

CHAPTER - I

INTRODUCTION

1.1 Background of the Study

It is obvious that economic development is impossible without the development of different sectors like Agriculture, Industry, and Trade etc. of the country. So, development of these sectors needs a regular supply of financial resources. In developing countries there is always shortage of the capital for the development activities. It is not possible to handle and develop all the sectors by the Government alone at a time. Private people also can not undertake large business because per capita income of the people is very low while their propensity to consume is very high. Due to low income their saving is very low and capital formation is very low. So their saving is not sufficient for carrying on development works.

It has been fully established that economic development if any country can be active only through a balanced growth in the fields of industry, trade, commerce and agriculture. It has equally self-evident that the development in these fields cannot be made possible without the existence of a sound banking system in the country. Many countries, aspiring for the rapid economic development, have developed several banking and non-banking specialized financial institutions with objectives of meeting the financial needs of their economy.

Banks are among the most important financial institution in the economy and essential business in the thousands of local town and cities. Certainly, banks must be identified by their functions, services and roles they perform in the economy. Now a day, the functions of banks are changing, but the functions of their principal competitors are also changing. The competitors like financial institution including security dealers, brokerage firms and insurance companies are trying to be similar as possible to bank in the services they offer.

There are various concepts among the economists about the origin of the word "Banking". The term bank derives from the Latin Bancus, which refers to the bench on which the banker would keep its money and his records. Some persons trace its

origin to the French word "Banque" and the Italian word "Banca" which means a bench for keeping; lending and exchanging go money in the market. The first bank called the "Bank of Venice" was established in Venice, Italy in year 1157. The bank of Barcelona and the bank of Genoa were established in 1401 and 1407 respectively. In England the banking began with English goldsmith only after 1640. The bank of Amsterdam was the great bank in seventeenth century.

"Economic development demands transformation of savings or investible resources into the actual investment. It is the financial institution that transfers funds from surplus spending units to deficit units," (Nepal Rastra Bank, 2005: 43).

Capital formation is one of the important factors in economic development. The capital formation leads to increase in the size of the national output, income, and employment, solving the problem of inflation and balance of payment and making the economy free from the burden of foreign debt. Domestic capital formation helps in making a country self-sustainable. Profit made by business community constituted the major part of the saving of the community and what was saved was assumed to be invested.

Banking sector plays an important role in the economic development of the country. Commercial Banks are one of the vital aspects of this sector, which deals in the process of channeling the available resources in the needed sector. It is the intermediary between the deficit and surplus of financial resources. Financial institutions like banks are a necessity to collect scattered saving and put them into productive channels. In the absence of such institutions it is possible that the saving will not be safely and profitably utilized within the economy. It will be diverted aboard or channeled into unproductive conspicuous consumption including real estate speculation.

"The business of banking is one of collecting funds from the community and extending credit (making loans) to people for useful purposes," (Edmister, 1990: 73). Loaning money has always been a basic function of commercial bank. After providing for its cash need a bank normally seeks to loan as large a portion of its deposit and excess capital as it prudentially can. The remaining portion of its

investible fund is placed in suitable securities (American Institute of Banking, 2006: 163).

Loans are an essential aspect of commercial bank. "First, income from loan contributes substantially to the revenues and profit of the bank. Second, lending money to people in the community strengthens the community- bank relationship. Third, lending money spurs business development and supports a growing economy" (Edmister, 1990: 82). Credit being the most important function of commercial banks, affects overall development of the country. So far as pace of economic development is considered, it is directly related to the quality and quantity of the credit, which is derived from various financial institutions, especially commercial banks in Nepal.

Investment operation of commercial banks is very risky one. For this, commercial banks have to pay due consideration while formulating Investment Policy. A healthy development of any commercial bank depends upon its investment policy. A good investment policy attracts both borrowers and lenders, which helps to increase the volume and quality of deposits, loans and investment.

1.2 Focus of the Study

A bank always puts in efforts to maximize its profitability. The profit is excess of income over expenses. To maximize profit, income should reasonably excess over expenses. The major source of income of a bank is interest income from loans and investments and fee based income. As loan and advances dominate the asset side of the balance sheet of any bank; similarly earnings from such loan and advances occupy a major space in income statement of the bank. However, it is very important to be reminded that most of the bank failures in the world are due to the shrinkage in the value of loans and advances. Hence loan is known as risky asset and investment operation of commercial banks is very risky one. Risk of non-repayment of loan is known as credit risk or default risk. Performing loans have multiple benefits to the society by helping for the growth of economy while non-performing loans erodes even existing capital. Considering the importance of lending to the individual banks

and also to the society it serves, it is imperative that the bank meticulously plans its credit operations. Sound credit policy has the following objectives:

-) To have performing assets.
-) To contribute to economic development.
-) To give guidance to lending officials.
-) To establish a standard for control, etc.

Considering these facts, this study mainly focuses on the investment policy of joint venture commercial banks in Nepal with special reference to the Nepal SBI Bank Limited.

1.3 Statement of the Problem

"The major problem in almost all underdeveloped countries and Nepal is no exception, is that of capital formation and proper utilization. In such countries, the commercial banks have to shoulder more responsibilities and act as development banks, due to the lack of other specialized institutions" (Dali, 1974: 52).

Credit extended by commercial banks is directly related to the National Interest of the country. So the investment policy of the commercial banks should be very sound and farsighted. "A policy is a statement or general understanding which provides guidance in decision making to members of an organization in respect to any course of action" (Gautam, 2002:33). Defining the commercial banks investment policy, Naughton (1994) says that investment policy should incorporate several elements such as regulatory environment, the availability of the funds, the selection of the risk, loan portfolio balance and term structure of the liabilities.

Project appraisal method followed by commercial banks is also not scientific one. So a large volume of credit extended by commercial banks is drifting from basic credit principle and found to have lower productivity. Loan supervision and follow up regarding whether clients are properly utilizing the bank investment is found to be poor in many of the commercial banks. Due to all these reasons, the proportion of non-performing asset on total loan and advances has been increasing significantly. It

has become a major problem of two large commercial banks, Nepal Bank Ltd and Rastriya Baniya Bank, and now private sector joint venture banks are also suffering from the NPA problem within the short time span of their operation.

Credit extended by commercial banks to agricultural and industrial sector is not satisfactory. Even if NRB has regulated to invest in priority sector like agriculture, small-scale industries and service, all the commercial banks have not yet financed full 12% of their loans to this sector. Commercial banks, including NSBL, are following conservative loan policy that is based on string security. They do not consider the profit potential of the project. There is not good trade-off between liquidity and profitability of banks.

Similarly, the investment portfolio position of the banks is not satisfactory. They are not following a sound diversification principle. Portfolio theory gives the concept of investment in very good ways that "do not put all eggs in a single basket". Diversity of funds reduces the risk. One-time commercial banks had invested a large proportion of their loan to Garment, Hotel and Carpet industries. But now these sectors became sick and banks are in trouble of their loan repayment.

The directions and guidance provided by Nepal Rastra Bank are the major policy statements for Nepalese commercial banks. A long term and published policy about their operation is not found even in the joint venture banks. Even if some how they have formulated some procedural guidelines they are failing in proper implementation due to poor supervision.

Thus, in this scenario of Nepalese commercial banking sector, this study mainly seeks the answers of the following specific problems related to investment policy of Nepal SBI Bank Ltd.:

- Has the bank been able to collect and utilize the funds efficiently?
- What is the relationship between investment and loan & advances with total deposits?
- Does the investment decision affect the total earnings of the bank?

- What is the proportion of Non-Performing Asset on total loans and advances of the bank?
- What is the portfolio behavior of the bank?
- What is the proportion of bank's investment on priority sector?
- What is the relationship of total deposit on total investment and total investment on total net profit of the bank?

1.4 Objective of the Study

Investment decision is one of the major decision functions of financial management. The objective of the study is mainly focused to assess and evaluate the investment policy and strategies followed by the NSBL.

The main objective of the study is to evaluate the investment policy of Nepal SBI Bank Ltd. However, the specific objectives of the study are:

- To find out the Non Performing Assets position of the bank in relation to loans and advances
- To analyze the portfolio management of the bank,
- To identify the bank's investment on priority sector,
- To analyze deposit utilization and it's relationship with total investment and net profit of the bank, and
- To suggest measures to improve the investment policy of the bank.

1.5 Significance of the Study

This study mainly fills a research gap on the study of investment policy of NSBL. Definitely, the study will provide a useful feedback to the policy makers of the bank and also becomes a useful reference for other commercial banks of Nepal and central bank (NRB) for the formulation of appropriate strategies. This study evaluates the investment policy of NSBL and finds its loopholes and significantly contributes to make the policy sound.

1.6 Limitations of the Study

This study has the following limitations:

- a) This is a case study of NSBL and findings of the study can not be generalized.
- b) The study is limited to five years period from 2007/08 to 2011/12 A.D.
- c) The study is based on secondary data collected from the bank, which may not be far from limitation due to inherent characters.
- d) Among many factors affecting investment decision, only certain factors i.e. liquidity, profitability, diversification, growth etc. have been considered.
- e) The study has been carried out based on the published financial documents such as balance sheets, profit and loss accounts, related journals, magazines and brochures. These published documents have their own limitations.

1.7 Organization of the Study

Since the study carried out to different stages and procedures, as it needed as well the study organized in the following chapters in order to make the study easy to understand:

Chapter 1. Introduction: This chapter includes background of study, focus of study, statement of problem, objectives, significance, limitations and organization of study

Chapter 2. Review of Literature: This chapter includes conceptual framework, review of related studies and research gap

Chapter 3. Research Methodology: This includes research design, population and sample, sources of data, data collection techniques and data analysis tools

Chapter 4. Presentation and Analysis of Data: This chapter includes measuring of liquidity position, assets management ratios, activity ratios, loans & advances portfolio, profitability ratios, growth ratios, correlation between variables, trend analysis, findings of study

Chapter 5. Summary, Conclusions and Recommendations

Bibliography

Appendix

CHAPTER – II

REVIEW OF LITERATURE

In this chapter, focus has been made on the review of literature that is relevant to the investment policy of commercial banks. Review of literature is basically a stock taking of available literature in the field of research. Every possible effort has been made to grasp knowledge and information that is available from libraries, document collection centers, other information managing bureaus and concerned commercial bank. This chapter helps to take adequate feed back to broaden the information base and inputs to the study. Conceptual framework given by different authors, research scholars, practitioners etc. are reviewed from books, research papers, annual reports, articles etc., which are arranged into the following order:

- (a) Conceptual framework
- (b) Review of related studies
 - Review of research papers
 - Review of articles
 - Review of Ph. D. Thesis
 - Review of Master's Degree Thesis
- (c) Research Gap

2.1 Conceptual Framework

Commercial bank is a corporation, which accepts demand deposits subject to check and makes short-term loans to business enterprises, regardless of the scope of its other services (American Institute of Banking, 1972: 345).

Commercial Bank Act of Nepal (1974) has defined that "A commercial bank is one which exchanges money, deposits money, accepts deposits, grant loans and performs commercial banking functions and which is not a bank meant for co-operative, agriculture, industries or for such specific purpose."

A Commercial Bank is business organization that receives and holds deposits of fund from others, makes loans or extends credits and transfers funds by written order of deposits (Grolier Incorporated, 1984).

This Act has laid emphasis on the functions of commercial bank while defining it. Commercial banks provide short-term debts necessary for trade and commerce. They take deposits from the public and grant loans in different forms. They purchase and discount bills for exchange, promissory notes and exchange foreign currency. They discharge various functions on the behalf of their customers provided that they are paid for their services.

Optimal investment decision plays a vital role in each and every organization. But especially for the commercial banks and other financial institutions the sound knowledge of investment is the most because this subject is relevant for all surrounding that mobilize funds in different sectors in view of return.

As it is concerned to the commercial banks and other financial institutions, they must mobilize (i.e., investment on different sectors) their collections (deposits) and other funds towards the profitable, secured and marketable sectors so that they will be in profit. For this purpose these banks and financial institutions should gather the sufficient information about the firm (client) to which supposed to be invested. These information include as financial background, nature of business as well as its ability to repay the loan back. These all information should be gathered from the viewpoint of security.

The income and profit of the bank depend upon the lending procedure applied by the bank. As well as lending policy and investment in different securities also affect the income and profit. In the investment procedures and policies it is always taken in mind that "the greater the credit created by the bank, higher will be the profitability." A sound lending and investment policy is not only pre-requisite for bank's profitability but also crucially significant for the promotion of commercial savings of a developing country like Nepal.

The sound policies help commercial banks maximize quality and quantity of investment and thereby, achieve the own objective of profit maximization and social welfare. Formulation of sound investment policies and coordinated and planned efforts pushes forward the forces of economic growth.

Commercial banks, as financial institutions, perform a number of internal functions. Among them, providing credit is considered as most important one. In the words of H. D. Crosse (1963), "Commercial banks bring into being the most important ingredient of the money supply, demand deposit through the creation of credit in the form of loan and investments."

Investment operation of commercial banks is very risky one. For this, commercial banks have to pay due consideration while formulating investment policy regarding loan investment. Investment policy is one facet of the overall spectrum of policies that guide banks investment operations. A healthy development of any bank depends heavily upon its investment policy. A sound and viable investment policy can attract both borrowers and lenders, which helps to increase the volume and quality of deposits, loan and investment. The loan provided by commercial bank is guided by several principles such as length of time, their purpose, profitability, safety, etc. These fundamental principles of commercial bank's investment are fully considered while making investment policy. Emphasizing upon this H.D. Crosse stated, "The investment policy should be carefully analyzed". Commercial bank should be careful while performing the credit creation function. Investment policy should ensure minimum risk and maximum profit from lending.

According to J.H. Clemens (1963), "Commercial bank should consider the national interest followed by borrower's interest and the interest of the bank itself before investing to the borrowers". To further pursue his view, bank lending must be for such purposes of the borrowers that are in keeping with the national policy and bank's overall investment policy. A bank's overall investment: -

- a) Should be basically of short term characters,
- b) Should be well spread,
- c) Should be repayable on demand,
- d) Must be profitable
- e) Must be well in adequate security.

Diana Mc Naughton (1994) in her research paper 'Banking institution in developing markets' stated that, "Investment policy should incorporate several elements such as

regulatory environment, the availability of funds, the selection of risk, loan portfolio balance and term structure of the liabilities".

Thus, commercial banks have to consider government and Nepal Rastra Bank's instructions and national and their own interest as well. Good investment policy ensures maximum amount of investment to all sectors with proper utilization.

2.1.1 Evolution of Financial System in Nepal (Early Era)

In almost all countries the logical historical order of the development of financial structure has gone through different stages. In Nepal, the first stage starts from rudimentary economy in which the commodity money such as gold and silver coins generally accepted as a means of payment. At 12th century silver coinage came into existence in Nepal. But no financial intermediation was possible in this stage.

The second major stage is the development of interest bearing debt such as bonds, mortgages and loans. In the year 79/80 A.D., we came across the term 'Debt' in Nepal. At the end of the 14th century we further came across the term 'Tanka Dhari', meaning money dealer, which is one of the sixty-four casts classified on the basis of occupation. In historical order of development an organized market was missed out in Nepal. The development of the market is seen only in the last stage. Treasury bills were only issued for the first time in 1962. Government bonds were introduced in February 1964 (Nepal Rastra Bank, 1996:27-40).

2.1.2 Evolution of Banking System

In Nepal financial system is still in evolutionary phase. The existence of unorganized money market consisting of Land-lords, Shahukars (Rich Merchants), Shopkeepers and other indigenous individual money lenders has acted as barriers to institutionalized credit.

During the Prime Ministership of Ranoddip Singh around 1877 A.D., a number of economic and financial reforms were introduced. The establishment of the "Tejarath Adda" fully subscribed by the government in the Kathmandu valley was one of them. The "Tejarath Adda" disbursed credit to the people especially on the collateral of gold

and silver. Thus the establishment of the "Tejarath Adda" could be regarded as the premier foundation of modern banking in Nepal (Nepal Rastra Bank, 1996:27-40).

Beginning of modern banking was the establishment of Nepal Bank Limited on November 1937. It laid the foundation of modern financial system in Nepal. It was a joint venture between government and the private sector. After then, the Nepal Rastra Bank came into existence as the central bank on April 26, 1956. It had authorized capital of Rs. 10 million fully subscribed by the government. It was empowered by act to have direct control over financial institutions within the country. It started issuing currency in 1959 A.D. The second commercial bank Rastriya Banijya Bank was established in 1966 A.D.

Besides Nepal Bank Limited and Rastriya Banijya Bank, other commercial banks didn't come into existence until 1984 A.D (Nepal Rastra Bank, 1996:27-40). The commercial banking act 1974 was amended in 1984 A.D. to increase the competition between commercial banks. As per the provision made in this act, private sector (including foreign investment) was given freedom in opening commercial bank. Consequently, Nepal Arab Bank Limited was established in 1984 A.D. as a joint venture bank (Joshi, 2000: 217-218). Likewise Nepal Indo-suez Bank Ltd. and Nepal Grindlays Bank Ltd. were established under joint venture in 1986 and 1987 A.D. respectively.

After the initiation of democracy in 1990 A.D., NRB adopted a more liberal policy in establishing the commercial banks. Now the number reached 31 more than three folds.

Following are the lists of commercial Banks operating in the Nepalese financial market:

1. Nepal Bank Limited
2. Rastriya Banijya Bank Limited
3. Agriculture Developmetn Bank
4. Nabil Bank Ltd.
5. Nepal Investment bank Ltd.
6. Standard chartard Bank Ltd.
7. Himalayan Bank Ltd.

8. Nepal SBI Bank Ltd.
9. Nepal Bangladesh Bank Ltd.
10. Everest Bank Ltd.
11. Bank of Kathmandu Ltd
12. Nepal Credit and Commerce Bank Ltd.
13. Lumbini Bank Ltd.
14. Macchapuchhre Bank Ltd.
15. Kumari Bank Ltd.
16. Laxmi Bank Ltd.
17. Siddhartha Bank Ltd.
18. Global Bank Ltd.
19. Citizens Bank Ltd.
20. Prime Commercial Bank Ltd.
21. Sunrise Bank Ltd.
22. DCBL Bank Ltd.
23. NMB Bank Ltd.
24. Kist Bank Ltd.
25. Janata Bank Ltd.
26. Mega Bank Ltd.
27. Commerz and Trust Bank Nepal Ltd.
28. Civil Bank Ltd.
29. Century Commercial Bank Ltd.
30. Sanima Bank Ltd.
31. NIC Asia Bank Ltd.

The banks are such types of institutions, which deal in money and substitute for money. They deal with cash, credit and credit instruments. Good circulation of credit is very much important for the bank. Unsteady and unevenly flow of credit with ad-hoc decisions harms the economy and the bank as well. Thus, to collect fund and utilize it in a good investment, is a very difficult and important task for such organization. An investment of fund may be the question of life and death for the bank.

Emphasizing the importance of investment policy, H. D. Crosse (1963) puts his view in this way, "Lending is the essence of commercial banking, and consequently the formulation and implementation of sound policies are among the most important responsibilities of bank directors and management. Well conceived lending policies and careful lending practices are essential if a bank is to perform its credit creating function effectively and minimize the risk inherent in any extension of credit".

He further adds, the formulation of sound lending policies for all banks should have adequate and careful consideration over community needs, size of loan portfolio, character of loan, credit worthiness of borrower and asset pledged to security borrowing , interest rate policy, etc.

According to Chandler L. V. (1973), "A banker seeks optimum combination of earning, liquidity and safety while formulating investment policy".

"Investing involves making a current commitment of funds in order to obtain an uncertain future return. It is a risky business that demands information. To process information effectively and select the best investments require goals that are clear cut and realistic" (Clark, 1981: 53).

According to V. K. Valla (1983: 2), there are basically three concepts of investment:

- a) Economic investment – that is an economist's definition of investment.
- b) Investment in a more general or extended sense which is used by 'the man of the street', and
- c) The sense in which we are going to be very much interested, namely financial investment.

According to S. P. Singh and S. Singh (1983), "The investment (credit) policies of banks are conditional, to great extent, by the national policy framework; every banker has to apply his own judgment for arriving at a credit decision, keeping, of course, his bank's credit policy also in mind".

They further stated, "The field of investment is more challenging as it offers relatively greater scope to bankers for judgment and discretion in selecting their loan portfolio. But this higher degree of freedom in the field of credit management is also

accompanied by greater risk, particularly during recent years, the credit function has become greater complex."

Singh (1985) has defined investment as "Investment is the employment of funds with the aim of achieving additional income or growth in value. The essential quality of an investment is that it involves 'waiting' for a reward."

Bexley, (1987) express his views as, "Investment policy fixes responsibilities for the investment disposition of the banks assets in terms of allocating funds for investment and loan, and establishing responsibility for day to day management of those assets."

In the words of Gitman and Jochnk (1990), "Investment is any vehicle into which funds can be placed with the expectation that will preserve or increase in value and generate positive returns."

Reilly (1991) defines investment as, "An investment may be defined as the current commitment of funds for a period of time to derive a future flow of funds that will compensate the investing unit for the time the funds are committed, for the expected rate of inflation and also for the uncertainty involved in the future flow of the funds".

Sharpe and. Gorden (1998) define investment as, "Investment, in its broadest sense, means the sacrifice of certain present value for (possible uncertain) future value"

According to Sharpe (1999), "Investment can be categorized as Real investments and financial investments. Real investments generally involve some kinds of tangible asset, such as land, machineries or factories. Financial investments involve contracts written on pieces of paper, such as common stocks and bonds."

Thus investment is the most important function of commercial banks. It is the long-term commitment of bank in the uncertain and risky environment. It is a very challenging task for commercial banks. So a bank has to be very cautious while investing their funds in various sectors. The success of a bank heavily depends upon the proper management of its investible funds.

Investment management of a bank is guided by the investment policy adopted by the bank. The investment policy of the bank helps the investment operation of the bank to be efficient and profitable by minimizing the inherent risk.

Various authors have expressed their views regarding investment policies of commercial banks, their formulation and implementation differently.

"A sound investment policy of a bank is such that its funds are distributed on different type of assets with good profitability on the one hand and provides maximum safety and security to the depositors and banks on the other hand. Moreover, risk in banking sectors tends to be concentrated in the loan portfolio. Therefore the banks investment policy must ensure that it is sound and prudent in order to protect public funds. Bank makes a variety of loans to a wide variety of customers for different purposes. Therefore no uniform rules can be laid down to determine a portfolio of a bank. The environment in which it operates influences the investment policy of the bank. The nature and availability of funds also differ widely from one region to another within the country. For example scope of a bank operating in Jumla will be different from the scope of bank operating in Kathmandu. Therefore the investment policy to be applied in Kathmandu may not be applicable to the bank operating in Jumla" (Baidhya, 1999: 46-47).

