.49
2016/17	27.20	28.10	29.93
2017/18	28.88	31.00	37.30
2018/19	25.75	47.10	39.22
2019/20	22.86	46.10	31.12
2020/21	21.13	39.82	24.25
2021/22	16.25	30.00	18.55
2022/23	13.54	42.39	21.72

3. Credit Risk

Year	SKBBL	CBBL	NUBL

2013/14	0.84	3.32	2.33
2014/15	0.62	1.91	2.13
2015/16	0.97	1.77	2.23
2016/17	0.66	1.25	1.82
2017/18	0.38	0.68	1.14
2018/19	0.25	0.83	0.80
2019/20	0.20	1.36	0.55
2020/21	0.16	2.78	0.74
2021/22	0.22	2.91	0.98
2022/23	0.12	2.46	0.84

4. Liquidity Risk

Year	SKBBL	CBBL	NUBL
2013/14	73.22	77.60	77.91
2014/15	76.57	74.70	74.90
2015/16	78.01	71.97	74.55
2016/17	66.63	72.93	64.43
2017/18	73.52	75.12	70.49
2018/19	84.05	75.30	65.38
2019/20	81.86	76.40	82.66
2020/21	87.01	72.40	81.96
2021/22	83.52	74.70	79.72
2022/23	85.30	80.10	89.84

5. Operating Cost

Year	SKBBL	CBBL	NUBL
2013/14	6.62	1.23	6.73
2014/15	4.79	1.22	4.84
2015/16	4.71	1.13	3.56
2016/17	3.39	1.01	3.53
2017/18	2.75	0.95	2.64
2018/19	4.15	0.90	3.40
2019/20	5.16	1.30	4.93
2020/21	5.86	1.40	5.49
2021/22	6.14	1.30	5.80
2022/23	4.85	1.20	5.22

6. Capital Adequacy Ratio

Year	SKBBL	CBBL	NUBL
2013/14	11.02	11.49	11.01
2014/15	11.59	11.27	11.59
2015/16	11.31	11.90	11.18
2016/17	13.33	14.92	11.57
2017/18	12.66	13.02	11.73
2018/19	14.54	13.02	12.90
2019/20	14.20	12.66	13.00
2020/21	13.74	13.26	12.50
2021/22	13.38	13.54	13.07
2022/23	12.47	14.71	12.77

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CHAPTER - I INTRODUCTION The introduction, literature review, research methods, analysis and discussion, and summary and conclusion are the five chapters that will make up this study. The introductory portion of the course will be covered in the first chapter. It will include the following: the study's history, problem statement, goals, theories, justification, and limitations. 1.1 Background of the Study The assessment and measurement of a person's or an organization's financial outcomes and achievements is known as financial performance. It is evaluating several financial measurements, ratios, and indicators to determine how profitable, successful, and efficient financial operations and management are. Financial performance analysis sheds light on how effectively resources are used, income is produced, expenses are controlled, and value is created for stakeholders. To evaluate an entity's financial health and performance, key metrics including revenue, profitability, return on investment, liquidity, solvency, efficiency, and cash flow are examined. To obtain a thorough grasp of a person's or an organization's financial operations and overall success, financial performance can be assessed, compared over time, or benchmarked against industry peers by analyzing these indicators and other pertinent financial data (Sangmi & Nazir, 2010). Both internal and external variables may have an impact on the effectiveness of microfinance organizations. These elements fall into two categories: microeconomic variables and internal, bank-specific characteristics. The performance of the bank is influenced by internal variables, which are specific features of the bank. Basically, the board and management's internal decisions have an impact on these elements. The external variables that impact the profitability of banks are those that are sector- or nation-wide, beyond the company's control (Ongore & Kusa, 2013). The majority of research on bank performance has concentrated on industry-specific elements that influence the overall performance of the banking industry. Nonetheless, the microeconomic factors must be taken into account. As a result, the analysis in this paper includes two important macroeconomic variables: GDP and inflation (Ongore & Kusa, 2013). This research also looked at the possibility that ownership identity has an impact on the correlation between bank performance and its factors. 1.2 Statement of the Problem Many difficulties in gathering disparate monies and allocating them to areas of productivity. Not every educated person can find job in the public or private sectors. The requirements of individuals are increasing as a result of liberalization and globalization. However,

Nepalese industries are not able **to provide Nepalese** goods. **Then, our** nation's **capital is**