Investment policy provides the bank several inputs through which they can handle their investment operation efficiently ensuring the maximum return with minimum exposure to risk, which ultimately leads the bank to the path of success.

According to Edward W. Reed, Richard V. Cotter, Edward K. Gill and Richard K. Smith (1980: 1-5), "Commercial banks still remain the heart of our financial system holding the deposits of millions of persons, governments and business units. They make funds available through their lending and investing activities to borrowers, individuals, business firms and governments. Commercial banks are the most important type of financial institutions in the nation in terms of aggregate assets." The primary function of commercial banks is the extension of credit to worthy borrowers. In making credit available, commercial banks are rendering a great social service. Through their actions, production is increased, capital investments are expanded, and a higher standard of living is realized. Although the investment activities of

commercial banks are usually considered separately from lending, the economic effects and social results are the same.

Reed et al. (1980: 195) added that "The rate of return on assets is a valuable measure when comparing the profitability of one bank with another or with the commercial banking system. A low rate might be the result of conservative lending and investment policies or excessive operating expenses. Banks could, of course, attempt to offset this by adopting more aggressive lending and investment policies to generate more income"

Investment policies include credit analysis and its principal purpose is to determine the ability and willingness of a borrower to repay a requested loan in accordance with the terms of the loan contract. Factors considered in credit analysis are capacity to borrow, characters (honesty, integrity, industry, morality, ability to create income, ownership of assets, economic conditions, etc. Loans are the most important assets held by banks and bank lending provides the bulk of bank income (Reed et al, 1980: 203, 235).

In broad sense the investment operation of bank includes lending and investing in different types of securities. We can say lending is the primary investment activity and investment in different types of securities is the secondary investment activity of the commercial banks.

Reed et al. (1980: 242) further stressed that "More and more banks have developed formal, written lending policies in recent years. They provide guidance for lending officers and there by establish a greater degree of uniformity in lending practices. Since lending is important both to the bank and to the community it serves, loan policies must be worked out carefully after considering many factors like:

- Capital position.
- Risk and profitability of various types of loans.
- Stability of deposits.
- Economic conditions.
- Influence of monetary and fiscal policy.
- Ability and experience of bank personnel.

- Credit needs of the area served”

Investment is concerned with the management of an investors wealth which are the sum of current income and the present value of all future income funds to be invested come from assets already owned, borrowed money and saving or forgone consumption by forgoing today and investing the saving, investors expects to enhance their future consumption possibilities i.e., they are invested to increase wealth. In pure financial sense the subsequent use of the term investment will be in the prevalent financial sense of the placing of money in the hands of others for their use, in return for a proper instrument entitling the holders to fixed income payments or the participation in expected profit. Whereas an economist view, investment as a productive process by means of which additions are made to capital equipment. For our purpose in the study of the financial institutions the investment and investment problem will revolve around the concept of managing the surplus financial assets in such a way which will lead to the wealth maximization & providing a significant further source of income, (*Limbu Ram, 2008*).

2.1.3 Features of a Sound Lending and Investment Policy

The income and profit of the bank depends upon its lending procedures, lending policy and investment of its funds in different securities. The greater the credit created by the bank, the higher will be the profitability. A sound lending and investment policy is not only prerequisite for banks profitability, but also crucially significant for the promotion of commercial savings of a backward country like Nepal.

Many authors have given some necessities or some of the main characteristics for sound lending and investment policies, which must be considered by the commercial banks:

(I) Safety and Security

The bank should never invest its funds in those securities, which are too volatile i.e., which are subject to too much depreciation and fluctuations because a little difference may cause a great loss. It must not invest its funds into speculative businessman who may be bankrupt at once and who may earn millions in a minute also. Security means adequate collateral having good value, which can be easily sold off if required at any

point of time. The bank should accept that type of securities, which are commercial, durable and marketable having fair market value. For this purpose 'MAST' should be applied while reaching an investment decision. (*Unpublished Masters Degree Thesis, Kathmandu*). Where MAST stands for,

M = Marketability,

A = Ascertainability,

S = Stability,

T = Transferability.

() Profitability

A commercial bank can maximize its volume of wealth through maximization of return on their investments and lending. So, they must invest their funds where they can gain maximum profit. The profit of commercial banks depends on the interest rate, volume of loan, its time period and nature of investment in different securities.

(III) Liquidity

Liquidity is the ability of a firm to satisfy its short-term obligations when they become due for payment. People deposit money at the bank in different account with confidence that the bank will repay their money when they need. To maintain such confidence of the depositors, the bank must keep this point in mind while investing its excess funds in different securities, so that it can meet current or short-term obligations when they become due for payment.

(V) Purpose of loan

From the viewpoint of security, a banker should always be known that why a customer is in need of loan. If a borrower misuses the loan granted by the bank, it can never repay and bank will possess heavy bad debts. Therefore in order to avoid this situation each and every bank should demand and examine all the essential detailed information about the scheme of the project or activities, before lending.

(V) Diversification

"A bank should not lay all its eggs on the same basket". This saying is very important to the bank and it should always be careful not to grant loan in only one sector. To

minimize risk, a bank must diversify its investment on different sectors. Diversification of loan helps to sustain loss according to the law of average because if securities of a company deprived, there may be appreciation in the securities of other companies. In this way the loss can be minimized or recovered. (*Wolf Howard K., 2002*)

(VII) Tangibility

Though it may be considered that tangible property does not yield an income apart from direct satisfaction of possession of property, many times, intangible securities have lost their value due to price level inflation. A commercial bank should prefer tangible security to intangible one.

(VI) Legality

Illegal securities will bring out many problems for the investor. A commercial bank must follow the rules and regulations as well as different directives issued by the central bank (Nepal Rastra Bank), Ministry of finance, Ministry of law and other relevant authorities, while mobilizing its funds.

(IX) National Interest

In addition to its own profitability the Bank should also consider the national interest. Even though the Bank cannot get maximum return from such investment, it should carry out its obligation towards the society and the country. The Bank is required to invest on such sectors as per the Government and Nepal Rastra Bank's instruction. Investment on government bonds, priority and deprived sector lending are the examples of such investments.

2.2 Review of Related Studies

2.2.1 Review of Research Papers

There are not much articles published related to investment management in Nepal. Shrestha (1993) in her research, "Investment planning of commercial banks in Nepal", has made remarkable efforts to examine the investment planning of commercial banks in Nepal. On the basis of the study she concludes that bank portfolio (loans and investment) of commercial banks has been influenced by the variable securities rates.

Investment planning of commercial banks in Nepal is directly traced to fiscal policy of government and heavy regulatory procedure of the central bank (Nepal Rastra Bank). So the investments are not made in professional manner. Investment planning and operation of commercial banks in Nepal has not been found satisfactory in terms of profitability, liquidity, safety, productivity and social responsibility. To overcome this problem, she has suggested, "commercial banks should take their investment function with proper business attitude and should perform lending and investment operation efficiently with proper analysis of the projects".

Thapa (1994: 29-37) has expressed his view that the commercial banks including foreign joint venture banks seem to be doing pretty well in mobilizing deposits. Likewise, loans and advances of these banks are also increasing. But compared to the high credit needs particularly by the newly emerging industries, the banks still seem to lack adequate funds. The banks are increasing their lending to non-traditional sectors along with the traditional sectors.

Out of the different commercial banks, Nepal Bank Ltd. and Rastriya Banijya Bank are operating with a nominal profit and also turning towards negative from time to time. Because of non-recovery of accrued interest, the margin between interest income and interest expenses is declining. These banks have not been able to increase their income from commission and discount, through traditional off-balance sheet operations. On the contrary, they have got heavy burden of personnel and administrative overheads. Similarly, due to accumulated overdue and defaulting loans, profit position of these banks has been seriously affected. On the other hand, the foreign venture banks have been functioning in an extremely efficient way. They are making huge profit year after year and have been distributing large amount of loans and dividends to its employees and shareholders.

Shrestha (1998) has given a short glimpse on the "Portfolio management in commercial banks; theory and practice". Mr. Shrestha has highlighted following issues in the article. The portfolio management becomes very important both for individuals as well as institutional investors. Investors would like to select a best mix of investment assets subject to the higher return; Good liquidity; Maximum tax concession; Economic, efficient and effective investment mix; Flexible investment and certain capital gains.

In view of above aspect, following strategies can be adopted:

-) Do not hold any single security i.e.; try to have a portfolio of different securities.
-) Do not put all the eggs in one basket i.e.; to have a diversified investment.
-) Choose such a portfolio of securities, which ensures maximum return with minimum risk or lower return but with added objective of wealth maximization.

However, Mr. Shrestha has also presented approaches to be adopted for designing a good portfolio and its management. Such as ; To find out the investible assets (generally securities) having scope for better returns depending upon individual characteristics like age, health, need, disposition, liquidity, tax liability, etc as well the risk of the securities depending upon the attitude of investor toward it; To develop alternative investment strategies for selecting a better portfolio that will ensure a trade-off between risk and return and also To identify securities for investment to refuse volatility of return and risk.

Mr. Shrestha has presented two types of investment analysis techniques ie; *fundamental analysis* and *technical analysis* to consider any securities such as equity, debentures or bonds and other money and capital market instruments. He has suggested that the banks having international network can also offer access to global financial markets. He has pointed out the requirements of skilled manpower, research and analysis team and proper management information system (MIS) in any commercial bank to get success in portfolio management and customer's confidence. According to him, the portfolio management activities of Nepalese commercial banks at present are in nascent stage. However, on the other hand, most of the banks are not doing such activities so far because of Unawareness of the clients about the service available and Hesitation of taking risk by the clients to use such facility as well due to Lack of proper techniques to run such activities in the best and successful manner.

2.2.2 Review of Articles

In this section, effort has been made to examine and review of some related articles in different economic journals, World Bank discussion papers, magazines, newspapers and other related books and publications.

F. Morris (1990) in his discussion paper, "Latin America's Banking System in the 1980^s" has concluded that most of the banks concentrated on compliance with central bank rules on reserve requirements, credit allocation and interest rates. While analyzing loan portfolio, operating efficiency and soundness of bank investment management has largely been overlooked. The huge losses now found in the bank's portfolio in many developing countries are testimony to the poor quality of this oversight investment function. He further adds that mismanagement in financial institutions has involved inadequate and overoptimistic loan appraisal, lower loan recovery, high risk diversification of lending and investments, high risk concentration, connected and insider lending, loan mismatching, etc. This has led many banks of developing countries to the failure in 1980^s.

Bajracharya (1990: 93-97) in his article "Monetary policy and deposit mobilization in Nepal", has concluded that mobilization of domestic savings is one of the prime objectives of the monetary policy in Nepal and commercial banks and the more active financial intermediary for generating resources in the form of deposit of private sector and providing credit to the investor in different sectors of the economy.

Pradhan (1996: 9) has presented a short glimpse on investment in different sectors, its problem and prospects, through his article "Deposit mobilization, its problem and prospects". On his article he has expressed that, "Deposit is the life blood of any financial institution, and be it commercial bank, finance company, co-operative or non-government organization". He also added, in consideration of 10 commercial banks and nearly three dozens of finance companies, the latest figure does produce a strong feeling that a serious review must be made of problems and prospects of deposit sector. Except few joint venture banks, other organizations rely heavily on the business deposit receiving and credit disbursement. Due to the lesser office hours of banking system people prefers for holding the cash in the personal possession. He mentioned that deposit mobilization carried out effectively is in the interest of depositors, society, financial sector and the nation. Lower level of deposit raising

allows squeezed level of loan delivery leaving more room to informal sector. That is why higher priority to deposit mobilization has all the relevance.

Kishi (2002: 27-32) in his article, "The changing face of the banking sector and the HMG/N recent budgetary policy", concluded that following an introduction of the reform in the banking sectors as an integrate part of the liberal economic policy, more banks and finance companies have come up as a welcome measure of competition. Slowly and steadily, the two government controlled banks, Nepal Bank Limited and Rastriya Banijya Bank have also shown an improvement of non-performing loans and are taking steps to adopt improved technology. However, higher economic growth with social justice bringing an significant benefit to the poor are yet to be achieved as envisaged by the HMG/N.

Prof. Shrestha (1997) in his article "Nepalma Banijya Bank Haruko Bhumika" has pointed out some important activities and its present scenario. In his words these activities are to be studied and revised as soon as possible, otherwise these may be disaster for the sound and effective banking system. The article is written in Nepali language. Some of the main points of his article are given as:

-) Possibility of capital flight: - which indicates the flow of capital outside the country due to the unstable political situation. In this controversial situation joint venture banks become the main source or medium of capital flight.
-) Minimum Deposit amount: - Many commercial banks have increased the minimum deposit amount (threshold). This policy may harass the lower level depositors. It also affects the banking habits of lower level depositors negatively.
-) Debt recovery and its effectiveness: - In these years, it can also be seen that effective debt recovery is also a great problem of banks due to the misinterpretation of use of loan more than this, a gap between banks and debtors (i.e.; effective supervision).

Dr. Shrestha (1998: 23-27) in her article, "Lending operation of commercial banks of Nepal and its impact on GDP", has presented with the objectives to make an analysis of contribution of commercial bank's lending to the gross domestic product (GDP) of Nepal. She has set hypothesis that there has been positive impact of lending of

commercial banks to the GDP. In research methodology she has considered GDP as the dependent variable and various sectors of lending viz. agriculture, industrial, commercial, service and general and social sectors as the independent variables. A multiple regression technique has been applied to analyze the contribution. The multiple regression analysis has shown that all the variables except service sector lending have positive impact on GDP. Thus, in conclusion she has accepted the hypothesis i.e.; there has been positive impact on GDP. She has accepted that there has been positive impact by the lending of commercial banks in various sectors of economy, except service sector investment.

Ghimire (2008) has published an article in which he has mentioned that most of the commercial banks of Nepal are ready to pay the penalty in spite of investing on rural, priority sector, poverty stricken and deprived areas. In the directives of Nepal Rastra Bank it is clearly mentioned and directed that all the commercial banks (under NRB) should invest 12 % of its total investments to the priority sectors. However these commercial banks are unable to meet the requirements of NRB.

Bhattarai (2009) has presented an article about the "Non Performing Assets (NPA) Management". According to him, a loan is very easy term for a borrower when he has already taken and for a lender not availed. It is equally difficult for a borrower to avail and for lender to recover. From a banker's view, it is just like a stone to roll down from the top of the hill while sanctioning, but too difficult to roll back the same stone to the top of the hill while recovering. A loan not recovered within the given time frame either in the form of interest servicing or principal repayment is called non-performing loan (NPL). There are other parameters as well to quantify an NPL. Security not to the extent of loan amount with specified safety margin, value of security not realizable, possession not as per the requirement of bank, conflict of charges are the other reason which causes difficulties while recovering the loan. According the loan for a bank is most important to generate revenue for operational expenses as well as to provide return to the shareholder.

A general survey reveals two major reasons why a good loan turns into bad. Firstly, *Situational Problem* which indicates poor analysis of project and its capital requirement; Faulty evaluation of loan and security; Problem in managing the unit;

Sudden change in internal and external environment and project not being run according to its plan; Mismatch in demand and supply; Delay in collection of receivables and secondly, *Intentional Problems*, which indicates intention to cheat the bank; Malicious act of both the bank-staff and borrower; Intention to auction the property, which is in least requirement, borrower and to waive interest/ penal interest or avail discount on loan if paid in latter stage when bank offer such facilities.

He added that a formula Know Your Customer (KYC) is to be always taken into consideration. A bank must be clever and must collect information greater than a borrower require for commencement of business and to be more rigid to give the loan than to give his own money without any security. Therefore every possible measure is to be implemented to keep a loan portfolio intact.

2.2.3 Review of Ph. D. Thesis

Shrestha (1993) has conducted a study on "Investment planning of commercial banks in Nepal" with the objectives of:

- To evaluate the financial performance of commercial banks in Nepal.
- To examine the investment of commercial banks of Nepal with reference to securities, loans & advances.
- To establish the relationship of bank portfolio variables with the national income and interest rates.

The research was conducted on the basis of primary and secondary data of commercial banks. As per her research findings, the general trend of commercial banks asset holding is growing. Deposits have been a major source of funds. Debt equity ratio is very high, greater than 100%. The return ratios are on the average higher for foreign joint venture banks than for the Nepalese bank but return of asset found to be statistically same. The investment of commercial banks in shares and securities is normal and not found to have strategic decision towards investment in shares and securities. Investment in various economic sectors shows industrial and commercial sector taking higher share of loan till 1990. Investment in various sectors has a positive impact on the national income from their respective sectors. Lending in priority sector showed cottage and small industry sector sharing higher loans which showed positive impact on the national income.

The secured loan analysis showed commercial loan as being very important followed by social and industrial loans. The loan loss ratio has been found to be increased with low recovery of loan. Demand of bank credit has been found to be affected by the national income and lending and treasury bill rate. The investment of commercial banks on government securities has been observed to be affected by total deposit, cash reserve requirements and treasury bill and lending rates. Interest rates, lending rate, deposit rate were found to constitute a set of significant variables affecting the bank portfolio composition.

2.2.4 Review of Master's Degree Thesis

Before this, several thesis works have been conducted by various students regarding the various aspects of commercial banks such as financial performance, lending policy, investment policy, interest rate structure, resources mobilization, capital structure, etc. Some of them, as supposed to be relevant for the study are presented below.

Bajracharya (2000) conducted a study on "Investment of commercial Banks in priority sector" with the objective of:

-) To analyse the trend of investments in Private sectors and the trend of repayment in private sectors for 10 years from 2047 B.S. to 2056 B.S.
-) To measure the effectiveness of the program in terms of the investment and repayment in rural and urban sector.
-) To evaluate the banking procedures and services in disbursing loan in this sector and provide package of suggestion based on this study.

The research was conducted through primary and secondary data. For the primary data, pre-structured questionnaire was distributed to entrepreneur. Secondary data from different sources like reports, books, bulletins, journals, magazine and other publications of Rastriya Banijya Bank, Nepal Rastra Bank, etc. are also collected.

The research findings of the study are as follows:

- The target of 12% investment of total outstanding liabilities in priority sector and 3% out of which has been invested in deprived sector has been met by RBB. The trend analysis shows that the commercial banks are giving due consideration to increase investment in priority sector.
- Interest charged on the loan disbursed in this sector is fairly less than that of loans for other purposes. The Chi square test of effectiveness of program shows that the program is more effective in rural and semi rural areas as compared to the urban areas. Investment on agriculture is higher than investment on industry and service sector.
- The study revealed that the procedure of loan disbursing itself is complicated for the borrowers to understand it.

Upendra Tuladhar (2000) conducted a study on "A study on investment policy of Nepal Grindlays Bank Limited in comparison to other Joint venture Banks of Nepal" with the objective :

- To study the fund mobilization and investment policy with respect to fee-based off-balance sheet transaction and fund based on-balance sheet transactions.
- To study the liquidity, efficiency of assets management and profitability position and evaluate the growth ratios of loan and advances and total investment with respective growth rate of total deposit and net profit.
- To perform an empirical study of the customers' views and ideas regarding the existing services and adopted investment policy of the Joint venture banks.

The study is mainly based on secondary data and in some aspects of the study primary data are also collected through questionnaire survey of 100 respondents. The research findings of the study are summarized as follows:

From the analysis of primary data concerning in which sector should JVBs invest; 28.37 % respondents emphasized on educational sector to be invested by these JVBs as the potential investment sector. Consequently poverty stricken and deprived sector was given second priority (26.24 %), whereas industrial sector (18.44 %), tourism sector (16 %), agricultural sector (16 %), and construction sector (4.25 %) are given third, fourth, fifth and sixth priority respectively.

From the analysis of secondary data it was found that the Nepal Grindlays Bank Ltd. has maintained consistent and successful liquidity than NABIL Bank Ltd. and Himalayan Bank Ltd. Consequently the mean of total investment to total deposits ratio is higher than the other JVBs. The mean of the loan and advances to total deposits ratio is less and inconsistent than NABIL Bank Ltd. and Himalayan Bank Ltd. Loan and advances to working fund ratio of Nepal Grindlays Bank Ltd. was found less than the mean ratio of other banks. Investment on government securities to working fund ratio had the highest mean ratio than NABIL Bank Ltd. and Himalayan Bank Ltd. during the study period. It was found that total Off-balance sheet operation to loan and advances ratio of Nepal Grindlays Bank Ltd. is found to be of highest mean ratio than that of NABIL Bank Ltd. and Himalayan Bank Ltd. The mean of investment on shares and debentures to total working fund ratio of Nepal Grindlays Bank Ltd. was found less than NABIL Bank Ltd. but higher than Himalayan Bank Ltd. The volume of growth ratio of loan and advances of Nepal Grindlays Bank Ltd. is found higher than that of NABIL Bank Ltd. but lower than Himalayan Bank Ltd. From the analysis of growth ratio of total investment it is found that Nepal Grindlays Bank Ltd. and NABIL Bank Ltd. have negative growth ratio.

Thapa (2001) conducted a study on "Investment policy of Nepal Bangladesh Bank Ltd. and other Joint Venture Banks (NABIL and Nepal Gridlays Bank Ltd.)" with the objective of:

- To examine the liquidity, asset management efficiency, profitability and risk position of NB Bank in comparison to NABIL and NGBL and analyse the relationship between loan & advances and total investment with other financial variables of NB Bank and compare them with NABIL and NGBL.
- To examine the fund mobilization of investment policy of NB Bank through off-balance sheet activities in comparison to the other two banks.
- To study the various risks in investment of NB Bank in comparison to NABIL and NGBL and also to analyse the deposit utilization trend and its projection for next five years of the NB Bank & compare it with that of NABIL and NGBL.

The study was conducted through secondary data. M/S Thapa has found that the liquidity position of NB Bank is comparatively better than that of NABIL and NGBL.

NB Bank is not in better position regarding its on balance sheet as well as off balance sheet activities in compare to NABIL and NGBL. It does not seem to follow any definite policy regarding the management of its assets. Profitability position of NB Bank is comparatively worse than that of NABIL and NGBL. It has maintained high growth rates in comparison to other banks though it is not successful to make enough investment. The position of NB Bank in regard to utilization of the fund to earn profit in not better in compare to NABIL and NGBL.

Laudari (2001) conducted a study on "A study on investment policy of Nepal Indosuez Bank Ltd. in comparison to Nepal SBI Bank Ltd." with the objectives of: -

- To examine the liquidity, asset management and profitability position and investment policy of NIBL in comparison to Nepal SBI bank ltd.
- To study the growth ratios of loans and advances and investment to total deposit and net profit of NIBL in comparison to Nepal SBI bank ltd.
- To analyse relationships between deposit and investments, deposits and loan & advances, net profit and outside assets of Nepal Indosuez Bank Ltd. in comparison to Nepal SBI Bank Ltd.

Mr. Laudari found that the current ratios for both the Banks is satisfactory. Although cash reserve ratio (CRR) is managed by both banks as per Nepal Rastra Bank directives, both banks have not paid sufficient insight toward cash management. Nepal SBI Bank Ltd. has increased investment in government securities where as Nepal Indosuez Bank Ltd. has decreased. Nepal Indosuez Bank Ltd. has maintained both current ratio and cash reserve ratio better than Nepal SBI Bank Ltd. But its cash and bank balance, investment in government securities and loan and advances in comparison to current assets are lower than that of Nepal SBI Bank Ltd. Deposit utilization of Nepal Indosuez Bank Ltd. is less effective than that of Nepal SBI Bank Ltd. Nepal Indosuez Bank Ltd. did a better performance in return on total assets and loan and advances and interest earning. The analysis of growth ratios shows that growth ratios of total deposit, loan and advances, total investment and net profit of Nepal Indosuez Bank Ltd. is less than that of Nepal SBI Bank Ltd. The trend value of loan and advances to total deposit ratio and total investment to total deposits ratio is decreasing in case of both the banks. *(The study was conducted through secondary data).*

Dhungana (2002) conducted a study on "Investment policy of Nepal Bangladesh Bank Limited & other Joint Venture Banks (Himalayan Bank Limited & Nepal SBI Bank Limited)." with the following objectives:

-) To study fund mobilisation and investment policy with respect to fee based off-balance sheet transaction and fund based on balance sheet transaction and the liquidity efficiency of assets management and profitability position.
-) To evaluate the trends of deposit utilisation towards total investment and loan & advances, the growth ratios of loan & advances and total investment with respect to growth ratios of total deposit and net profit.
-) To study the various risks in investment.

The research found out that the liquidity position of NB bank is not better than that of HBL and NSBL but it is in better position regarding its on balance sheet activities but not better regarding off-balance sheet transactions. The profitability position of NB bank is comparatively not better than that of HBL but better than that of NSBI. The credit risk ratios and interest rate risk ratios of NB Bank is higher than that of HBL and NSBI. It has not maintained adequate capital in relation to the nature and condition of its assets, its deposit liabilities and other corporate liabilities. NB Bank has maintained high growth rate and deposit collection position, lending position, investment position and net profit position is not better in comparison to HBL but better than NSBI. *(The study was conducted on the basis of secondary data)*

Ojha (2002) conducted a study on "Lending practices: A study on NABIL Bank Ltd., SCB Nepal Ltd. and Himalayan Bank Ltd." with the objective of:

-) To determine the liquidity position, the impact of deposit in liquidity and its effect on lending practices.
-) To measure the bank's lending strength.
-) To analyze the portfolio behavior of lending and measuring the ratio and volume of loans and advances made in agriculture, priority and productive sector.
-) To measure the lending performances in quality, efficiency and its contribution in total income.

Based on the research, the measurement of liquidity has revealed that the mean current ratio of all the three banks is not widely varied. The total liability to total assets of SCBNL has the highest ratio. Himalayan Bank Ltd. has high volume of saving and fixed deposits as compared to current deposit. SCBNL's tendency to invest in government securities has resulted with the lowest ratio of loans and advances to total assets ratio whereas NABIL Bank Ltd. has highest due to steady and high volume of loans and advances throughout the years. The loans and advances and investment to deposits ratio has shown that NABIL Bank Ltd. has deployed the highest proportion of its total deposits in earning activities. The absolute measures of lending strength have revealed that the mean volume of net assets and deposits is highest in SCBNL with moderate variation. The volume of net assets of Himalayan Bank Ltd. is the least due to the low share capital, reserves and surplus in its capital mix. But the volume contributed by Himalayan Bank Ltd. in case of loans and advances is highly appreciable as compared to its net assets. The volume of loans and advances contributed by NABIL Bank Ltd. is the greatest in five years of study period. The mean investment of NABIL Bank Ltd. is the highest but the investment on government securities of SCBNL is the highest. The contribution made by Himalayan Bank Ltd. in industrial sector is the greatest and that of SCBNL is the least. The lending in commercial purpose is highest in case of NABIL Bank Ltd. and least in case of SCBNL. SCBNL has highest contribution in service sector lending. The loan loss provision to loans and advances analysis shows that NABIL Bank Ltd. has the highest mean ratio. It indicates that the volume of sub-standard loan in the loan mix of NABIL Bank Ltd. is higher and the volume of non-performing loan in the mix of NABIL Bank Ltd. is likely to increase in coming future. The mean ratio of interest income to total income has concluded that the contribution of interest income in total income is higher in case of Himalayan Bank Ltd. and lower in case of SCBNL. The interest expenses to total deposits ratio indicates that the cost of fund in Himalayan Bank Ltd. is the highest and that of SCBNL is the least. The productivity of expenses in SCBNL is the best. Thus, the performance of SCBNL is significantly better than other two banks in case of profitability. EPS is highest in case of SCBNL. *(The study was conducted on the basis of secondary data.)*

Shahi (2004) conducted a study on "Investment policy of commercial banks in Nepal" with the main objectives of:

-) To evaluate the liquidity, profitability and risk position of Nepal bank limited to the Joint venture banks and to discuss investment policy of Nepal bank limited in comparison to the Joint venture banks.
-) To find out the empirical relationship between different variables as deposits, loan and advances, investment, net profit, etc. and compare them with the Joint venture banks and to analyze the deposit utilization trend and compare it with that of the Joint venture banks.
-) To provide a package of workable suggestions and possible guidelines to improve investment policy of Banks.

Mr. Shahi found that the liquidity position of NBL is comparatively better than that of the JVBs. The mean ratio of loan and advances to total deposit of NBL is slightly lower than that of the JVBs. Likewise NBL's ratios seem to be more variable than that of the JVBs. The mean ratio of total investment to total deposit of NBL is lower than that of the JVBs. The mean ratio of investment on government securities to total working fund of NBL is slightly lower than that of the JVBs. The mean ratio of total off-balance sheet operation to loan and advances of NBL is found significantly lower than that of JVBs. Profitability position of NBL is comparatively not better than that of the JVBs. There is comparatively higher risk in NBL than that of the JVBs regarding various aspects of the banking function. From the analysis of different growth ratios it can be concluded that NBL has not been more successful to increase its sources of funds. Similarly it seems to have failed to maintain high growth rate of profit in comparison to that of other JVBs. It has been found that there is negative relationship between deposits and investment in case of NBL and positive in case of the JVBs. NBL has higher trend analysis values of loan and advances and deposit, but lower trend values of net profit and total investment in comparison to the JVBs for next 5 years.

High portion of cash and bank balance in NBL shows its negligence and inefficiency in its best utilization. Higher percentage of loan loss ratios shows that NBL is weak in credit collection. Poor quality of loan due to lack of necessary skills of project

appraisal, improper collateral evaluation, irregular supervision, etc. is a severe problem for the bank's success. *(The research was conducted mainly on the basis of the secondary data)*

Shrestha (2004) on his thesis entitled "Role of Rastriya Banijya Bank in priority sector credit & its recovery" has tried to reveal the following objectives:

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

The major findings made by the researcher found that the Bank's total no of borrowers in PSC about 76 % to 78 % of borrowers lie under DSC & out of the total loan outstanding of RBB invested on PSC about 28 % to 29 % has been invested under DSC. RBB is very much success in complying the NRB policy. The study reveals that the disbursement & recovery under DSC is in decreasing trend; however the ratio of repayment to disbursement is in increasing trend. Loan repayment under DSC was more satisfactory from industry sector. The trend values of recovery of RBB under PSC shows that the recovery position of the bank is in downward sloping whereas its overdue loan under PSC is in increasing trend which brings no return to the bank.

Basnet (2005) conducted a study on "A study on the investment policy of NABIL Bank Ltd. in comparison to other Joint venture Banks of Nepal" with the objective:

- To evaluate the liquidity and profitability positions in relation to fund mobilization of NABIL Bank Ltd. in comparison to other Joint venture Banks.
- To discuss fund mobilization and investment policy of NABIL Bank Ltd. in comparison to other JVBS.

- To evaluate the growth ratios of loan and advances and total investment with respective growth rate of total deposits and net profit of NABIL Bank Ltd. in comparison to other JVBS.
- To find out the relationship between deposits and total investment, deposit and loan and advances, and net profit and outside assets of NABIL Bank Ltd. in comparison to other JVBS.

The study was conducted using secondary data. The research found that the liquidity position of NABIL Bank Ltd. is comparatively worse than that of other JVBS. It has more portions of current assets as loans and advances but less portion as investment on government securities. NABIL Bank Ltd. is comparatively less successful in on-balance sheet operation as well as off-balance sheet operations than that of other JVBS. Profitability position of the Bank is comparatively not better than that of other JVBS. The mean ratio of return on loan and advances of NABIL Bank Ltd. has been found slightly lower than that of other JVBS. Similarly the mean ratio of total interest earned to total outside assets of NABIL Bank Ltd. has been found slightly lower than that of other JVBS.

Though NABIL Bank Ltd. seems to be more successful to increase its sources of funds as well as mobilization of it by increasing loan and advances and total investment, it seems to be failure to maintain its high growth rate of profit in comparison to that of other JVBS. There is significant relationship between deposit and loan and advances as well as outside assets and net profit but not between deposit and total investment in case of both NABIL Bank Ltd. and other JVBS.

Gurung (2006) explored in his research “lending policy and recovery management of Standard Chartered Bank Nepal Ltd and Nabil bank Ltd” has found out the following result.

-) The deposit collection by the bank is increasing but in a fluctuating trend.
-) Out of different types of deposit collection account, higher account has been collected in saving deposit account. Out of the total deposit collection, SCBNL has disbursed 36% of average as a loan and Nabil has disbursed 52% of its

deposit collection as a loan disbursement to deposit collection ratio of commercial banks, it is around 60%.

) This ratio is quite low incasing of sample bank especially of SCBNL. It is further proved by the calculation of correlation coefficient, which is 0.75 and 0.23 of SCBNL and Nabil respectively.

While looking on the loan loss provision of SCBNL it is in decreasing trend from 2002. The correlation coefficient of loan loss provision and loan disbursement of SCBNL is 0.36. While looking at the future trend it shows the increasing trend in case of SCBNL and the trend of Loan loss provision is decreasing every year in case of Nabil. The correlation of loan loss provision and loan disbursement of Nabil is negative.

The main statement of his problem shows many banks are mushrooming although banks are not interested to expand their branch in remote rural area. There are difficulty and length formality of procedure for long term and medium term as well as short-term loan, Low deposit habit of Nepalese people and lack of strong recovery act of lending and bad debt. The main objectives of the dissertation are loan and advance providing procedure of bank, lending and investment sector of bank, recovery condition of both SCBNL and NABIL bank.

Pokharel (2007) conducted a study on "Investment pattern and policy of Rastriya Banijya bank" with the objective of:

- To review the present investment policy of RBB.
- To examine whether the bank has been fully utilizing the deposits mobilized or not.
- To establish the relationship between deposits, loans and advances and the effect on them by the change of interest rate.
- To recommend for the improvements in the investment policy.

The research was conducted mainly on the basis of secondary data. Interview technique has also been used to collect information on the investment policy of the bank.

The research findings of the study are concluded as:

- From the study of investment pattern of RBB, it is observed that the investment is mainly towards the security of gold and silver.
- From the study it has been revealed that there has never been any clear and specific investment policy. In fact the bank is running its business without having any definite direction, except to follow the directives issued by NRB.
- The deposits raised by the bank are not properly utilized. The effect of changes in interest rate has neither contributed to raise deposits nor has been favorable in investment extension.
- Time to time checking and supervision by the bank should be faithfully followed.

Silwal (2009) has conducted a study on "Lending policy of commercial banks in Nepal" with the objective of:

- To analyze the role of commercial banks in its historical prospective.
- To show the relationship between deposits and loan & advances.
- To identify major weakness of lending policy of the commercial banks.

The research findings of the study are summarized as follows:

Effectiveness of lending policy is directly based upon a sound banking system. But due to geographical variation, transportation and other regional disparities, it is very difficult to expand branches in different rural areas. So, it can be said that commercial banks in Nepal are not playing an active role to utilize their sources collected from different sectors.

By paying higher interest rate, the banks are increasing deposits, which in turn increase saving habits of the general people. Then the banks will be able to utilize these idle funds in productive channels. This type of business of commercial bank is really a necessary one in an agricultural country like Nepal, where public investment has limited capacity. (*The research was conducted mainly on the basis of secondary data*).

Limbu, (2010) in his dissertation "Credit Management of NABIL Bank Limited" highlighted that aggregate performance and condition of Nabil bank. In the aspect of liquidity position, cash and bank balance reserve ratio shows the more liquidity position. Cash and bank balance to total deposit has fluctuating trend in 5 years study

period. Cash and bank balance to current deposit is also fluctuating. The average mean of Cash and bank balance to interest sensitive ratio is able to maintain good financial condition

In the aspect of assets management ratio, assets management position of the bank shows better performance in the recent years. Non-performing assets to total assets ratio is decreasing trend. The bank is able to obtain higher lending opportunity during the study period. Therefore, credit management is in good position of the bank. In leverage ratio, Debt to equity ratio is in an increasing trend. High total debt to total assets ratio posses' higher financial risk and vice-versa. It represents good condition of Total assets to net worth ratio. In the aspect of profitability position, total net profit to gross income, the total interest income to total income ratio of bank is in increasing trend. The study shows the little high earning capacity of NABIL through loan and advances. Earnings per share and The Price earning ratio of NABIL is in increasing trend. These mean that the better profitability in the coming last years. It represents high expectation of company in market and high demand of share. Loan loss provision to total loan and advances ratio and None-performing loan to total loan and advance ratio of NABIL is in decreasing trend. The ratio is continuously decreasing this indicates that bank increasing performance. Thus, credit management is in a good position.

The main objectives of the research study are as follow.

-) To evaluate various financial ration of the Nabil Bank.
-) To analyze the portfolio of lending of selected sector of banks
-) To determine the impact of deposit in liquidity and its effect on lending practices.
-) To offer suitable suggestions based on findings of this study.

In the statistical tools analysis, average mean, correlation analysis and trend analysis have been calculated. Correlation coefficient between total credit and total assets shows high degree of positive correlation. Correlation coefficient between total deposit and loan & advances has high degree of positive correlation it is concluded that increasing total deposit will have positive impact towards loan & advances.

Trend analysis tools are done for future forecasting. Trend analysis for total deposit is calculated to see future deposit trend of the bank. Trend analyses for loan & an advance is done to see future loan & advances. Trend analyses for Total asset is calculate to see future total asset.

The study is conducted on credit management of Nabil Bank, which is one of the leading banks in Nepal. NABIL has been maintaining a steady growth rate over this period. In the study every aspect of banks seems to be better and steady in every year. Its all analysis indicates better future of concern bank.

Shrestha, (2010) has conducted a thesis research entitled "*Investment portfolio Analysis of JVB's*".

The specific objectives of the study were:-

To analyze the risk and return ratios of commercial banks.

To evaluate the financial performance of JVB's.

To provide suggestion package based on the analysis of data.

To study existing investment policies taken by NIBL in various sectors.

To study portfolio structure of NIBL in investment as compared to other JVB's.

Preference given by NIBL for investment between, Loan Investment, Investment in real fixed assets, Investment in financial assets.

The main findings of the study were:

BOKL has the highest return on shareholders' fund and total assets. It has also been successful in mobilizing its deposits as investments. NIBL and EBL have invested high amounts of deposits as loan and advances in comparison to BOKL, NIBL and HBL.

Among the JVB's, looking at the investment portfolio, EBL has investment highest amount of funds in government securities, NBB has invested highest amount of funds

on shares and debentures and NIBL has invested highest amount of funds in NRB bonds in comparison to other JVB's.

BOKL has the highest EPS and EBL the lowest EPS among the JVB's Commercial banks have huge deposit collection. These deposits need to be properly utilized. Effective utilization of collected fund is possible only through implementation of sound investment policy.

NIBL and BOKL are the best examples of Commercial Banks in Nepal that have been able to mobilize the funds in an effective manner and achieved phenomenal growth and profit year after year by formulating and implementing sound investment policy. Most research studies conducted prior to this study involving comparative analysis comprised of a successful bank and an emerging bank as samples. It was obvious that the successful bank with sound financial health would excel in various aspects of banking. The possibility of the samples showing different result during data analysis was high. The financial and empirical analysis to data revealed higher degree of consistency in case of successful bank and less uniformity in case of emerging bank.

This study comprises of two of the most successful Commercial Banks as sample viz NIBL and BOKL. This study is also different from previous studies in view of the time period its covers. During this period the country has witnessed political uncertainty, deteriorating security situation that have rendered the economy further sluggish. There has been a restructuring in the banking business.

This study gives a new dimension to the research topic in the sense that it has adhered to most of the fresh guidelines and directives issued by NRB to commercial banks, which previous studies lack. This study aims at providing a more realistic picture to various financial aspects of the sample banks. In line with fresh guidelines and NRB directives and practices adopted by banks, some items of the balance sheet that were previously booked under one heading have now been accounted under a different heading. For instance, leasehold improvements or deferred expenditure that were previously a part of current assets have been accounted for under fixed assets as they are amortized over the period of lease. Similarly, staff loan and advances previously

part of Loan Advances and Bills purchase have been booked under other assets, checks presented for clearing have been booked under other assets. Gratuity is expensed on accrual basis and is now a part of personnel expense. Previously, it was the practice of banks to include it under current liabilities and appropriate it from profit and loss Account. This study will reveal the strength and weaknesses of the sample bank and serve as a valuable input in decision-making process of the concerned banks and other emerging banks in formulating appropriate investment policy.

Gautam (2010) conducted a study on " Investment policy of Nepal SBI Bank Ltd. with the objective of:

-) To find out the Non Performing Assets position of the bank in relation to loans and advances
-) To analyze the portfolio management of the bank,
-) To identify the bank's investment on priority sector,
-) To analyze deposit utilization and its relationship with total investment and net profit of the bank.

The study was conducted using secondary data. The research found that the liquidity position of NSBL is comparatively worse than that of other JVBS. It has more portions of current assets as loans and advances but less portion as investment on government securities. NSBL. is comparatively less successful in on-balance sheet operation as well as off-balance sheet operations than that of other JVBS. Profitability position of the Bank is comparatively not better than that of other JVBS. The mean ratio of return on loan and advances of NSBL has been found slightly lower than that of other JVBS. Similarly the mean ratio of total interest earned to total outside assets of NSBL has been found slightly lower than that of other JVBS.

Shrestha (2011) conducted a study on "An investment policy of Machhapuchhre Bank Ltd. with the objective of:

- To study the resource mobilization and investment policy of MBL.
- To identify investment sector.
- To find out the relationship between deposit and investment trends of the bank.

- To evaluate financial efficiency and performance (profitability, risk, liquidity and assets management) of MBL.
- To recommend the policies to be adopted by the sample organization in the financial analysis for its future development

Mr. shtestha found that banking sector plays an important role in the economic development of the country. Commercial banks are one of the vital aspects of this sector, which deals in the process of channelling the available resources in the needed sector. It is the intermediary between the deficit and surplus of financial resources. Financial institutions like banks are a necessity to collect scattered savings and put them into productive channels. In the absence of such institutions it is possible that the saving will not be safely and profitably utilized within the economy. It will be diverted aboard or channelled into unproductive conspicuous consumption including real estate speculation.

Investment operation of commercial banks is a very risky one. It is the most important factor from the point of view of shareholders and bank management. For this, commercial banks have to pay due consideration while formulating investment policy. A healthy development of any commercial bank depends upon its investment policy. A good investment policy attracts both borrowers and lenders, which helps to increase the volume of quality deposits, loans and investment.

The major source of income of a bank is interest income from loan and investment and fee based income. As .loan and advances dominate the assets side of the balance sheet of any bank, similarly earnings from such loans & advances occupy a m3jor space in the income statement of the bank. However, it is very important to be reminded that most of the bank failures in the world are due to the shrinkage in the value of loans-& advances. Hence loan is known as risky assets and investment operation of commercial banks is very risky one. Risk of and-payment of loan is known as credit risk of default risk. Performing loans have multiple benefits to the society by helping for the growth of economy while non- performing loans erodes even existing capital. Considering the importance of lending to the individual banks and also to the society it serves, it is imperative that the bank meticulously plans its credit operations.

2.3 Research Gap

Investment in different sectors is made on the basis of the directives and circulars of Nepal Rastra Bank as well as the investment guidelines and policy of the concerned commercial bank. The directives of NRB change over time. NRB makes necessary amendments in prevailing directives and circulars and communicates to commercial banks. Commercial banks should follow these directives and circulars. Furthermore, their own investment guidelines and policies should be in line with NRB directives and circulars. So, the up to dated study over the change of time frame is major concern for the researcher and concerned organization as well as industry as a whole. This study covers the more recent financial data, NRB circulars and guidelines than that of studies previously conducted.

No research has yet been undertaken regarding the sector-wise loan and advances diversification of NSBL. Portfolio management is the major part of the bank's investment policy. The optimum diversification of loan and advances reduced the default risk of credit. It is the major concern of stakeholders to know the portfolio behavior of the bank. This study puts its effort to find out the proportion of total loan and advances of the bank disbursed to different sectors of economy and analyse the diversification of its investment.

No case study has yet been conducted about the investment policy of NSBL. Some comparative studies are previously done but in-depth study about the bank is not found. Investment function is the major function of the commercial bank. NSBL is one of a leading joint venture commercial bank of the country having huge market share and its investment activities has significant impact on the national economy. Hence, this study fulfills the prevailing research gap about the in depth analysis of the investment policy pursued by the organization, which is the major concern of public shareholders and other stakeholders.

CHAPTER - III

RESEARCH METHODOLOGY

Research methodology refers to the various sequential steps to be adopted by a researcher in studying a problem, with certain objectives in view. In other words, research methodology describes the methods and processes applied in the entire subject of the study. Research Methodology is a way to systematically solve the research problem. It may be understood as a science of studying how research is done significantly. It is necessary for the researcher to know not only the research methods / techniques but also the methodology. Researchers not only need to know how to develop certain indices or tests, how to calculate the mean, the mode, the research techniques, but they also need to know which of these methods or techniques are relevant and which are not, and what would they mean and indicate and why.

The topic of the problem has been selected as "Investment Policy of Nepal SBI Bank Limited". The sole objective of this study is to evaluate the investment policy of Nepal SBI Bank Limited. In order to reach and accomplish the objectives of the study, different activities are carried out and different stages are crossed during the study period. For this purpose the chapter aims to present and reflect the methods and techniques those are carried out and followed during the study period. The research methodology adopted for the present study is mentioned in this chapter which deals with research design, sources of data, data collection, processing and tabulating procedure and methodology.

3.1 Research Design

A research design is purely and simply the framework or plan for a study that guides the collection and analysis of data. Research design is the plan, structure and strategy of investigations conceived so as to obtain answers to research questions and to control variances. A true research design is basically concerned with various steps to collect the data for analysis and draw a relevant conclusion. It is the arrangement of conditions for collection and analysis of data that aims to combine relevance to the research purpose with economy in procedure. To achieve the objective of this study, descriptive and analytical research design has been used. Some financial and

statistical tools have been applied to examine facts and descriptive techniques have been adopted to evaluate investment policy of Nepal SBI Bank Limited.

3.2 Population and Sample

The population refers to the industries of the same nature and its services and product in general. Thus, the total Commercial Banks constitutes the population of the data and the bank under study constitutes the sample for the study. So, from the population of 31 Commercial Banks operating in Nepal, Nepal SBI Bank Limited has been selected as the sample for the study.

3.3 Sources of Data

Data are collected from two sources. They are Primary sources and Secondary sources. The data presented in this study are of secondary type. The secondary sources of data are those that have been used from published sources or used by someone previously. The annual reports of the concerned Bank are the major sources of data for the study. However, besides the annual reports of the subjected bank, the following sources of data have also been used in the course of the study:

- NRB reports and bulletins.
- Various publications dealing in the subject matter of the study.
- Various articles published in the News Papers.
- Periodic returns submitted by the Bank's Head Office to NRB.
- The NEPSE reports, etc.

Formal and informal talks with the concerned authorities of the bank were also helpful to obtain the additional information of the related problem.

3.4 Data Collection Techniques

This study is mainly based on secondary data obtained from various sources mentioned above. The annual reports of Nepal SBI Bank Limited for the period of five years from fiscal year 2007/08 to 2011/12 A.D were obtained from the field visit of its shares department at its corporate office located at Hattishar, Kathmandu. NRB publications such as Quarterly Economic Bulletins, Banking and Financial Statistics,

Economic report, etc. have been collected by the personal visit of concerned departments of Nepal Rastra Bank at Baluwatar. The unpublished data of sector wise loans and advances has been collected from reporting department of NSBL. The data on some aspects of the bank has also been obtained from the publications and websites of Nepal Stock Exchange. The reference of NRB directives has been used from Butwal Branch of NSBL. Some supplementary data and information and literature review have been collected from the Central Library T.U., Central Department of management, kirtipur, Shankar Dev Campus Library, NRB Library, different Journals, magazines and other published and unpublished reports documented by the concerned authorities.

3.5 Data Analysis Tools

Presentation and Analysis of the collected data is the core of the research work. The collected raw data are first presented in systematic manner in tabular forms and are then analysed by applying different financial and statistical tools to achieve the research objectives. Besides these, some graph charts and tables have been presented to analyze and interpret the findings of the study. The tools applied are:

3.5.1 Financial Tools

Financial tools basically help to analyze the financial strength and weakness of a firm. Ratio analysis is one of the important financial tools that have been used in the study. A ratio is simply one number expressed in term of another and such it expresses the quantitative relationship between any two numbers. Ratio can be expressed in terms of percentage, proportion and as coefficient. Logarithmic graph and break-even chart are the graphic forms of expressing a ratio. Financial ratio is the mathematical relationship between two accounting figures. Ratio analysis is a part of the whole process of analysis of financial statements of any business or industrial concern especially to take output and credit decisions. Even though there are many ratios to analyze and interpret the financial statement, only those ratios that are related to the investment operation of the bank are have been covered in this study. Different types of ratios have been used in this study.

3.5.1.1 Liquidity Ratios

This ratio measures the liquidity position of a firm. It measures the firm's ability to meet its short-term obligations or its current liabilities. It measures the speed with which a bank's assets can be converted into cash to meet deposit withdrawal and other current obligations. As a financial analytical tool, following four liquidity ratios has been used to come into the facts and findings of the study.

(i) Current ratio

This ratio shows the banks short-term solvency. It shows the relationship between current assets and current liabilities.

Current assets includes cash (Nrs), cash (foreign currency), balance with other banks, balance held aboard, inter-bank lending, bills purchased/discounted, 40% of loan and advances (assumption), investment on government securities(treasury bills), interest receivable and staff loan and advances. Similarly, current liabilities includes Current Deposits, Saving Deposits,(assumption) Other deposits (margin,calldeposit), Forex Deposits, Expense Payable, Bonus Payable, Income Tax Payable and Proposed Dividend.

Current Assets

Current Liabilities

The widely accepted standard of current ratio is 2:1 but accurate standard depends on the circumstances of the business and the nature of business.

(ii) Cash and bank balance to total deposit ratio

Cash and bank balance are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositor.

This ratio is computed by dividing cash and bank balance by total deposit. This can be presented as,

Cash & bank balance

Total deposits

Cash and bank balance includes cash in hand, foreign cash in hand, cheques and other cash items, balance with domestic and foreign banks. The total deposit includes current deposits, saving deposits, fixed deposits, call deposits and other deposits.

(iii) Cash and bank balance to current assets ratio

This ratio measures the proportion of most liquid assets i.e. cash and bank balance among the total current assets of the bank. Higher ratio shows the bank's ability to meet its demand for cash.

The ratio is computed by dividing cash and bank balance by current assets, stated as under,

$$\frac{\text{Cash \& bank balance}}{\text{Current assets}}$$

(iv) Investment on government securities to total current assets ratio

This ratio is calculated to find out the percentage of current assets invested in government securities i.e. treasury bills and development bonds. The ratio is computed as under,

$$\frac{\text{Investment on government securities}}{\text{Total current assets}}$$

3.5.1.2 Asset Management Ratios

Asset management ratio measures the proportion of various assets and liabilities in balance sheet. The proper management of assets and liability ensures its effective utilization. The banking business converts the liability into assets by way of its lending and investing functions. Asset and liability management ratio measures its efficiency by multiplying various liabilities into performing assets. The following are the various ratios relating to asset and liability management, which are used to determine the efficiency of the subjected bank in managing its assets and efficiency in portfolio management

(i) Loan & Advances to total deposit ratio

This ratio is also called credit-deposit ratio (CD ratio). It is calculated to find out how successfully the banks are utilizing their total deposits on loan and advances for profit generating purpose. Greater ratio implies the better utilization of total deposits. This ratio can be obtained by dividing loan and advances by total deposit as under,

$$\frac{\text{Loan and advances}}{\text{Total deposits}}$$

(ii) Total investments to total deposit ratio

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

$$\frac{\text{Total investment}}{\text{Total deposits}}$$

The numerator includes investment on government securities, debenture and bond, shares in subsidiary companies, shares in other companies and other investment.

iii) Loan and advances to working fund ratio

Loan and advances is the major component in the total working fund (total assets), which indicates the ability of bank to channelize its deposits in the form of loan and advances to earn high return.

This ratio is computed by dividing loan and advances by total working fund, that is stated as under,

$$\frac{\text{Loan and advances}}{\text{Total working fund}}$$

Here, the denominator includes all assets of on balance sheet items but excludes off balance sheet items like letter of credit, letter of guarantee etc.

iv) Investment on government securities to total working fund ratio

This ratio shows that bank's investment on government securities in comparison to the total working fund. This ratio is calculated by dividing investment on government securities by total working fund. This is presented as,

$$\frac{\text{Investment on government securities}}{\text{Total working fund}}$$

v) Investment on shares and debenture to total working fund ratio

This ratio shows the bank's investment in shares and debenture of the subsidiary and other companies. This ratio can be derived by dividing investment on shares and debentures by total working fund mentioned as under,

$$\frac{\text{Investment on government securities}}{\text{Total working fund}}$$

The numerator includes investment on debentures, bonds and shares of other companies.

Total outside assets to total deposits ratio

(vi) Total outside asset to total deposit ratio

Loan & Advances and investment comprises the total outside assets of a bank. This ratio measures how well the deposits liabilities have been mobilized by the bank in income generation. This ratio is computed by dividing total loan and advances and investment by total deposits.

$$\frac{\text{Total outside asset}}{\text{Total deposit}}$$

(vii) Loan & Advances to total outside assets ratio

This ratio measures the contribution made by loans & advances in total amount of loans and advances and investments. The proportion between investment and loans and advances measures the management's attitude towards more risky assets and lower risky assets. Loans & Advances are more risky and also generate more returns in comparison to investments. This ratio is computed by dividing Loan & Advances by total outside assets as under,

$$\frac{\text{Loan and advances}}{\text{Total outside asset}}$$

(viii) Investment on government securities to total outside assets ratio

This ratio measures the proportion of the banks investment in risky area and risk free areas. This ratio is computed by dividing investment on government securities by total outside asset as under,

$$\frac{\text{Investment on government securities}}{\text{Total outside asset}}$$

(ix) Total outside assets to total assets ratio

Loans & Advances and investments are the outside assets of commercial banks. This ratio is calculated by dividing total outside assets by total assets

$$\frac{\text{Total outside asset}}{\text{Total asset}}$$

These are the proportion of assets employed by the bank for the purpose of income generation. This ratio shows the ability of the bank to utilize its funds into income generating assets.

(x) Total Off-Balance sheet operation to Loan & Advances ratio

The OBS operation shows the bank's efficiency in conducting modern off-balance sheet transaction in comparison to loan and advances i.e. issue of letter of credit, letter of guarantee etc. This ratio shows the proportion of fee-based off-balance sheet activities to fund based loan and advances of the bank. Now a day fee-based off-balance sheet activity play an important role for the better performance of a bank. This ratio is calculated by dividing total OBS operations by loan and advances, which is stated as hereunder,

$$\frac{\text{Total OBS operation}}{\text{Loan and advances}}$$

3.5.1.3 Activity of Performing Ratios

Activity ratio measures the performance efficiency of an organization from various angles of its operations. These ratios indicate the efficiency of activity of an enterprise to utilize available funds, particularly short-term funds. These ratios are used to

determine the efficiency, quality and the contribution of loans and advances in the total profitability. The following activity ratios measure the performance efficiency of the bank to utilize its funds

(i) Loan loss provision to total loans and advances ratio

The ratio of loan loss provision to total loans and advances describes the quality of assets that a bank is holding. Nepal Rastra Bank has directed the commercial banks to classify its loans & advances into the category of pass, sub-standard, doubtful and loss on the basis of the maturity of principal, to make the provision of 1, 25, 50 & 100 percentage respectively. The provision for loan loss reflects the increasing probability of non-performing loans in the volume of total loans and advances. This ratio is calculated by dividing the loan loss provision by total loans and advances as presented hereunder.

Total loan loss provision

Total loans and advances

(ii) Non-performing loans to total loans & advances ratio

This ratio measures the proportion of non-performing loans on the total volume of loans and advances. This reflects the quantity of quality assets that the bank have. Higher ratio reflects the bad performance of the bank in mobilizing loans and advances and bad recovery rate and vice versa. This ratio is computed by dividing the non-performing loans by total loans and advances as under.

Non-performing loans

Total loans and advances

3.5.1.4 Loans & Advances Portfolio

To analyze the portfolio behavior of loans and advances of the bank for the study period, the ratios of loans & advances granted to various sectors of economy and for various purposes to total volume of loans and advances have been measured. Under this topic the following ratios have been studied.

(i) Priority sector lending to total loans & advances ratio

This ratio measures the contribution of banks lending in priority sector as directed by NRB. Under the priority sector, credit to agriculture and agro based business, cottage

and small industries, service sector and other business are included. Credit to the deprived sector is also a part of priority sector lending. The priority sector lending requirement is 12% for the study period, except for the year 2002/03, for which it is decreased to 7%. This ratio is calculated by dividing priority sector lending by total loans and advances as under,

$$\frac{\text{Priority sector lending}}{\text{Total loans and advances}}$$

(ii) Sector wise loan and advances classifications

Here, the total loans and advances diversified to different sectors of the economy are calculated. Total economy has been classified into five sectors as agricultural sector, industrial/ production sector, trading/ commercial sector, service sector and others. These ratios are computed by dividing sector wise loan and advances by total loan and advances

3.5.1.5 Profitability ratios

Profitability ratios are used to indicate and measure the overall efficiency of a firm in terms of profit and financial performance. For better performance, profitability ratios of firms should be higher. Under this topic the following profitability ratios of Nepal SBI Bank Ltd. have been studied.

(i) Interest income to total income ratio

This ratio measures the volume of interest income in total income of the bank. The high ratio indicates the high contribution made by the lending and investing activities and vice versa. This ratio can be computed by dividing interest income to total income presented as under.

$$\frac{\text{Interest Income}}{\text{Total income}}$$

(ii) Total interest earned to total outside assets ratio

This ratio measures the interest earning capacity of the bank through the efficient utilization of out side assets. Higher ratio implies efficient use of outside assets to

earn interest. This ratio is calculated by dividing total interest earned by total outside assets and can be mentioned as,

$$\frac{\text{Total interest earned}}{\text{Total outside assets}}$$

The denominator includes loan and advances, bills purchased and discounted and all types of investments. The numerator comprises total interest income from loans and advances and investments.

(iii) Interest expenses to total expenses ratio

This ratio measures the portion of total interest expenses in the volume of total expenses. The high ratio indicates the low operational expenses and vice versa. This ratio is computed by dividing interest expenses by total expenses, which is presented hereunder,

$$\frac{\text{Interest Expenses}}{\text{Total Expenses}}$$

(iv) Total interest earned to total working fund ratio

This ratio is calculated to find out the percentage of interest earned to total assets (working fund). Higher ratio implies better performance of the bank in terms of interest earning on its total working fund. This ratio is calculated by dividing total interest earned by total working fund. This is stated as,

$$\frac{\text{Total interest earned}}{\text{Total working fund}}$$

(v) Total interest paid to total working fund ratio

This ratio is calculated to find out the percentage of interest paid on liabilities with respect to total working fund. This ratio can be calculated by dividing total interest paid by total working fund, which can be presented as,

$$\frac{\text{Total interest paid}}{\text{Total working fund}}$$

(vi) Total income to total expenses ratio

The comparison between total expenses and total income measures the productivity of expenses in generating income. The amount of income that a unit of expenses generates is measured by the ratio of total income to total expenses. The high ratio is indicative of higher productivity of expenses and vice versa. This ratio is calculated by dividing total income by total expenses.

$$\frac{\text{Total Income}}{\text{Total Expenses}}$$

(vii) Total income to total working fund ratio

This ratio measures how efficiently the asset of a business is utilized to generate income. It also measures the quality of assets in income generation. This ratio is calculated by dividing total income by total assets as stated hereunder,

$$\frac{\text{Total Income}}{\text{Total working fund}}$$

(viii) Return on loan and advances ratio

This ratio indicates how efficiently the bank has employed its resources in the form of loan and advances. This also measures the earning capacity of its loan and advances. This ratio is computed by dividing net profit (loss) by loan and advances. This can be expressed as,

$$\frac{\text{Net Profit (Loss)}}{\text{Loans and advances}}$$

(ix) Return on total working fund ratio (ROA)

This ratio measures the overall profitability of all working funds i.e. total assets. It is also known as return on assets (ROA). This ratio is calculated by dividing net profit (loss) by total working fund. This can be mentioned as,

$$\frac{\text{Net Profit (Loss)}}{\text{Total working fund}}$$

The numerator indicates the portion of income left to the internal equities after deducting all costs, charges and expenses.

(x) Return on equity ratio (ROE)

Net worth refers to the owner's claim of a bank. The excess amount of total assets over total liabilities is known as net worth. This ratio measures how efficiently the banks have used the funds of the owners. This ratio is calculated by dividing net profit by total equity capital (net worth). This can be stated as,

$$\frac{\text{Net Profit (Loss)}}{\text{Total equity capital}}$$

Here, total equity capital includes shareholder's reserve including profit and loss account, general loan loss provision and share capital i.e. ordinary share and preference share capital.

(xi) Earning Per Share (EPS)

EPS refers to net profit divided by total number of shares outstanding. The amount of EPS measures the efficiency of a firm in relative terms. This ratio is computed by dividing total net profit (loss) by total number of shares

$$\frac{\text{Net Profit (Loss)}}{\text{Total number of shares}}$$

(xii) Net Interest Margin

Net interest margin in general term is the difference between the interests received from investment on loan and advances and interest paid on deposits collected by the bank. It shows the bank's efficiency to earn high profit to meet various costs. Higher ratio shows the higher profitability and vice versa. This ratio is computed by dividing the difference between interest revenues from earning assets less interest costs on borrowed funds by total earning assets.

$$\frac{\text{Interest revenues from earning assets}-\text{Interest costs on borrowed funds}}{\text{Total earning assets}}$$

Here, interest revenues from earning assets is the total interest income of the bank and interest costs on borrowed funds is the total interest expenses of the bank. Total loan and advances comprises the total earning assets of the bank.

3.5.1.6 Growth Ratios

To examine and analyze the expansion and growth of the banking business, following growth ratios are calculated in this part of the study.

- (i) Growth ratio of total deposits
- (ii) Growth ratio of loan and advances
- (iii) Growth ratio of total investment
- (iv) Growth ratio of net profit

3.5.2 Statistical Tools

Some important statistical tools are used to achieve the objective of this study. In this study statistical tool such as mean, standard deviation, coefficient of variation, coefficient of correlation and trend analysis have been used.

3.5.2.1 Mean

A mean is the average value or the sum of all the observations divided by the number of observations and it is denoted and given by the formula:

$$\bar{X} = \frac{X}{N}$$

Where, \bar{X} = Mean of the values.

N = Number of Pairs of Observations.

During the analysis of data, mean is calculated by using the statistical formula 'AVERAGE' on excel data sheet on computer.

3.5.2.2 Standard Deviation

The standard deviation measures the absolute dispersion. It is said that higher the value of standard deviation the higher the variability and vice versa. Karl Pearson

introduced the concept of standard deviation in 1823 and this is denoted by the small Greek letter σ (read as sigma).

The formulas to calculate the standard deviation are given below:

$$\sigma = \sqrt{\frac{\sum x^2}{N}}$$

Where, $x = (X - \bar{X})$

During the analysis of data, standard deviation is calculated by using the statistical formula 'STDEV' on excel data sheet on computer.

3.5.2.3 Coefficient of Variation

The standard deviation calculated in the above formulas gives an absolute measure of dispersion. Hence, where the mean value of the variables is not equal, it is not appropriate to compare two pairs of variables based on standard deviation only. The coefficient of variation measures the relative measures of dispersion, hence capable to compare two variables independently in terms of their variability. The coefficient of variation (C.V.) is given by the following formula and this gives the percentage.

$$\text{Coefficient of variation (C.V.)} = \frac{\sigma}{\bar{X}} * 100$$

3.5.2.4 Measures of Correlation

We examine the relation between the various variables. The correlation between the different variables of a bank is compared to measure the performance of these banks. Correlation refers to the degree of relationship between two variables. If between two variables, increase or decrease in one causes increase or decrease in another, then such variables are correlated variables. The reliability of the value of coefficient of correlation is measured by probable error. The correlation coefficient between two variables describes the degree of relationship between those two variables. It interprets whether two or more variables are correlated positively or negatively. This tool analyzes the relationship between those variables of the bank which are helpful to make appropriate investment policy regarding deposit collection, fund mobilization and profit maximization. The Karl Pearson coefficient of correlation (r) is given by the following formula:

$$\text{Coefficient of correlation } (r) = \frac{\sum xy}{N \sigma_x \sigma_y}$$

Where,

$$x = (X - \bar{X}),$$

$$y = (Y - \bar{Y}),$$

$$\sigma_x = \text{Standard deviation of series X,}$$

$$\sigma_y = \text{Standard deviation of series Y.}$$

N = Number of Pairs of Observations.

During the analysis of data, correlation coefficient is calculated by using the statistical formula 'CORREL' on excel data sheet on computer.

$$\text{Probable Error of } r \text{ (P.Er.)} = 0.6745 \frac{\sigma_r}{\sqrt{N}}$$

The Karl Pearson coefficient of Correlation r always fall between -1 to $+1$. The value of correlation in minus signifies the negative correlation and in plus signifies the positive correlation. As the value of correlation coefficient reaches near to the value of zero, it is said that there is no significant relationship between the variables.

The coefficient of correlation has been interpreted based on probable error (P.Er.). If the value of correlation coefficient is greater than 6 times the value of probable error, the correlation coefficient is deemed as significant and reliable. If the value of correlation coefficient is less than probable error, the correlation coefficient is said to be insignificant and there is no evidence of correlation.

In this section of the study, Karl Pearson's coefficient of correlation has been used to find out the relationship between the following variables:

- (i) Correlation between Deposits and Loans and Advances
- (ii) Correlation between deposits and investments
- (iii) Correlation between loan and advances and net profit
- (iv) Correlation between investment and net profit

3.5.2.5 Trend Analysis

Among the various methods of determining trend of time series, the most popular and mathematical method is the least square method. Using this least square method, it has been estimated the future trend values of different variables. For the estimation of linear trend line following formula has been used.

$$y = a + bx$$

Where,

y= Dependent variable

x= Independent variable

a= y intercept

b= slope of the trend line

By using this method, trend analysis of following variable is conducted

- (i) Trend analysis of total deposit
- (ii) Trend analysis of loan and advances
- (iii) Trend analysis of investment
- (iv) Trend analysis of net profit

CHAPTER – IV

PRESENTATION AND ANALYSIS OF DATA

In this chapter, the data collected from various sources have been presented and analyzed to measure the various dimensions of the problems of the study and in major findings of the study are presented systematically.

4.1 Measuring the Liquidity Position of the Bank

A commercial bank must maintain its satisfactory liquidity position to satisfy the credit needs of the community, to meet demands for deposits withdrawal, pay maturity obligation in time and convert non cash assets into cash to satisfy immediate needs without loss to the bank and without consequent impact on long-run profitability of the bank. To measure the liquidity position of the bank, the following measures of liquidity ratio has been calculated and a brief analysis of the same has been done as below.

4.1.1 Current ratio:

This ratio indicates the ability of the bank to meet its current obligation. This is the broad measure of liquidity position of the bank. This ratio shows the banks short-term solvency. It shows the relationship between current assets and current liabilities. Current assets includes cash (NRs), cash (foreign currency), balance with other banks, balance held aboard, inter-bank lending, bills purchased/discounted, 40% of loan and advances (assumption), investment on government securities(treasury bills), interest receivable and staff loan and advances. Similarly, current liabilities includes non-interest bearing accounts, Saving Deposits, non-interest bearing Other deposits (margin), Forex Deposits, Expense Payable, Bonus Payable, Income Tax Payable and Proposed Dividend. It is derived by dividing total current assets by total current liabilities. (Detail in -III). The current ratios of NSBL are given in the following table 1.

Table 1

Current ratios (Times)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	1.34	0.97	1.10	1.24	1.14	1.158	0.125	10.85

(Source: -III)

The above table 1 shows that the current assets of NSBL have exceeded current liabilities in average, in the study period from 2007/08 to 2011/12, except in 2008/09. The highest ratio is 1.34 in 2007/08 while the lowest ratio is 0.97 in the year 2008/09 with an average ratio of 1.158 during the study period. The ratio shows the fluctuating trend during the period. The coefficient of variation (C.V.) between the ratios for the study period is 10.85% which shows that the current ratios during the study period are somewhat consistent. In general, the bank is able to meet its short-term obligations.

Though the optimal standard of current ratio should be 2:1, the conventional measure of liquidity is not applicable in banking business. Banking business holds big portion of deposits as a core deposit (the minimum level of deposits which the commercial banks hold at all the times) and this deposits remains all the time throughout the years. This core deposit forms the fixed liability of the bank though it is current in nature. So the ratio maintained by the commercial banks at the level of around 1:1 can be regarded as good and sufficient to meet the normal contingencies. Therefore the above current ratio analysis of the bank over the five years period indicates that the bank has satisfactory liquidity position.

4.1.2 Cash and bank balance to total deposit ratio:

Cash and bank balance are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositors. This ratio is computed by dividing cash and bank balance by total deposits. (Detail in -IV). Both higher and lower ratios are not desirable. The reason is that if a bank maintains higher ratio of cash, it has to pay interest on deposits and some earnings may be lost. In contrast, if a bank maintains low ratio of cash, it may

fail to make payment for the demands of the depositors. So, sufficient and appropriate cash reserve should be maintained properly.

Table 2

Cash and bank balance to total deposit ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	5.19	3.92	7.62	7.87	8.36	6.59	1.73	26.21

(Source: Appendix-IV)

The above table 2 shows that the cash & bank balance to total deposit ratio of NSBL has fluctuating trend. The highest ratio is 8.36 % in 2011/12 and the lowest is 3.92 % in 2008/09. The mean of the ratios for the study period is 6.59 % and the C.V. between them is 26.21 %. On the basis of the C.V. it can be concluded that the ratios are variable and less consistent.

Though the ratios are not consistent, the cash & bank balance position of NSBL with respect to deposits is better to serve its customers deposit withdrawal demands. Commercial banks have to maintain its cash & bank balance in terms of total deposit as directed by NRB time to time. Otherwise they are imposed penalty. A high ratio of non-earning cash & bank balance may be unfit which indicates the banks inability to invest into short-term marketable security, treasury bills, etc ensuring enough liquidity which will help the bank to improve its profitability.

4.1.3 Cash and bank balance to current assets ratio:

This ratio shows the percentage of the banks most liquid fund over current assets of the bank. This ratio is computed by dividing cash and bank balance by current assets. (Detail in -V)

Table 3

Cash and bank balance to current assets ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	7.52%	10.46%	18.26%	17.93%	21.63%	15.16	5.28	34.82

(Source: Appendix-V)

The above table 3 shows that the cash & bank balance to current assets ratio of NSBL has fluctuating trend. The highest ratio is 21.63% in 2011/12 and the lowest is 7.52 % in 2007/08. The mean of the ratios for the study period is 15.16 % & the C.V. between them is 34.82 %. On the basis of C.V. the ratios are seemed to be variable and less consistent.

In conclusion it can be said that NSBL is in good position in terms of its cash & bank balance but it does not mean that it has mobilized its more funds in profitable sectors. It actually means that NSBL can meet its daily requirements to make the payments on customer deposit withdrawals.

4.1.4 Investment on government securities to current assets ratio:

This ratio examines the portion of a commercial banks current asset, which is invested on government securities. More or less, each commercial bank is interested to invest their collected fund on different securities issued by the government time to time to utilize their excess funds and/or for other purposes. Though government securities are not so liquid as cash & bank balance, they can easily be sold in the market or they can be easily converted into cash in other ways and they are risk free also. So these are additional source of liquidity for the bank to support cash and bank balance to meet unexpected liquidity needs on adverse situations. This ratio is calculated by dividing the amount invested on government securities by current ratio (detail in -VI).

Table 4

Investment on government securities to current assets ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	30.49	31.55	29.63	29.94	22.13	28.75	3.37	11.73

(Source: Appendix-VI)

The above table 4 shows that investment on government securities to current assets ratio of NSBL has up and down trend and from minimum of 22.13 % in 2011/12 to the maximum of 31.55 % in the year 2008/09. The mean of the ratios for the study period is 28.75 % and the C.V. between them is 11.73 %. On the basis of the C.V. it can be concluded that the ratios are less volatile and consistent.

4.2 Asset Management Ratios:

This ratio measures the efficiency of a commercial bank in its fund mobilization. A commercial bank must be able to manage its assets properly to earn high profit maintaining the appropriate level of liquidity. Asset management ratio measures the efficiency of the bank to manage its assets in profitable way satisfactorily. By the help of following ratios, asset management ability of Nepal SBI Bank Limited has been analyzed.

4.2.1 Loan & Advances to total deposit ratio:

This ratio measures the extent to which the bank is successful to mobilize its total deposit on loan and advances for the purpose of income generation. A high ratio indicates better mobilization of collected deposits and vice versa. But it should be noted that too high ratio might not be better from liquidity point of view. This ratio is calculated by dividing loans and advances by total deposits (detail in -VII).

Table 5

Loan & Advances to total deposit ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	88.32	54.12	50.09	50.37	49.01	58.40	15.06	25.78

(Source: Appendix-VII)

The above table 5 shows that loan & advances to total deposit ratio of the bank is 88.32 % in 2007/08 which is highest of the study period. It is decreased up to 49.01 % in 2011/12. Then it is increased to 54.12 % in the year 2008/09 and again decreased to 50.09 % in year 2009/10. So, it has increasing and decreasing trend. The mean of the ratios is 58.40 % with 25.78 % C.V. between them, which shows that the ratios are volatile and inconsistent over the study period.

This ratio is also called CD ratio i.e. Credit-Deposit ratio and around 70 % of CD ratio is taken as standard. From this point of view, the loan & advances to total deposit ratio of the bank is in somehow in Increasing and decreasing trend.

4.2.2 Total Investments to total deposit ratio:

A commercial bank may mobilize its deposit by investing in different securities issued by government and other financial or non-financial organized institutions. This ratio measures the extent to which banks are able to mobilize their deposits on investment in various securities. In the process of portfolio management of bank assets, various factors such as excess availability of fund, liquidity requirement, central banks norms, etc, are to be considered in general.

This ratio indicates the proportion of deposits utilized for the purpose of income generation as well as for maintaining liquidity in appropriate level. A high ratio is the indicator of high success to mobilize deposits in securities and vice versa. This ratio is calculated by dividing total investment by total deposit (detail in no.VIII).

Table 6

Total investment to total deposit ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	22.52	47.52	46.73	44.59	45.87	41.45	9.33	22.50

(Source: Appendix-VIII)

The above table 6 shows that total investment to total deposit ratios of NSBL are in increasing and decreasing trend during the study period. The highest ratio is 47.52 % in 2008/09 and lowest is 22.52 % in 2007/08 with mean ratio of 41.45 %. The C.V. of 22.50 % between them shows that the ratios are less consistent and more variable.

In the later period of the study, the bank is increasing its mobilization of resources on investment. It may be due to the slack in the different sectors of the economy due to which banks are unable to mobilize its fund in loan and advances. It can be justified by comparing CD ratios and investment to total deposit ratios. When CD ratios are in decreasing trend, investment to total deposit ratios are in increasing trend.

4.2.3 Loan and Advances to total working fund ratio:

Loan and advances of any commercial bank represent the major portion in the volume of total working fund. This ratio measures the volume of loans and advances in the structure of total assets. The high degree of this ratio indicates the good performance of the bank in mobilizing its funds by way of lending function. However, in its reverse side, the high degree of this ratio is representative of low liquidity ratio either. Granting the loans and advances always carries a certain degree of risk. Thus this asset of banking business is regarded as risky assets. This ratio measures the management attitude toward risk assets. The low ratio is indicative of low productivity and high degree of safety in liquidity and vice versa. The interaction between risk and return determines this ratio. This ratio also shows the credit risk taken by the bank towards mobilizing its funds into different types of assets. This ratio reflects the extent to which the banks are successful in mobilizing their total assets on loans and advances for the purpose of income generation. This ratio is computed by dividing loan and advances by total working fund i.e. total assets (detail in no.IX).

Table 7

Loans & Advances to total working fund ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	70.48	50.16	45.94	46.36	45.03	51.65	9.60	18.59

(Source: Appendix-IX)

Table 7 shows that the ratio ranges from the minimum of 45.03% in 2011/12 to the maximum of 70.48% in 2007/08. The mean of the ratio is 51.65 % and the C.V. between them is 18.59 %, which shows the ratios are volatile and inconsistent over the study period.

4.2.4 Investment on government securities to total working fund ratio:

This ratio measures the contribution made by investment on government securities in total working fund of the bank. Besides mobilizing its major portion of funds in the form of loans and advances, banks invests their funds in purchasing different types government securities. They do so mainly to utilize the excess funds for income generation without taking more risk and to maintain the adequate level of liquidity since these securities are more liquid assets than loans and advances. A high ratio indicates better mobilization of fund as investments on government securities and vice versa. This ratio is calculated by dividing investment on government securities by total working fund (detail in no.X).

Table 8

Investment on government securities to total working fund ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	16.81	10.96	11.34	11.66	7.86	11.72	2.88	24.59

(Source: Appendix-X)

Table 8 explains that the ratio has slightly increased and decreased. The ratio has an similar trend in the study period. The mean of the ratio is found to be 11.727 % with 24.59 % C.V. between them, which indicates that the ratio is highly variable and less consistent over the study period.

4.2.5 Investment on shares & debentures to total working fund ratio:

This ratio measures the contribution made by investment on shares and debentures government securities in total working fund of the bank. Nowadays, commercial banks invest its fund not only on government securities, but also invest on the shares and debenture of other different types of companies. A high ratio indicates better mobilization of fund as investments on shares & debentures and vice versa. This ratio is calculated by dividing investment on shares & debentures by total working fund (detail in no.XI).

Table 9

Investment on shares & debentures to total working fund ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	0.12	0.11	0.10	0.09	0.05	0.094	0.024	25.70

(Source: Appendix-XI)

Table 9 explains that the ratio has decreased from 0.12% in 2007/08 to 0.05% in 2011/12. The ratios have a decreasing trend in the study period. The mean of the ratio is found to be 0.094 % with 25.70 % C.V. between them, which indicates that the ratio is variable and some what inconsistent over the study period.

4.2.6 Total outside assets to total deposits ratio:

Loan & Advances and investment comprises the total outside assets of a bank. They are the major area of fund mobilization of commercial banks for income generation. Loans & advances is the first type of application of funds, which has more risk as comparable to investment and gives more returns. Investment is cushion against the liquidity risk and at the same time it gives return. The investing activity of banks has low level of risk and low level of return. Loans & Advances and investment to total deposits ratio indicates the firms fund mobilizing power in gross. The main source of banks fund is its deposits. Thus, this ratio measures how well the deposits liabilities have been mobilized by the bank in income generation. This ratio is computed by dividing total loan and advances and investment by total deposits (details in no.XII).

Table 10

Total outside assets to total deposits ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	110.84	101.65	96.82	94.96	94.88	99.80	6.03	6.04

(Source: Appendix-XII)

Table 10 shows total outside assets to total deposits ratio of the bank is consistent over the study period, except for the year 2007/08 & 2008/09. The maximum ratio is 110.84 % in 2007/08 and minimum ratio is 94.88 % in the year 2011/12. The mean of the ratios is 99.80 % and C.V. between them is 6.04 %. On the basis of C.V. it can be concluded that the ratios are satisfactorily consistent during the study period.

4.2.7 Loan & advances to total outside assets ratio:

Loans and advances and investments made by the bank comprise the total outside asset of a commercial bank. This is the portion of assets employed by the bank for the purpose of income generation. This ratio measures the contribution made by loans & advances in total amount of loans and advances and investments. The proportion between investment and loans and advances measures the management's attitude towards more risky assets and lower risky assets. Loans & Advances are more risky and also generate more returns in comparison to investments. The total mobilized fund i.e., loans and advances and investments in whole don't provide the quality of assets that a bank has created. Thus this ratio measures the risk of the banking business also. The high ratio indicates the mobilization of funds in more risky area and vice versa. This ratio is computed by dividing Loan & Advances by total outside Assets (detail in no.XIII).

Table 11

Loan & advances to total outside assets ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	79.68	53.25	51.74	53.05	51.66	57.88	10.92	18.87

(Source: Appendix-XIII)

Table 11 shows that loan & advance to total outside assets ratio ranges from the minimum 51.66 % in 2011/12 to the maximum of 79.68 % in 2007/08. The mean of the ratios is 57.88 % and the C.V. between them is 18.87 %, which shows that the ratios are inconsistent over the study period with decreasing trend.

4.2.8 Investment on government securities to total outside assets ratio:

This ratio measures the proportion of the banks investment in risky area and risk free areas. Total outside asset contains loans & advances and investments. This is the portion of total assets engaged in income generation. Loan and advances are major income generating assets of the bank. But there is high risk in advancing loan and advances. Investment activity involves the purchasing of securities issued by government and other institutions and purchasing of shares and debentures issued by other organized institutions. Though investment activities are safer than the loan and advances from risk point of view, their rate of return is lower than the return from loan and advances. From the risk point of view, investment activities are classified into two categories, investment on government securities and others. Investment on government securities is considered as risk free investment and other investments are considered as risky one. Thus this ratio measures the amount of risk free investment made by the bank while mobilizing its funds. This ratio is computed by dividing investment on government securities by total outside assets (detail in no.XIV). This ratio measures the risk of the banking business also. This also reflects the management's attitude towards risky assets and risk free assets. The high ratio indicates the mobilization of funds in safer area and vice versa. The high ratio also indicates the lower rate of return and vice versa. However, safety doesn't provide with satisfactory return. So, a compromising ratio between risk and profit should be maintained.

Table 12

Investment on government securities to total outside assets ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	19	11.63	12.77	13.34	9.01	13.15	3.28	24.95

(Source: Appendix-XIV)

Table 12 shows that the bank has invested minimum fund on government securities for the year 2011/12 and the ratio is 9.01 % for this year. Highest ratio is 19 % in 2007/08. The mean of the ratios is 13.15 % and C.V. between them is 24.95 %, which shows that the ratios are volatile and less consistent with increasing trend.

4.2.9 Total outside assets to total assets ratio:

Loans & Advances and investments are the outside assets of commercial banks. These are the proportion of assets employed by the bank for the purpose of income generation. This ratio shows the ability of the bank to utilize its funds into income generating assets. A high ratio indicates better mobilization of funds in the form of income generating assets and vice versa. This ratio is calculated by dividing total outside assets by total assets (detail in no.XV).

Table 13

Total outside assets to total assets ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	88.45	94.20	88.80	87.39	87.16	79.2	10.32	13.03

(Source: Appendix-XV)

Table 13 explains that the ratios are ups and down. The ratios are in increasing trend. The mean of the ratio is found to be 79.2% with 13.03 % C.V. between them, which indicates that the ratios are consistent and less variable during the study period.

4.2.10 Total Off-Balance sheet operation to Loan & Advances ratio:

This ratio shows the proportion of fee-based off-balance sheet activities to fund based loan and advances of the bank. Now a day fee-based off-balance sheet activity plays an important role for the better performance of a bank. These fee based activities are very much dependent on mode of operation, management strategy, banking network with foreign banks, etc. A commercial bank should not concentrate only on fund-based activities such as loan and advances, investment on different sectors and so on. But it should pay its attention to increase fee-based off-balance sheet activities. Income generated through the fee-based off-balance sheet activities constitutes a significant proportion in the total income of most of the commercial bank's income

statement. A high ratio indicates the higher OBS transaction and vice versa. This ratio is computed by dividing total OBS transaction by total loan and advances (detail in no.XVI).

Table 14

Total Off-Balance sheet operation to Loan & Advances ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	20.79	18.03	18.04	18.82	20.09	19.15	1.110	5.80

(Source: Appendix-XVI)

Table 14 explains that the ratios are ranged from 20.79 % in 2007/08 to 18.03 % in 2008/09. The ratios are in fluctuating trend. The mean of the ratios is found to be 19.15 % with 5.80 % C.V. between them, which indicates that the ratios are consistent during the study period and has shown fluctuating trend.

4.3 Activity or Performing Ratios:

In this section, the lending efficiency in terms of quality and turnover is measured. Here different ratios are used to analyze the lending efficiency of the bank. For this purpose the relationship of different variables of balance sheet and profit and loss account have been established. The following ratios are analyzed for this purpose.

4.3.1 Loan loss provision to total loans and advances ratio:

The ratio of loan loss provision to total loans and advances describes the quality of assets that a bank is holding. Nepal Rastra Bank has directed the commercial banks to classify its loans & advances into the category of pass, restructured, sub-standard, and doubtful and loss to make the provision of 1, 15, 25, 50 & 100 percentages respectively. Nepal Rastra Bank has classified the pass loan as performing loans and other four types of loans as non-performing loans. This volume of non-performing loan is called Non Performing Asset (NPA) of the commercial bank. Loan loss provision set aside for performing loans is defined as General Loan Loss Provision and loan loss provision set aside for non-performing loan is defined as Specific Loan Loss Provision. The provision for loan loss reflects the increasing probability of non-performing loans in the volume of total loans and advances. Loan loss provision on

the other hand signifies the cushion against future contingency created by the default of the borrowers. The low ratio signifies the good quality of assets in the total volume of loans and advances. The high ratio signifies the relatively more risky assets in the volume of loans and advances. The loan loss ratio shows how efficiently the bank manages its loans and advances and makes effort for timely recovery of loans. This ratio is calculated by dividing the loan loss provision by total loans and advances (detail in no.XVII).

Table 15

Loan loss provision to total Loans & Advances ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	0.47	1.01	1.72	0.61	1.23	1.01	.45	44.37

(Source: Appendix-XVII)

The above table 15 exhibits that the ratios for the study period has fluctuating trend. The ratio ranges from 1.23% % in 2011/12 to 0.47 % in 2007/08 with an average of 1.01 %. The C.V. between them is 44.37 %, which indicates that the ratios are more variable and inconsistent with the increasing trend.

4.3.2 Non-Performing loans to total loans and advances ratio:

This ratio measures the proportion of non-performing loans on the total volume of loans and advances. This reflects the quantity of quality assets that the bank have. Higher ratio reflects the bad performance of the bank in mobilizing loans and advances and bad recovery rate and vice versa. This ratio is computed by dividing the non-performing loans by total loans and advances (detail in no.XVIII).

Table 16

Non-performing loans to total loans & Advances ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	4.03	2.09	2.82	1.12	0.55	2.12	1.23	58.2

(Source: Appendix-XVIII)

The above table 16 exhibits that the ratios for the study period are decreasing over the years. The ratio ranges from 0.55 % in 2011/12 to 4.03 % in 2007/08 with an average of 2.12%. The C.V. between them is 58.2 %, which indicates that the ratios are variable.

The data of non-performing loan for the year study period shows that the bank has lower amount of bad loans. So, it can be concluded that the bank has mobilized its fund on good sectors.

The non-performing assets for commercial banks should be in single digit i.e. less than 10% as per international standard. The mean NPA level of NSBL is 2.12 %, which is fit the standard level.

4.4 Loans & Advances Portfolio:

(Analyzing the Portfolio behavior of Loans & Advances)

In this chapter, we examine the portfolio management of loans and advances. Bank advances loan to various sector of economy and to various types of borrowers. Similarly, it invests fund in various types of securities and shares. In this chapter, to analyze the portfolio behavior of loans and advances of the bank for the study period, the ratios of loans & advances granted to various sectors of economy and for various purposes to total volume of loans and advances have been measured.

4.4.1 Priority sector lending to total loans & advances ratio:

This ratio measures the contribution of banks lending in priority sector. Priority sector lending is also called directive credit. Nepal Rastra Bank has regulated the commercial banks to provide credit to the priority sector from their total lending portfolio. In the course of non-compliance, the commercial banks are compelled to pay for penalty. Under the priority sector, credit to agriculture and agro based business, cottage and small industries, service sector and other business are included. Credit to the deprived sector is also a part of priority sector lending. But now NRB has decided to deregulate the priority sector lending on phase wise basis. This ratio is calculated by dividing priority sector lending by total loans and advances (detail in no.XIX).

Table 17

Priority sector loans to total loans & Advances ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	18.85	17.84	20.09	13.38	9.76	15.98	3.95	24.07

(Source: Appendix-XIX)

The above table 17 shows that the ratios are ranged from 9.76 % in 2011/12 to 20.03% in 2009/10. The mean of the ratios is found to be 15.98 % with 24.07% C.V. between them, which indicates that the ratios are almost consistent over the study period.

4.4.2 Sector wise loan and advances classifications:

Here, the total loans and advances disbursed to different sectors of the economy is calculated. Commercial banks should have to diversify its loans and advances to different sectors. They cannot pour all of its productive assets into a single sector, which eventually increases the risk factor. Total economy has been classified into five sectors as under.

-) Agricultural Sector
-) Industrial/ Production Sector
-) Trading/ Commercial Sector
-) Service Sector
-) Others: Include miscellaneous credit to Staffs, Loan against Fixed Deposit Receipt, Loan against the security of shares and debentures, personal loans, consumer loans etc.

This ratio is computed by dividing sector wise loan and advances by total loan and advances (detail in no.XX).

Table 18

Sector wise loan and advances of Nepal SBI Bank Limited

{Loans and advances disbursed to different purposes sectors of the economy
(In %)}

Sectors	F.Y.					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
Agricultural	0.02	0.91	0.27	0.39	0.40	0.40	0.3255	81.40
Industry/ Production	50.03	46.28	49.84	54.89	54.31	51.07	3.5566	6.96
Trading/ Commercial	23.69	27.56	18.32	17.25	18.88	21.14	4.3539	20.60
Service	5.83	14.02	13.84	15.67	18.23	13.52	4.6439	34.35
Others	20.43	11.23	17.72	11.80	8.17	13.87	5.0399	36.34
Total	100	100	100	100	100	100	-	-

(Source: Appendix-XX)

The above table 18 explains NSBL's diversification of lending in different sectors. NSBL has mostly used its funds in production sector. In average, lending in industrial, commercial, others, service and agricultural sector take the first, second, third, fourth and fifth place with mean percentage of 51.07 %, 21.41 %, 13.87%, 13.52 %, and 0.40 % respectively in the lending portfolio of the bank. The lending in the agricultural sector is very nominal comparing to others. The ratios are fluctuating over the study period ranging from minimum of 0.02% in 2007/08 to maximum of 0.91% in 2008/09. The mean of the ratios is 0.4% with 81.40% C.V. between them, which suggests that the ratios are highly volatile and less consistent.

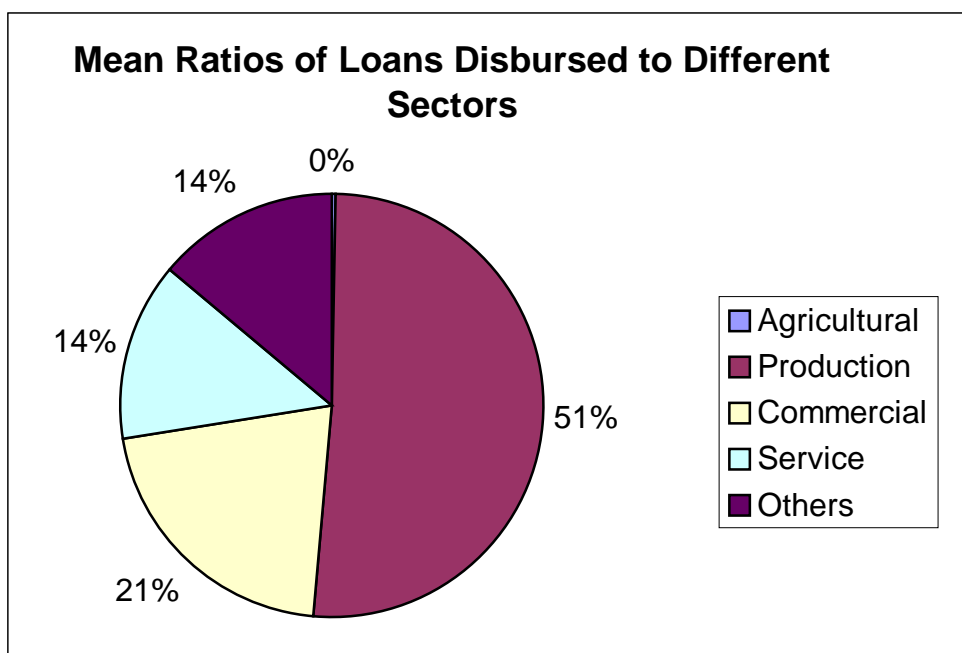


Figure 1: Mean Ratios of Loans disbursed to Different Sectors of NSBL.

The lending in industrial sector is in more consistent than others. Bank has invested half of its fund to production sector. The ratios are in fluctuating trend and ranges from 54.89% in 2010/11 to 46.28% in 2008/09. The average ratio is 51.07% with C.V. 6.96% between the ratios over the study period. It signifies that the ratios are consistent and less variable. The lending in commercial sector shows the overall decreasing trend with the ratios ranging from the minimum 17.25% in 2010/11 to the maximum 27.56% in 2008/09. The mean ratio is 21.14% and the C.V. between the ratios is 20.60%, which shows the ratios are less consistent over the study period. The lending in service sector shows overall increasing trend over the study period. The ratio ranges from the minimum 5.83% in 2007/08 to the maximum of 18.23% in 2011/12 and the C.V. 34.35% shows the ratios are variable and not consistent during the study period. The mean of the ratios is 13.52%. The lending to the other sectors shows the decreasing trend with the fluctuations between them. The ratios range from the minimum of 8.17% in 2011/12 to the maximum of 20.43% in 2007/08. The mean ratio is 13.87%. The C.V. of 36.34% shows the ratios are less consistent and more variable over the study period.

4.5 Profitability ratios:

The main objective of a commercial bank is to earn profit by providing different types of banking services to its customers. No bank can survive without profit. Profit is the indicator of efficient operation of a bank. Profitability ratios are the best indicators of overall efficiency. Higher profitability ratio shows the higher efficiency of a bank and vice versa. Through the following ratios, effort has been made to measure the profit earning capacity of Nepal SBI Bank Ltd.

4.5.1 Interest income to total income ratio:

This ratio measures the volume of interest income in total income of the bank. This ratio helps to measure the banks performance on how well they are mobilizing their fund for the purpose of income generation. This ratio also helps to measure the banks performance on other fee-based activities, since after investing functions fee based activities are the major source of banks income generation. The high ratio indicates the high contribution made by the lending and investing activities and vice versa. This ratio can be computed by dividing interest income to total income (detail in no.XXI).

Table 19

Interest income to total income ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	88.80	88.33	89	88.25	88.32	88.54	0.30	0.33

(Source: Appendix-XXI)

The above table 19 shows the ratios are highly satisfactory consistent over the study period The mean of the ratios is 88.54 % and the C.V. between them is 0.33 %, which shows the highly satisfactory of the ratios over the study period.

These ratios suggest that the large proportion of the income is generated from mobilizing the fund to loan and advances and investment activities.

4.5.2 Total interest earned to total outside assets ratio:

The main assets of a commercial bank are its outside assets in the form of loans and advances and investments employed for income generation purpose. This ratio reflects the extent to which the banks are successful to earn interest as major income

from the outside assets. A high ratio indicates high earning power of total outside assets and vice versa. This ratio is computed by dividing total interest income by total outside assets (detail in no.XXII).

Table 20

Total interest earned to total outside assets ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	6.38	5.14	6.72	7.71	7.45	6.68	0.90	13.53

(Source: Appendix-XXII)

The above table 20 explains that the ratios are fluctuating over the period ranging from 6.38% in 2007/08 to 7.45% in 2011/12. The mean of the ratio is found to be 6.68% with 13.53% C.V. between them, which indicates that the ratios are satisfactorily consistent during the study period.

4.5.3 Interest expenses to total expenses ratio:

This ratio measures the portion of total interest expenses in the volume of total expenses. The high ratio indicates the low operational expenses and vice versa. Interpreting in other way the high ratio can be due to the costly sources of funds. This ratio is computed by dividing interest expenses by total expenses (detail in no.XXIII).

Table 21

Interest expenses to total expenses ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	66.69	70.49	75.28	75.40	78.80	73.33	4.24	5.40

(Source: Appendix-XXIII)

Table 21 shows the ratios are in increasing trend ranging from 66.69 % in 2007/08 to 78.80 % in 2011/12. The mean of the ratios is 73.33 % with 5.40 % C.V., which shows the ratios are satisfactorily consistent over the study period.

4.5.4 Total interest earned to total working fund ratio:

This ratio reflects the extent to which the bank is successful in mobilizing its total assets to generate high income as interest. A high ratio is an indicator of high earning power of the banks total assets and vice versa. This ratio is calculated by dividing total interest income by total assets (detail in no.XXIV).

Table 22

Total interest earned to total working fund ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	5.65	4.84	5.97	6.74	6.49	5.94	0.67	11.26

(Source: -XXIV)

The above table 22 shows that the ratios are ranging between 4.84% in 2008/09 to 6.49% in 2011/12. The mean of the ratios is found to be 5.94% with 11.26% C.V. between them, which indicates that the ratios are consistent over the study period.

4.5.5 Total interest paid to total working fund ratio:

This ratio measures the percentage of total interest expenses against total working fund. A high ratio indicates higher interest expenses on total working fund and vice versa. This ratio is calculated by dividing total interest expenses by total working fund (detail in no.XXV).

Table 23

Total interest paid to total working fund ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	2.65	2.73	3.79	4.55	4.77	3.70	0.62	16.60

(Source: -XXV)

Table 23 explains that the ratios are fluctuating over the years. The ratio ranges between 2.65% in 2007/08 to 4.77% in 2011/12. The mean of the ratios is found to be 3.70% with 16.60% C.V. between them, which means the ratios are a bit variable over the period.

4.5.6 Total income to total expenses ratio:

The comparison between total expenses and total income measures the productivity of expenses in generating income. The amount of income that a unit of expenses generates is measured by the ratio of total income to total expenses. The high ratio is indicative of higher productivity of expenses and vice versa. This ratio is calculated by dividing total income by total expenses (detail in no.XXVI).

Table 24

Total income to total expenses ratio (Times)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	1.60	1.41	1.33	1.27	1.21	1.36	0.0003	0.024

(Source: Appendix-XXVI)

Table 24 explains that the ratios are consistent during the study period ranging from the minimum 1.21 % in 2011/12 and 1.60 in year 2007/08. The mean of the ratios is found to be 1.36 times with 0.024% C.V., which shows that the ratios are consistent during the study period.

4.5.7 Total income to total working fund ratio:

This ratio measures how efficiently the asset of a business is utilized to generate income. It also measures the quality of assets in income generation.

This ratio is calculated by dividing total income by total assets (detail in no.XXVII).

Table 25

Total income to total working fund ratios (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	6.36	5.48	6.70	7.63	7.35	6.70	0.76	11.34

(Source: Appendix-XXVII)

The above table 25 explains that the ratios are in fluctuating trend for the study period ranging from the minimum 5.48 % in 2008/09 to the maximum 7.63 % in 2010/11. The mean of the ratios is found to be 6.70% with 11.34% C.V. between them, which indicates that the ratios over the study period are consistent.

4.5.8 Return on loan and advances ratio:

Return on loan & advances ratio measures the earning capacity of a commercial bank through its mobilized funds in the form of loans and advances. A high ratio indicates greater success to mobilize fund as loans & advances and vice versa. This ratio is calculated by dividing net profit by loan and advances (detail in no.XXVIII). Table 27 shows the return on loan and advances ratios of NSBL for the study period.

Table 26

Return on loan & advances ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	2.05	2.09	2.24	2.17	1.84	2.07	0.14	6.58

(Source: Appendix-XXVIII)

Table 26 explains that the ratios are fluctuating with overall increasing trend ranging between 1.84% in 2011/12 to 2.24% in 2009/10. The mean of the ratios is found to be 2.07% with 6.58% C.V. between them, which indicates that the ratios less variable during the period of study.

4.5.9 Return on working fund ratio (ROA):

Return is the result of investment and it measures the profit earning capacity of the investable resources into different types of assets. Total working fund of a bank means its total assets. If the banks total working fund is well managed and efficiently utilized, return on such assets will be higher and vice versa. This ratio is calculated by dividing net profit by total working fund (detail in no.XXIX). The following table 28 shows the profitability position of NSBL with respect to total assets for the study period.

Table 27

Return on total working fund ratio (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	1.44	1.05	1.03	1.01	0.83	1.07	0.20	18.69

(Source: -XXIX)

Table 27 explains that the ratios are fluctuating during the study period with overall increasing trend. The ratio ranges between 1.44 in 2007/08 to 0.83% in 2011/12. The mean of the ratios is found to be 1.07% with 18.69% C.V. between them, which indicates that the ratios are variable and a bit consistent during the study period.

4.5.10 Return on Equity (ROE):

This ratio measures the amount profit that a rupee of shareholders fund has generated. The high ratio is indicative of high return to shareholders equity and vice versa. This ratio is calculated by dividing net profit by total shareholders fund (detail in no.XXX).

Table 28
Return on equity (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	17.52	18.47	15.99	16.13	15.02	16.60	1.21	7.34

(Source: -XXX)

The above table 28 shows that the ratios are fluctuating during the study period with increasing and decreasing trend. The ratio ranges between 17.52% in 2007/08 to 15.02% in 2011/12 with the mean ratio of 16.60%. C.V. between them is 7.34 %, which shows that the ratios are uniform and consistent during the study period.

4.5.11 Earning Per Share (EPS):

EPS refers to net profit divided by total number of shares outstanding. The amount of EPS measures the efficiency of a firm in relative terms. The figure is the indicative of the overall good or bad performance of an organization. How far an organization is able to use its resources to generate profit is determined by the profit it has earned. This ratio is computed by dividing total net profit by total number of shares (detail in no.XXXI).

Table 29
Earning per share (in Rs.)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	28.35	36.20	23.70	24.86	22.94	27.21	4.86	17.86

(Source: -XXXI)

Table 29 shows that EPS are fluctuating over the years. It ranges between Rs22.94 in 2011/12 to Rs.36.20 in 2008/09. The mean EPS during the study period is found to be Rs.27.21 with 17.86% C.V. between them, which shows that the earning is less variable and a bit consistent over the period of study.

4.5.12 Net Interest Margin:

Net interest margin in general term is the difference between the interests received from investment on loan and advances and interest paid on deposits collected by the bank. In other words this is the gross income in percentage from the intermediation cost of any bank. It shows the bank's efficiency to earn high profit to meet various costs i.e. office expenses, staff expenses etc and to provide attractive return to the shareholders. Generally, net interest margin of 4% and above is considered better. This ratio is computed by dividing the difference between interest revenues from earning assets less interest costs on borrowed funds by total earning assets (detail in no.XXXII).

Table 30
Net Interest Margin (%)

Bank	FY					Mean	S.D.	C.V. (%)
	2007/08	2008/09	2009/10	2010/11	2011/12			
NSBL	3.93	4.20	4.73	4.72	3.82	4.28	0.38	8.96

(Source: Appendix-XXXII)

Table 30 shows that Net Interest Margin ratios are fluctuating in ups and down trend over the years in the study period. It ranges between 3.82% in 2011/12 to 4.72% in 2010/11. The mean NIM during the study period is found to be 4.28% with 8.96% C.V. between them, which shows that the net interest margin is less variable over the period of study.

4.6 Growth Ratios

To examine and analyze the expansion and growth of the banking business, following growth ratios are calculated in this part of the study. The higher ratios represent the better performance of the bank. Growth ratios are directly related to the fund mobilization and investments decision of the bank. This ratio represents how well the

commercial banks are maintaining their economic and financial position. These ratios can be calculated by dividing the difference of last period figure and the first period by the first year figure (detail in no.XXXIII). Under these topic four types of growth ratios namely growth ratios of total deposits, Loan and advances, total investments, and net profit of Nepal SBI Bank Ltd. for the study period have been analyzed.

Table 31

Growth ratio of total deposits (Rs. In Million)

Bank	FY					Growth Ratio (%)
	2007/08	2008/09	2009/10	2010/11	2011/12	
NSBL	13715.39	27957.22	34896.43	42415.44	53337.26	388

(Source: Appendix-XXXIII)

Table 32

Growth ratio of total loan & advances (Rs. In Million)

Bank	FY					Growth Ratio (%)
	2007/08	2008/09	2009/10	2010/11	2011/12	
NSBL	12111.69	15131.74	17480.54	21365.77	26142.09	99

(Source: Appendix-XXXIII)

Table 33

Growth ratio of total investments (Rs. In Million)

Bank	FY					Growth Ratio (%)
	2007/08	2008/09	2009/10	2010/11	2011/12	
NSBL	3088.88	13286.18	16305.63	18911.02	24463.45	691

(Source: Appendix-XXXIII)

Table 34

Growth Ratio of Net Profit (Rs. In Million)

Bank	FY					Growth Ratio (%)
	2007/08	2008/09	2009/10	2010/11	2011/12	
NSBL	247.77	316.37	391.74	464.56	480.10	93

(Source: Appendix-XXXIII)

The above table 31 to 34 explains the growth ratios of total deposits, total loan & advances, total investments, and net profit of Nepal SBI Bank Limited during the study period. The analysis shows that total deposit of the bank is in increasing trend with the net growth rate of 388.00% during the study period. Similarly loan and advances of the bank is in also increasing trend with the net growth rate of 99.00% during the study period. The analysis shows that the total investments of the bank is in increasing trend over the years having net growth rate of 691.00% during the study period. The net profit of the bank is also in increasing trend with fluctuations over the years with the net growth rate of 93.00% during the study period.

4.7 Measuring Correlation Between Different Variables:

4.7.1 Correlation between Deposits and Loans and Advances:

The correlation between total deposits and loans and advances describes the degree of relationship between these two items. How a unit increases in deposits impact in the volume of loans and advances is measured by this correlation. Here, deposit is the independent variable and the loans and advances is the dependent variable (detail in no.XXXIV).

Table 35

Correlation between deposits and loans & advances

Correlation Coefficient (r)	P.E(r).	6* P.E(r).	Remarks
0.77	0.1227	0.736	r > 6*P.Er.

(Source: Appendix-XXXIV)

The above table 35 shows that the correlation coefficient (**r**) between deposits and loans & advances of the bank is 0.77 and probable error multiplied by six is found to be 0.736. Since $r > 6*P.Er.$, and **r** is positive and nearby 1, it can be inferred that there is very strong positive correlation between deposits and loans & advances during study period.

4.7.2 Correlation between total deposits and total investment:

The correlation between total deposits and total investment describes the degree of relationship between these two items. How a unit increases in deposits impact in the

volume of investment is measured by this correlation. Here, deposit is the independent variable and the investment is the dependent variable (detail in no.XXXV).

Table 36

Correlation between deposits and investment

Correlation Coefficient (r)	P.Er.	6* P.Er.	Remarks
0.98	0.008	0.048	$r > 6*P.Er.$

(Source: -XXXV)

The above table 36 shows that the correlation coefficient (r) between total deposits and total investment of the bank is 0.98 and probable error multiplied by six is found to be 0.048. Since $r > 6*P.Er.$, it is significant and there is positive correlation between total deposit and total investments during study period in Nepal SBI Bank Limited.

4.7.3 Correlation between total loan and advances and total net profit:

The correlation between total loan and advances and total net profit measures the degree of relationship between these two variables. The value of (r) explains whether a percentage change in loans and advances contribute to increase the same percentage of net profit. Loans and advances is independent variable and total net profit is dependent variables (detail in no.XXXVI).

Table 37

Correlation between loans & advances and total net profit

Correlation Coefficient (r)	P.E(r).	6* P.E(r)	Remarks
0.95	0.028	0.168	$r > 6*P.Er.$

(Source: -XXXVI)

The above table 37 shows that the correlation coefficient (r) between loans & advances and total net profit of the bank is 0.95 i.e. positive and probable error multiplied by six is found to be 0.168. Since $r > 6*P.Er.$, the relation is significant. That is the increase or decrease of total loan and advances affects to total net profit in Nepal SBI Bank Limited.

4.7.4 Correlation between total investment and total net profit:

The correlation between total investment and total net profit measures the degree of relationship between these two variables. The value of (r) explains whether a

percentage changes in investment contribute to increase the same percentage of net profit. Investment is independent variable and total net profit is dependent variables (detail in no.XXXVII).

Table 38

Correlation between investment and total net profit

Correlation Coefficient (r)	P.E(r)	6* P.E(r)	Remarks
0.95	0.028	0.165	$r > 6*P.Er.$

(Source: Appendix-XXXVII)

The above table 38 shows that the correlation coefficient (r) between total investment and total net profit of the bank is 0.95 i.e. positive and probable error multiplied by six is found to be 0.165. Since $r > 6*P.Er.$, it is significant and there is correlation between total investment and total net profit in Nepal SBI Bank Limited.

4.8 Trend Analysis and Projection for Next Five Years:

The objective of this topic is to analyze trend of deposit collection, its utilization and net profit of Nepal SBI Bank Limited. Under this topic trend of deposit, total loan and advances and total net profit are forecasted for next five years.

4.8.1 Trend analysis of total deposit:

Table 39

Trend value of total deposit (Rs.Million)

Years	Trend Value
2008	15727.66
2009	25094.15
2010	34464.34
2011	43834.53
2012	53204.72
2013	62574.91
2014	71945.1
2015	81315.29
2016	90685.48
2017	100055.67

(Source: Appendix-XXXVIII) Here, an effort has been made to analyze the trend values of total deposit of NSBL from 2008 to 2012 and forecasted for next 5 years till 2017. The following table 39 shows the trend values of NSBL for 10 years from 2008 to 2017 (detail in -XXXVIII)

From the above table 39, it is clear that the total deposit of NSBL is in increasing trend. Other things remaining the same, total deposit of NSBL in 2017 will be Rs. 100055.67 million, which is the highest under the study period.

4.8.2 Trend analysis of total loan and advances:

Here, the trend values of total loan and advances from 2008 to 2012 is calculated and forecasted for next 5 years till 2017. The following table 40 shows the trend values of total loan and advances of NSBL for 10 years from 2008 to 2017 (detail in -XXXIX)

Table 40

Trend value of loan and advances (Rs.Million)

Years	Trend Value
2008	11588.54
2009	15017.62
2010	18446.7
2011	21875.78
2012	25304.86
2013	28733.94
2014	32163.02
2015	35592.1
2016	39021.18
2017	42450.26

(Source: Appendix-XXXIX)

From the above table 40, it is seen that the total loan and advances of NSBL is in increasing trend. Other things remaining the same, total loan and advances of NSBL in 2017 will be Rs. 42450.26 million, which is the highest under the study period.

4.8.3 Trend analysis of total investment:

Here, an attempt has been made to analyze the trend values of total investment of NSBL for 5 years from 2008 to 2012 and forecasted the same for next 5 years till 2017. The following table 41 shows the trend values of total investment of NSBL for 10 years from 2008 to 2017 (detail in -XXXX)

Table 41

Trend value of total investment (Rs.Million)

Years	Trend Value
2008	5536.23
2009	10373.63
2010	15211.03
2011	20048.43
2012	24885.43
2013	29723.23
2014	34560.63
2015	39398.03
2016	44235.43
2017	49072.83

(Source: Appendix-XXXX)

From the above table 41, it is clear that the total investment of NSBL is in increasing trend. Other things remaining the same, total investment of the bank in 2017 will be Rs. 49072.83 million, which is the highest under the study period.

4.8.4 Trend analysis of total net profit:

Here, an attempt has been made to analyze the trend values of total net profit of NSBL for 5 years from 2008 to 2012 and forecasted the same for next 5 years till 2017. The following table 42 shows the trend values of total net profit of NSBL for 10 years from 2008 to 2017 (detail in -XXXXI)

Table 42

Trend value of total net profit (Rs. Million)

Years	Trend Value
2008	257.54
2009	318.82
2010	380.10
2011	441.38
2012	502.66
2013	563.94
2014	625.22
2015	686.5
2016	747.78
2017	809.06

(Source: Appendix-XXXXI)

From the above table 42, it is clear that the net profit of NSBL is in increasing trend. Other things remaining the same, net profit of the bank in 2017 will be Rs. 809.06 million, which is the highest under the study period.

Figure 2: Trend Values of Total Deposit of NSBL

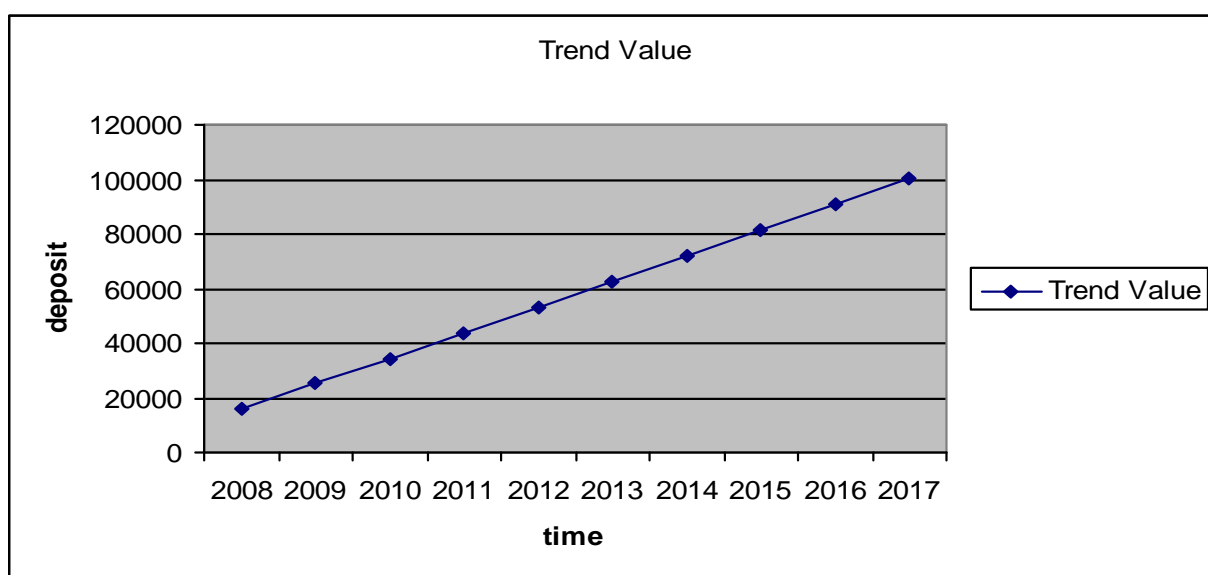


Figure 3: Trend Values of Total Loans and Advances of NSBL

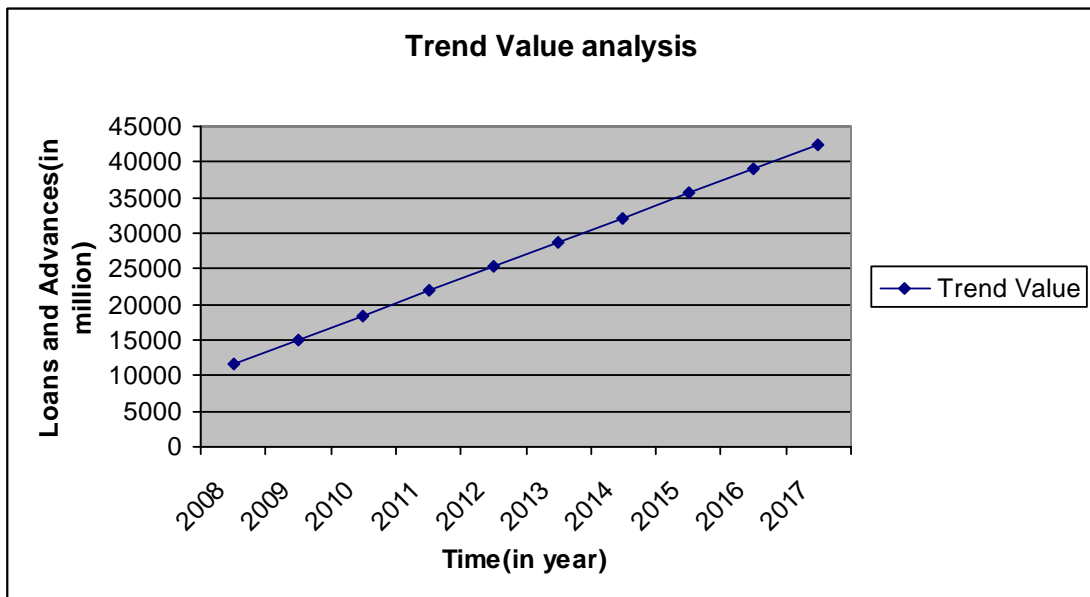


Figure 4: Trend Values of Total Investment of NSBL

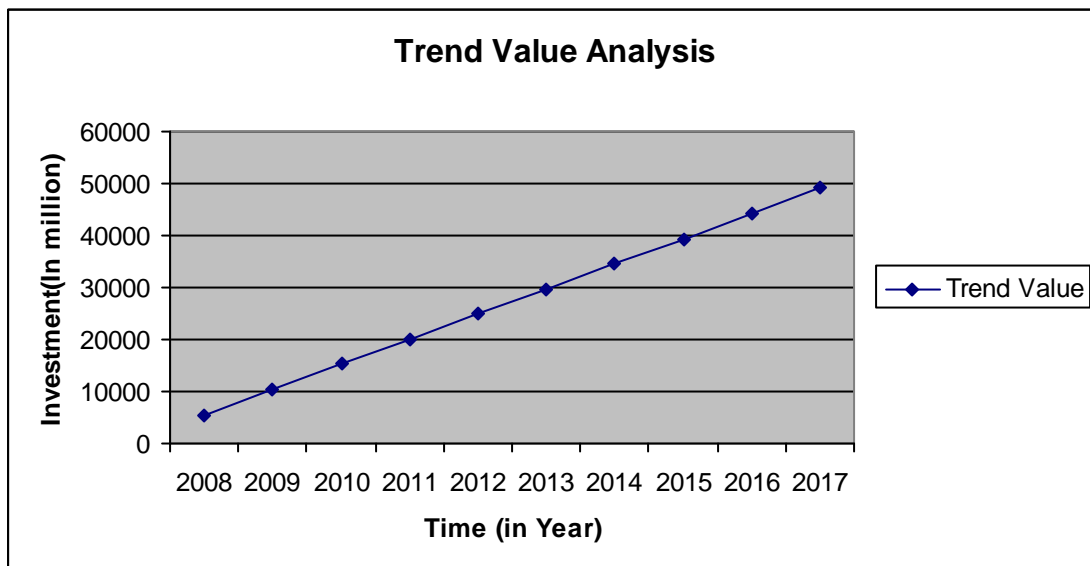
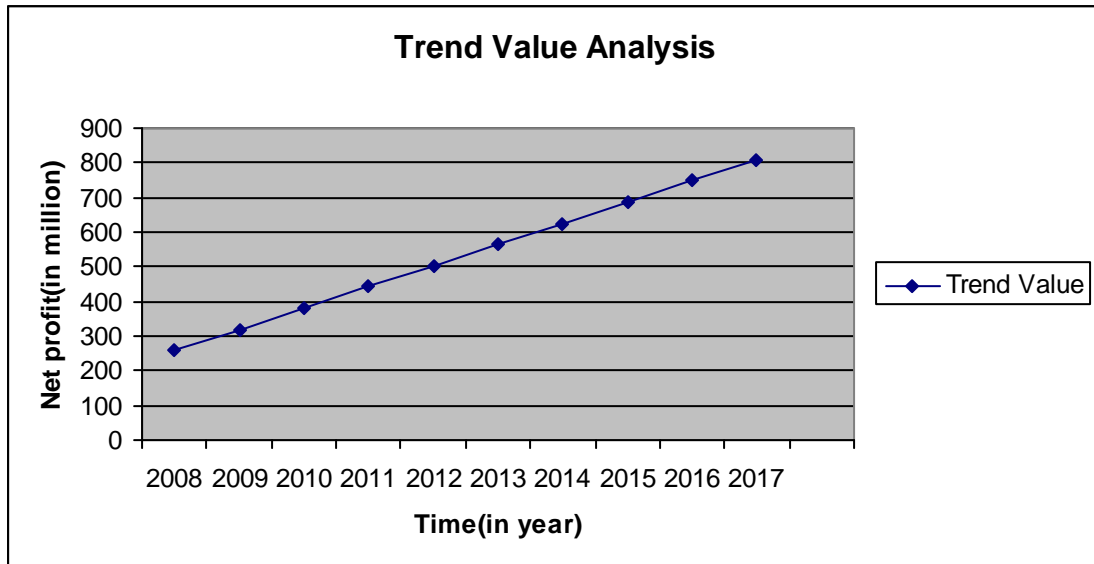


Figure 5: Trend value of Net profit of NSBL



4.9 Major Findings of the Study

The preceding chapter have discussed and explored the facts and matters required for the various parts of the study. Analytical part, which is the heart of the study, makes an analysis of various aspects of the investment policy of commercial banks by using some important financial as well as statistical tools.

Having completed the basic analysis required for the study, the final and most important task of the researcher is to enlist findings issues and gaps of the study and give suggestions for further improvement. This would be meaningful to the top management of the bank to initiate action and achieve the desired result. The objective of the researcher is not only to point errors and mistakes but also to correct them and give directions for further growth and improvement.

The main findings of the study that are derived on the basis of financial data analysis of Nepal SBI Bank Limited are presented below.

4.9.1 Findings from the Liquidity Ratios Analysis:

1. From the analysis of the current ratio, current assets of NSBL have exceeded current Liabilities in average of the study period from 2007/08 to 2011/12 except in 2008/09. The ratio ranges from lowest 0.97 in 2008/09 to highest 1.34 in 2007/08 with an average ratio of 1.158. The ratio shows the fluctuating trend during the period. The coefficient of variation (C.V.) between the ratios for the study period is 10.85 %, which shows that the current ratios during the study period are consistent. In general, the current ratio analysis of the bank over the five years period indicates that the bank has been able to meet its short-term obligations and has satisfactory liquidity position.

2. The cash & bank balance to total deposit ratio of NSBL has fluctuating trend. The mean ratio is 6.69 % for the study period. The C.V. between the ratios is found to be 26.21 %, which shows that the ratios are not consistent.

This analysis indicates that the cash & bank balance position of NSBL with respect to deposits is better to serve its customers deposit withdrawal demands. It implies the satisfactory liquidity position of NSBL.

3. The cash & bank balance to current assets ratio of NSBL has fluctuating with increasing trend. The lowest ratio is 7.52% in 2007/08 and the highest is 21.62 % in 2011/12. The mean of the ratios for the study period is 15.16 % & the C.V. between them is 34.82 %. On the basis of C.V. the ratios are seemed to be variable and less consistent.

It indicates that NSBL is in better position in maintaining its cash & bank balance to meet its daily requirements to make the payments on customer deposit withdrawals.

4.9.2 Findings from the Asset Management Ratios Analysis

1. The loan & advances to total deposit ratio of the bank is 88.32 % in 2007/08. It is decreased up to 40.01 % in 2011/12, which is lowest of the study period. The mean of the ratios is 58.40 % with 25.78 % C.V. between them, which shows that the ratios are not consistent over the study period.

This ratio is also called CD ratio i.e. Credit-Deposit ratio and around 70 % of CD ratio is taken as standard. From this point of view, the loan & advances to total deposit ratio of the bank is low. Loan and advances is the proportion banks investment into most risky assets. High level of risk is not desirable for commercial banks as any default can create the liquidity problem.

2. The investment to total deposit ratios of NSBL are in increasing and decreasing trend during the study period. The highest ratio is 47.52 % in 2008/09 and lowest is 22.52 % in 2007/08 with mean ratio of 41.45 %. The C.V. of 22.50 % between them shows that the ratios are less consistent

The figures suggest that the bank has not mobilized significant amount of fund on the government securities and shares and debentures of other companies. But for the investment on shares and debentures of other companies, the security market of the country is not so developed. There are limited companies listed in the stock exchange.

3. The loan and advance to total working fund ratio ranges from the minimum of 45.03 % in 2011/12 to the maximum of 70.48 % in 2007/08. The mean of the ratio is 51.65 % and the C.V. between them is 18.59 %, which shows the ratios are inconsistent over the study period. This shows that loan and advances comprises 51.65 % in average of the total asset of the bank.

The study shows that about two-third of the asset of the bank comprises loan and advance i.e. risky asset. Loan and advances is the most risky and most productive asset of the bank. High ratio suggests high risk and eventually high return of the bank. So, NSBL has taken optimum risk towards the mobilization of its fund to risky assets.

4. The total outside assets to total deposits ratio of the bank is consistent over the study period, except for the year 2007/08 and 2008/09. The maximum ratio is 110.84 % in 2007/08 and minimum ratio is 94.88 % in the year 2011/12. The mean of the ratios is 99.80 % and C.V. between them is 6.04 %. On the basis of C.V. it can be concluded that the ratios are satisfactorily consistent during the study period.

Outside asset i.e. loan and advances and investment is the major area of fund mobilization by the commercial banks. This is the most productive area for the fund mobilization. NSBL has consistently mobilized its funds in the productive area. So, the deposit mobilization of the bank for the income generation is satisfactory.

5. The Loan & Advances to total outside assets ratio ranges from the minimum 51.66% in 2011/12 to the maximum of 79.68 % in 2007/08. The mean of the ratios is 57.88 % and the C.V. between them is 18.87 %, which shows that the ratios are inconsistent over the study period with decreasing trend.

The study suggests that the more proportion of total outside asset is loan and advances. Loan and advances is the more risky asset and generates more income in comparison to investment. So NSBL has mobilized more proportion of its fund in risky area.

6. The total outside assets to total assets ratio has ranged from 87.16 % in 2011/12 to 94.20 % in 2008/09. The ratios have a fluctuating trend between them. The mean of the ratio is found to be 79.20 % with 13.03 % C.V. between them, which indicates that the ratios are consistent and less variable during the study period.

More proportion of the bank's asset is outside asset i.e. loan and advances and investment. So, the bank has consistently mobilized its fund into income generating assets.

4.9.3 Findings from the Activity Ratios Analysis

The Loan loss provision to total loans & advances ratios for the study period has fluctuating trend. The ratio ranges from 0.47 % in 2007/08 to 1.72 % in 2009/10 with an average of 1.01 %. The C.V. between them is 44.37 %, which indicates that the ratios are highly variable and inconsistent with the fluctuating trend.

The loan loss provision is the cushion against future defaults by borrowers. But in short term, it affects on the profitability of the bank. The high ratio is the indicative of the low quality of productive asset. The loan loss provision for performing loan is 1% and higher ratio than 1% indicates that the bank has certain proportion of non-performing loan. The average provision for loan loss indicates that quality of loan becoming satisfactory.

4.9.4 Findings from the Loans & Advances Portfolio Analysis

1. The priority sector loans to total loans & advances the ratios are ranged from 9.76 % in 2011/12 to 20.09% in 2009/10. The mean of the ratios is found to be 15.98% with 24.07 C.V. between them, which indicates that the ratios are almost consistent and not variable over the study period.

For the years of study period the bank has fulfilled its priority sector lending requirement, which the NRB has set.

2. The sector wise total loans & advances into agricultural, industrial, commercial, service and others sectors explains NSBL's diversification of credit to different sectors of economy. The bank has mostly used its funds in industrial sector. In average, lending in industrial, commercial, others, service and agricultural sector take the first, second, third, fourth and fifth place with mean percentage of 51.07 %, 21.41 %, 13.87%, 13.52 %, and 0.40 % respectively in the lending portfolio of the bank.

The lending in the agricultural sector is very nominal comparing to others. The ratios are fluctuating over the study period ranging from minimum of 0.20% in 2007/08 to maximum of 0.91% in 2011/12. The mean of the ratios is 0.4% with 81.40% C.V. between them, which suggests that the ratios are highly volatile and less consistent.

The lending in industrial sector is in more consistent than others. Bank has invested half of its fund to production sector. The ratios are in fluctuating trend and ranges from 54.89% in 2010/11 to 46.28% in 2008/09. The average ratio is 51.07% with C.V. 6.96% between the ratios over the study period. It signifies that the ratios are consistent and less variable.

The lending in commercial sector shows the overall decreasing trend with the ratios ranging from the minimum 17.25% in 2010/11 to the maximum 27.56% in 2008/09. The mean ratio is 21.14% and the C.V. between the ratios is 20.60%, which shows the ratios are less consistent over the study period.

The lending in service sector shows overall increasing trend over the study period. The ratio ranges from the minimum 5.83% in 2007/08 to the maximum of 18.23% in 2011/12 and the C.V. 34.35% shows the ratios are variable and not consistent during the study period. The mean of the ratios is 13.52.

The lending to the other sectors shows the decreasing trend with the fluctuations between them. The ratios range from the minimum of 8.17% in 2011/12 to the maximum of 20.43% in 2007/08. The mean ratio is 13.87%. The C.V. of 36.34% shows the ratios are less consistent and more variable over the study period.

The analysis shows that the lending portfolio of NSBL is not well managed and it is not properly diversified. Half of the fund from is poured in a single sector i.e. industrial/ production sector. If the industrial sector will be in slack, the bank will definitely suffer from it.

4.9.5 Findings from the Profitability Ratios Analysis

1. The Interest income to total income ratios are fluctuating over the study period ranging from the minimum of 88.25% in 2011/12 to the maximum of 89 % in 2009/10. The mean of the ratios is 88.54% and the C.V. between them is 0.33%,

which shows the highly satisfactory consistency of the ratios over the study period.

Income generated from loan and advances constitutes the major portion of total income of the bank consistently. So, loan and advances is consistently playing major role for the profitability of the bank.

2. Interest expenses to total expenses ratios are in increasing trend ranging from 66.69 % in 2007/08 to 78.80 % in 2011/12. The mean of the ratios is 73.33 % with 5.40 % C.V., which shows the ratios are satisfactorily consistent over the study period.

Interest expenses paid to the depositors is the main expenses for the commercial banks. NSBL has more than half portion of interest expenses on total expenses. The decreasing trend of the ratios suggests that the cost of fund of the bank is also decreasing.

3. Total income to total expenses ratios are ranging in decreasing trend from the 1.60 % in 2007/08 to 1.21% in 2011/12. The mean of the ratios is found to be 1.36 times with 0.024% C.V., which shows that the ratios are highly satisfactory consistent during the study period.

The analysis suggests that one unit of expenses is generating 1.36 unit of income in average. The total income is consistently over the total expenses.

4. Return on assets (ROA) ratios are fluctuating with overall decreasing trend during the study period. The ratio ranges between 83% in 2011/12 to 1.44% in 2007/08. The mean of the ratios is found to be 1.07 % with 18.69% C.V. between them, which indicates that the ratios are less variable and consistent during the study period.

The return on assets of the bank is good in average. It indicates the good earning capacity of the bank's assets and good utilization of its assets but decreasing rate of it is not good at all.

5. Return on equity (ROE) ratios are fluctuating during the study period. The ratio ranges between 15.02% in 20 11/12 to 18.47% in 2008/09 with the mean ratio of 16.60%. C.V. between them is 7.34 %, which shows that the ratios are less variable and consistent during the study period.

The average ratio of 16.60% suggests that the return on shareholders fund of NSBL is very good and the ratios are in increasing trend.

6. Earnings per share of NSBL is fluctuating over the years. It ranges between Rs.22.94 in 2011/12 to Rs.36.20 in 2008/09. The mean EPS during the study period is found to be Rs.27.21 with 17.86% C.V. between them, which shows that the earning is less variable and satisfactorily consistent over the period of study. The mean EPS of the bank is very good and the ratios are also satisfactorily consistent and less volatile.

4.9.6 Findings from the growth ratios analysis

The analysis of the growth ratios of total deposits, total loan & advances, total investments, and net profit of Nepal SBI Bank Limited during the study period shows that total deposits of the bank is in increasing trend with the net growth rate of 388%. Similarly loan and advances of the bank is in also increasing trend with the net growth rate of 99% during the study period. The analysis shows that the total investments of the bank is also in increasing trend with over the years having net growth rate of 691% during the study period. The net profit of the bank is also in increasing trend over the years with the net growth rate of 93% during the study period.

The major source of fund of the bank is deposit from its customers and it is in increasing trend with reasonable growth rate. Similarly the bank's utilization of its funds in the form of loan and advances and investment also are in increasing trend with satisfactory growth rate. The net profit of the bank, which actually shows the performance of the bank in its overall operation, has the positive growth rate with increasing trend.

4.9.7 Findings from the correlation analysis

The correlation analysis between total deposit and total loan and advances, between total investment and total deposit, between total loans and advances and net profit, between total investment and total net profit shows that the correlation coefficient (r) between them are positive. Since $r > 6 * P.Er$ in all cases and r is positive and

nearby 1. So, it is inferred that there is very strong positive correlation between all the terms.

The increase and decrease of one variable of the bank strongly affects the volume of other variables.

4.9.8 Findings from the trend analysis:

Trend analysis of total deposit, total loan and advances, total investment and total net profit from 2008 to 2012 and projection for next 5 years till 2017 is conducted in this chapter of study

Since the earning assets of the bank, loan and advances and investment, are in increasing trend and the earning of the bank is also in increasing trend. This suggests that the quantity of the productive assets is increasing, in the same time the quality of the assets is also in increasing trend. Bank management not only should effort towards the increment of its total assets but also it should give due attention towards the increment of the quality of the assets for the better productivity.

CHAPTER - V

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

This chapter includes two aspects of the study. First aspect of the study focuses on summarizing the fact-findings of the study and making concluding remarks upon them. While the second aspect of the study focuses on making some useful suggestions and recommendations based on findings of the study to improve the investment policy of Nepal SBI Bank Limited.

5.1 Summary

The development of any country largely depends upon its economic development. Economic development demands transformation of savings or investable resources into the actual investment. Capital formation is the prerequisite in setting the overall pace of the economic development of a country. It is the financial institution that transfers funds from surplus spending units to deficit units.

Banking sector plays an important role in the economic development of the country. Commercial Banks are one of the vital aspects of this sector, which deals in the process of channeling the available resources in the needed sector. It is the intermediary between the deficit and surplus of financial resources. Financial institutions like banks are a necessity to collect scattered saving and put them into productive channels. In the absence of such institutions it is possible that the saving will not be safely and profitably utilized within the economy. It will be diverted aboard or channeled into unproductive conspicuous consumption including real estate speculation.

Investment operation of commercial banks is very risky one. It is the most important factor from the view point of shareholders and bank management. For this, commercial banks have to pay due consideration while formulating Investment Policy. A healthy development of any commercial bank depends upon its investment

policy. A good investment policy attracts both borrowers and lenders, which helps to increase the volume and quality of deposits, loans and investment.

The major source of income of a bank is interest income from loans and investments and fee based income. As loan and advances dominate the asset side of the balance sheet of any bank; similarly earnings from such loan and advances occupy a major space in income statement of the bank. However, it is very important to be reminded that most of the bank failures in the world are due to the shrinkage in the value of loans and advances. Hence loan is known as risky asset and investment operation of commercial banks is very risky one. Risk of non-repayment of loan is known as credit risk or default risk. Performing loans have multiple benefits to the society by helping for the growth of economy while non-performing loans erodes even existing capital. Considering the importance of lending to the individual banks and also to the society it serves, it is imperative that the bank meticulously plans its credit operations.

Though several commercial banks have been established in our country within short period of time, stable, strong and appropriate investment policy has not been followed by the commercial banks to earn sufficient return. They have not been able to utilize their funds more efficiently and productively. Thus proper utilization of the resources has become relevant and current issue for the banks. The directions and guidance provided by Nepal Rastra Bank are the major policy statements for Nepalese commercial banks. However, a long term and published policy about their operation is not found even in the joint venture banks.

The main objective of the study is to evaluate the investment policy of Nepal SBI Bank Ltd and to suggest measures to improve the investment policy of the bank. The study has been constrained by various common limitations.

The study is based on secondary data from F/Y 2007/08 to 2011/12. The data have been basically obtained from annual reports and financial statements, official records, periodicals, journals and bulletins, various published reports and relevant unpublished master's thesis. Besides this, personal contacts with the bank personnel have also been made.

Financial as well as statistical tools have been deployed in order to analyze and interpret the data and information. Under financial analysis, various financial ratios

related to the investment function of commercial banks i.e. liquidity ratio, asset management ratio, activity ratio, loan and advances portfolio, profitability ratio and growth ratio have been analysed and interpreted. Under statistical analysis, some relevant statistical tools i.e. co-efficient of correlation and trend analysis have been used. This analysis gives clear picture of the performance of the bank with regard to its investment operation.

5.2 Conclusion

Liquidity

The current ratio of the bank over the five years is 1.158 times on an average. Although the current ratio of 2:1 is considered as standard, acceptability of the value depends on the industry. For the banks a current ratio of 1:1 or above would be considered acceptable. Therefore the liquidity position of NSBL is normal from the viewpoint of current ratio.

The cash and bank balance to total deposit ratio is somehow low to meet the short-term obligation of the bank. The mean cash and bank balance to total deposits ratio of 6.59% shows that the bank has little liquidity. But the ratios are less consistent over the study period.

Similarly 15.16% of mean cash and bank balance to current assets ratio shows that one-sixth of the current asset is very liquid. 34.82% C.V. shows that the ratios are not consistent.

The investment on government securities to current assets ratio is 28.75% on an average during the study period, which indicates that the bank has maintained sufficient amount of adequate liquid assets to meet the unexpected future liquidity needs. And the ratios over the study period are consistent.

Hence, the above results show that the liquidity position of NSBL is good enough to meet the short-term obligations. The maintenance of the liquidity also depends on the past withdrawal trend of the bank. The inconsistency of the ratios shows the lack of

specific corporate policy about the maintenance of liquidity. The proportion of cash and bank balance to current assets is satisfactory, which shows that the bank is maintaining and investing in government securities to get return.

Asset Management

The mean CD ratio of the bank is 58.40%, which is satisfactory. It shows that the bank is perfect in lending. The ratios are satisfactorily consistent over the study period.

The mean Investment to total deposits ratio is 41.45% and the ratios are more volatile. The increasing trend of the ratio suggests that the bank is increasing its investment on government securities and shares and debentures of other companies.

The loan and advances to working fund ratio is 51.65% in average and the ratios are consistent also. This shows that NSBL has satisfactorily utilized its total assets for the purpose of income generation. Majority of the total asset in average is mobilized in productive area.

NSBL has invested 11.72% of fund from total asset on government securities in average. The ratios are inconsistent also. So the bank has less investment on risk-free area, which has less return also. The inconsistency of the ratios shows that the bank has not specific policy for the investment on government securities.

The bank has very nominal investment on shares and debentures of other companies. The mean investment is 0.094% on study period and the ratios are inconsistent.

The mean total outside assets to total deposits ratio is 99.80% and the ratios are less variable during the study period. It shows that out of total deposits liability, the bank has utilized about 99.80% of it in income generating assets.

The loan & advances to total outside assets ratio of the bank is 57.88% on an average during the study period and the ratios are consistent during the period. It shows that the bank has given priority to invest in more income generating assets as loan and advances.

Investment on government securities to total outside assets ratio is 13.15% on an average during the study period but the ratios are not consistent and more variable during the period. It indicates that the bank does not have any specific and stable policy regarding how much to invest in risk free assets and how much in more risky assets for the purpose of income generation. The bank has more aggressive risk taking approach.

Total outside assets to total assets ratio is found to be 79.20% on average during the study period and the ratios are consistent. It shows that bank is utilizing more proportion of its assets for income generating purpose.

Total Off-balance sheet operation to loans and advances ratio is found to be 19.15% on an average during the study period and the ratios are in fluctuating trend with consistency between them during the period. It shows that the bank is not focusing well on fee based OBS transactions in comparison to loans and advances. The proportion of growth of loans & advances and OBS transactions is consistent. Volume of loans & advances increases more than OBs transactions.

Hence, the above results show the asset management efficiency of the bank, which is directly related to the investment policy of the bank. The bank has utilized about 90% of its deposits liability into income generating assets and most of them in the form of loans and advances. The bank has given priority to invest in risky assets than in risk free assets and the policy seems to be consistent because of the consistency of the ratios of risk free assets to total outside assets. The bank has been utilizing about 80% of its total assets for income generating purposes, which shows the aggressive risk taking policy of the bank. About 80% of CD ratio also suggests the aggressive lending policy of the bank. Similarly the bank does not seem to have proper policy to increase the fee based OBS transactions in comparison to loan and advances.

Activity

Loan loss provision to total loans & advances ratio is found 1.01 % on an average during the study period and the ratios are in increasing trend and are variable due to their continuous increasing nature year by year. This increasing nature of loan loss

provision indicates that the quality of loans becoming degrading year by year i.e., it seems that amount of non-performing loans is increasing and possibility of default in future is increasing. The loan loss provision for the performing loan is 1% of total loan and advances. So, the higher ratio of loan loss provision more than 1% signifies that the bank is having certain proportion of non-performing loan.

The analysis shows that Non-Performing loans to total loans & advances ratio of NSBL is 2.12% on an average during the study period. The ratio has been fluctuating over the years and although the highest ratio was found in 2007/08 which is 4.03%. The bank has decreased the ratio next year. This shows bank is aware of Non-performing loans problem.

Loans & Advances Portfolio

Priority sector loans to total loans & advances ratio is found 15.98% on an average during the study period and the ratios are almost inconsistent. The average ratio required is 12%, except for the year 2011/12. So, the bank is fulfilling the directive credit requirement every year.

Sector wise portfolio analysis of the loans and advances shows that the bank has given priority to industrial or production sector for lending. On an average during the study period the bank has advanced 51.07% on average of loans and advances to industrial sector and the ratio is consistent also. The bank has invested very nominal fund in the agricultural sector i.e. 0.4% on average. Lending in commercial sector is 21.14% on average and less consistent. Service sector lending on an average is found about 13.52% and the ratios are in increasing trend.

Hence, the analysis shows that the lending portfolio of NSBL is not well managed. Although the bank is fulfilling the NRB requirement for priority sector lending, the sector wise lending portfolio it is not properly diversified. Half of the fund is poured in a single sector i.e. industrial/ production sector. The industrial sector lending is considered as more risky than commercial and service sector lending. The investment in a single sector increases the portfolio risk.

Profitability

Interest income to total income ratio of the bank is 88.54% on an average during the study period and the ratios are highly satisfactory consistent. The average interest income to total outside asset is 6.68% during the study period and the ratios are consistent.

Interest expenses to total expenses ratio is 73.33% on average and the ratios are in increasing trend. This shows that the bank is increasing its cost of fund over the year. This also shows that bank has low proportion of operating and overhead expenses.

There is 5.94% of interest income on total asset on average. The ratios are consistent also. So, the interest earning capacity of total asset is consistent.

The mean interest paid to total working fund ratio is 3.70% and the ratios are consistent. This shows that the cost of funds utilizing in the form of different assets to generate income has been consistent during the study period.

Total income to total expenses ratio is found to be 1.36 times on an average during the study period and the ratios are highly consistent over the years. So the total income is consistently over the total expenses.

Total income to total assets ratio is found to be 6.70% on an average during the study period and the ratios are consistent. This show that the earning power of the assets is consistent and it is generating income at the consistent rate.

Return on loan & advances ratio is 2.07% on an average during the study period and the ratios are fluctuating. But consistency of loans and advance is satisfactory.

Return on total assets ratio is 01.07% on an average during the study period and the ratios are not variable between them. This shows that the bank has been able to achieve stable rate of return on its assets.

Return on equity ratio is 16.60% on an average during the study period and the ratios are in fluctuating trend with over the years and the ratios are satisfactorily consistent and less variable. This shows that the mean ratio of ROE is satisfactory and it is increasing during the recent years.

Earning per share is Rs.27.21 on an average during the study period and the ratios are consistent and in fluctuating trend.

Net Interest Margin is 4.28% on average during the study period and the ratios are consistent. This shows that the bank has satisfactory net interest margin and is doing better to recover the costs and to earn higher profit. The consistency of the ratios shows that bank has specific policy to get the consistent net interest margin over the period.

Hence, the above result shows that the bank does have specific policy to increase the profitability of the bank. The interest earning capacity of total loan and advances, total outside asset and total working fund are consistent. Net interest margin of the bank is also satisfactory. The profitability ratios like return on loan and advances, return on assets, return on equity, earning per share etc are also in satisfactory level over the year. This shows that the non-operating expenses of the bank like provision for loan loss is decreasing, which is increasing the profitability of the bank. Interest income has high contribution to the total income of the bank. This shows that the bank has less proportion of income from fee based transactions. Interest expenses contribute about 73% of the total expenses of the bank, which shows that the bank has low proportion overhead expenses. In overall, investment policy adopted by the bank is satisfactory appropriate from the profitability point of view.

Growth

The growth ratio of total deposits during the study period is 388% and the amount of deposits is in increasing trend every year. The growth ratio of total loan and advances during the study period is found to be 99% and is in increasing trend every year. So, the total deposit and loan and advances are increasing with almost equal proportion. The growth ratio of investments during the study period is 691% with increasing trend. The net profit of the bank is also in increasing trend with net growth rate of 93%.

Hence, the above result shows that the bank has been collecting the deposits funds in increasing trend and it has been increasing its loans and advances and investments with the almost same rate. So, both the sources and uses of fund is in increasing trend. At the same time net profit of the bank has also positive growth and it is increasing over the year. It shows that the bank has been successful to adopt the appropriate investment policy to increase the profitability of the bank with positive growth rate of deposit and loans and advances.

Correlation

The correlation analysis shows that the correlation coefficient r between deposits and loans & advances of the bank is 0.770 and is more than six times the probable error, which infers that there is very strong positive correlation between deposits and loans & advances during study period. The analysis shows that there is significant correlation between total deposit and total investment. Similarly, there is positive correlation between total loan & advances and total net profit and it is greater than six times the probable error. So, the total loan and advances and total net profit are also correlated during the study period. The same is for total investment and total net profit and they are also correlated during the study period. This analysis shows that the increase of deposit, loan and advances and investment is contributing to increase the net profit of the bank. The net profit of the bank may decrease if total loan and advances and investment of the bank are decreased.

Trend analysis

From the trend analysis of total deposit, loan and advances, investment and net profit shows that total deposit, loan and advances and investment are in increasing trend.

Total value projected for total deposit, loan and advances and investment are Rs. 100055.67 million, 42450.25 million and 49072.83 million respectively. The net profit is in increasing trend and total net profit projected till 2017 is Rs. 809.06 million.

Hence the NSBL is able to increase the profitability of the bank due to its fund collection and its utilization is increasing. Bank is adopting the proper policy to increase the profit of the organization. If the net profit moves in this trend, bank will be surely in good position after some years. So the investment policy of the bank in terms of optimum utilization of its resources to generate optimum return is well managed.

Hence from the overall analysis of investment policy of NSBL with the help of financial, mathematical and statistical tools the problems set for the study is answered as under, which is the main objective of this study.

1. The proportion of non-performing assets on total loan and advances of the bank is more than the satisfactory level. It should be less than 5% to be graded as internationally A grade commercial bank. For the Nepalese context also, NPA should be in single digit to be considered as satisfactory. The NPA level of the bank is a bit higher than these standards. So, the management of the bank should give its due attention in time to manage the NPA level within the satisfactory level.
2. The loan and advances portfolio of the bank is not satisfactory. The lending is not properly diversified. Half of the loan from total portfolio is given to industrial sectors. Bank is unable to explore the new and profitable sectors for the lending purpose. So, the bank has very risky portfolio of loan and advances. If industrial sector will not function properly, its impact to the bank will be huge.
3. Bank is fulfilling its priority sector investment requirement every year, during the study period. In the course of failure to fulfill the directive credit requirement, bank is subject to penalty, which affects the profitability of the bank. The average priority sector lending of the bank is more than required 12% landmark.

4. The relation of total deposit is positive to total investment i.e. if total deposit increases, bank's loan and advances, investment on government securities, shares and debentures of other companies also increases. The bank's investment, in the form of loan and advances and other investments, has positive relation to total net profit of the bank. Bank's total profit is positive to its total investment.

5.3 Recommendations

On the basis of analysis and findings of the study, following recommendations can be made as suggestions to overcome the weakness and less effectiveness in the existing investment policy of Nepal SBI Bank Limited.

5.3.1 Before mobilizing fund well, NSBL is recommended to increase its deposit to lower the credit/deposit ratio in certain extent. The bank has to collect a large variety of deposit schemes. The bank should explore the new deposit products to attract the deposit considerably. For this bank should lunch the new schemes like prize scheme, gift schemes, child deposit schemes, recurring deposit schemes etc. As the competition on the banking sector is increasing, bank should follow the innovative approach to bank marketing.

5.3.2 As the amount of investments made by the bank is found very little and also inconsistent during the period, the bank is recommended to increase the investment which helps to utilize the idle funds into income generation as well as minimizes risk and also helps to maintain optimal level of liquidity. Increasing the amount of investment in government securities also helps the bank to maintain an equilibrium level of risk free and risky assets.

5.3.3 Interest income from loan and advances and investment has dominance to the total income of the bank. Income from other fee-based transactions has low proportion. The portion of OBS transactions is found decreasing in comparison to loans and advances. Now a day most of the commercial banks are getting more benefits and increasing their earnings through the

enhancement of the fee-based OBS transactions. So the bank is recommended to give more priority to increase the fee-based OBS transactions to generate more income.

5.3.4 The non-performing loan of the bank is increasing and it is above the satisfactory level. So, the bank management is recommended to give due consideration towards the NPA management in time. The bank has to give its effort towards the recovery of the loan. For this bank has to form the loan monitoring and recovery committee in its central level which keeps the updated database of total loan and advances and its repayment trend. Bank is recommended to adopt the aggressive loan recovery and follow-up policy. Similarly, the improper project appraisal also increases the chances of default of the loan and advances. So, the bank is recommended to follow-up the scientific project appraisal approach and train the employee in the loan section accordingly.

5.3.5 The bank is advised to examine carefully from time to time the portfolio management strategies to maintain equilibrium in the portfolio of loans and investment and make continuous efforts to explore new, competitive and high yielding investment opportunities to optimize the return. The bank has been lending more than 50% of its credit to industrial only during the study period, but at present this sectors is not doing well. So the bank is recommended not to expand its business in this sector so heavily, instead it is advised to give more focus to increase its volume of credit to other sectors specially to retail financing. Bank must develop new lending products. Banking sector is going in consumer credit all over the world by financing the consumer goods. So, NSBL is recommended to focus the fixed income generating people and lunch new credit products like housing loan, education loan, car loan etc. The bank has to concentrate on customer oriented lending policy to sustain in the competitive banking business.

Similarly, the bank is fulfilling its lending requirement towards the priority sector. It is the efficiency of the bank's management. It may affect highly towards the profitability of the bank but it may degrade the image of the

bank towards the regulatory authority. Bank has to duly follow the legislative provisions of the central bank. Bank also has to give its attention towards the national interest of the country. But due to the lack of reliable lending opportunities and fear of losing the principle in rural sector, all commercial banks including NSBL has been less oriented toward the priority sector and deprived sector lending function. Hence it is recommended that the government and Nepal Rastra Bank should take appropriate action to initiate the commercial banks to attract to flow credit in rural economy so that we can expect the increase in the priority and deprived sector lending by the banks. Posing the compulsions by directives does not create long term healthy lending practices unless the commercial banks are not self motivated to flow credit in this sector.

5.3.6 The bank should be careful in increasing net profit in a real sense to maintain the confidence of shareholders, depositors, its customers and the general public. The overall profitability of the bank has been increasing during the period resulting the sharp increase in the return to the shareholders. The return on loan and advances, return on total assets, return on equity, earning per share all is increasing. The sources of fund and its utilization have been increasing and also the total income of the bank has been increasing due to which the bank has been able to increase the profitability. One of the reasons for this is more increase in the operating income of the bank. Therefore the bank is recommended to decrease the expenses of the bank by controlling the operating expenses as well as by collecting the interest free deposits. It is also recommended to increase the income by enhancing the fee-based OBS transactions as well as utilizing the excess liquid funds in the form of investments.

5.3.7 The bank is recommended to adopt innovative approach to marketing. In the light of growing competition in the banking sector, the business of the bank should be customer oriented. It should strengthen and activate its marketing function, as it is an effective tool to attract and retain the customers. For the purpose, the bank should develop an innovative approach to bank marketing and formulate new strategies of serving customers in a convenient way.

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APPENDIX - I

An Introduction to Nepal SBI Bank Limited

Nepal SBI Bank Ltd. (NSBL) is the first Indo-Nepal joint venture in the financial sector sponsored by three institutional promoters, namely State Bank of India, Employees Provident Fund and Agricultural Development Bank of Nepal through a Memorandum of Understanding signed on 17th July 1992. NSBL was incorporated as a public limited company at the Office of the Company Registrar on April 28, 1993 under Regn. No. 17-049/50 with an Authorized Capital of Rs.12 Crores and was licensed by Nepal Rastra Bank on July 6, 1993 under license No. NRB/1.Pa./7/2049/50. NSBL commenced operation with effect from July 7, 1993 with one full-fledged office at Durbar Marg, Kathmandu with 18 staff members. The staff strength has since increased to 351. Under the Banks & Financial Institutions Act, 2063, Nepal Rastra Bank granted fresh license to NSBL classifying it as an "A" class licensed institution on April 26, 2006 under license No. NRB/I.Pra.Ka.7/062/63. The Authorized, Issued and Paid-Up Capitals have Rs.300 crores, 210.29 crores and 209.39 crores respectively till 2012. The management team and the Managing Director who is also the CEO of the Bank are deputed by SBI. SBI also provides management support as per the Technical Services Agreement. Fifty five percent of the total share capital of the Bank is held by the State Bank of India, fifteen percent is held by the Employees Provident Fund and thirty percent is held by the general public.

1.2.2 Branch Network

The bank has established its branches in all the developmental regions of the Kingdom. At present, the bank is providing services to its clients through 56 branches, situated at different cities of the country. Its corporate office is situated at Hattishar, Kathmandu and main branch at Durbar Marg,

1.2.3 Present Products and Services provided by the Bank

Presently bank is providing different deposit schemes such as saving bank deposit, current deposit, fixed deposit, call deposit and recurring deposit. It is also availing various loan products as housing loan, vehicle loan, educational loan, mortgage loan, mortgage plus loan, doctor plus, teacher plus, overdrafts against shares and SME Loan for Small and Medium Enterprises. Besides it is providing Anywhere Banking facility, WUMT, Remittance facility from India etc. and also providing ATM debit card facility to its customer.

APPENDIX – II

NRB Directives Relating to Banking Regulations / Prudential Norms

Nepal Rastra Bank issues circulars time to time as guidance/regulation with respect to operation of commercial banks in Nepal. The NRB has formulated banking regulations/prudential norms in terms of loan classification and provisioning, investment on priority and deprived sector, single borrower limit, cash reserve requirement, interest rate spread, capital adequacy, investment in share and securities etc. We discuss some of those in brief, which are related to investment function of commercial banks.

1) Directives Relating to Loan Classification and Provisioning. (Circular dated 2062.4.3/ July 18, 2005 with ref no Bai. Bi. Ni. Bi. 148/1/2062/63)

Effective FY 062/63 (2005/2006), Banks shall classify outstanding loan and advance on the basis of aging of principal amount. Loan and Advance shall be classified into the following four categories:

- a) Pass:** All Loans and Advances the principal of which are not past due or past due for the period up to 3 (three) months shall be included in this category.
- b) Substandard:** All loan and advances the principal of which are past due for the period of more than 3 months and up to 6 months shall be included in this category.
- c) Doubtful:** All loans and advances which are past due for a period of 6 months to 1 year shall be included in this category.
- d) Loss:** All loans and advances which are past due for a period of more than 1 year as well as advances which have least possibility of recovery or considered

unrecoverable and those having thin possibility of even partial recovery in future shall be included in this category.

Here, if it is appropriate in the views of the bank management, there is not restriction in classifying the loan and advance from low risk category to high risk category. For instance, loans falling under Sub-standard may be classified into Doubtful or loss, and loans falling under Doubtful may be classified into Loss category. And the term Loans and Advance also include Bills Purchased and Discounted.

Loan Loss Provisioning

The loan loss provisioning, on the basis of the outstanding loans and advances and bills purchased classifies as above shall be provided as follows:

Classification of Loan	Loan Loss Provision
Pass	1%
Substandard	25%
Doubtful	50%
Loss	100%

Loan loss provision set aside for performing loans is defined as General Loan Loss Provision and loan loss provision set aside for non-performing loan is defined as Specific Loan Loss Provision.

Before this arrangement was in force i.e. up to 2057.3.31, the classification and provisioning of loans and advances as per circular dated 2047.12.8 (July 15, 2001) was as follows:

Classification of Loans	Time	Provision Required
Good	Not overdue	1%
Acceptable	Overdue upto 1 Month	1%
Evidence of sub-standard	Overdue 1-6 Months	5%
Substandard	Overdue 6 mths.-1 Year	25%
Doubtful	Overdue 1-5 Years	50%
Bad	Overdue more then 5 Years	100%

