CREDIT MANAGEMENT OF LAXMI BANK LIMITED AND SIDDHARTHA BANK LIMITED

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2nd Year Symbol No.: 390145

A Thesis Submitted To:

Office of the Dean

Faculty of Management

Tribhuvan University

In Partial Fulfillment of the Requirement for the Degree Of

Master of Business Studies (MBS)

Kathmandu Nepal

July, 2024

RECOMMENDATION

This is to certify that the thesis

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

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VIVA-VOCE SHEET

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And found the thesis to be the original work of the student and written According to the prescribed format. We recommend the thesis to be Accepted as partial fulfillment of the requirement for the degree of

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DECLARATION

I hereby declare that the work reported in this thesis " **CREDIT MANAGEMENT OF LAXMI BANK LIMITED AND SIDDHARTHA BANK LIMITED "**submitted to Office of the Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the degree of Master of Business Studies (MBS) under the supervision of Asso Prof. Dr. Kapil Khanal of Shanker Dev Campus, T.U.

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ACKNOWLEDGMENTS

Though management accounting is a new evolving phenomenon of accounting concept in modern business world, whatever the tools and techniques have been developed, are accepted as the inevitable management instruments for effective, efficient and rational decision-making. Realizing this fact, an attempt has been made in this thesis to shed light on the present practice of management accounting tools and techniques in commercial banks of Nepal.

Firstly I would like to offer my sincere gratitude to my respected supervisor Lecturer Ramesh Kumar Paudel of Shankar Dev Campus, Putalisadak for his constant encouragement, guidance and valuable supervision at every step of my work. This study would not have been materialized in the present form without his incisive observations and intellectual direction in the course of completion.

I am totally grateful to lecturer Asso. Prof. Dr. Kapil Khanal and Research Head Asso . Prof. Dr. Sajeeb Kumar Shrestha for their help and support while preparing the thesis. I am thankful to the managers, department chief, respective authorities and staffs of commercial banks which are taken as sample for this thesis work for providing me all the necessary data and information for my study.

Lastly but not least I would like to thank my friends and family, senior graduates who gave suggestions about this task and for their kind support for achieving the goal.

Bhola Nath Chaulagain

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ABBREVIATIONS

A.D.	:	Anno Domini
ADBL	:	Agricultural Development Bank Limited
B.S.	:	Bikram Sambat
BOK	:	Bank of Kathmandu
BWP	:	Banking With Poor
C.V.	:	Coefficient of Variation
CB	:	Commercial Bank Development
CEO	:	Chief Executive Officer
DICGC	:	Deposit Insurance and Credit Guarantee Corporation
e.g.	:	For Example
EBIT	:	Earning before Interest and Taxes
EPF	:	Employees' Provident Fund
EPS	:	Earning Per Share
etc.	:	Et cetera
FC	:	Foreign Currency
FD	:	Fixed Deposit
FY	:	Financial Year / Fiscal Year
GDP	:	Gross Domestic Product
govt.	:	Government
HMG	:	His Majesty's Government
i.e.	:	That is
IMF	:	International Monetary Fund
IPO	:	Initial Public Offering
JVB	:	Joint Venture Bank
LBL	:	Laxmi Bank Limited
Ltd.	:	Limited
m	:	Million
MBS	:	Master's Degree of Business Studies
NBL	:	Nepal Bank Limited
NEPSE	:	Nepal Stock Exchange Limited
NIDC	:	Nepal Industrial Development Corporation

NRB	:	Nepal Rastra Bank
NSBL	:	Nepal SBI Bank Limited
P	:	Page
PNB	:	Punjab National Bank
pp	:	Pages
PPA	:	Power Purchase Agreement
RBB	:	Rastriya Banijya Bank
Rs.	:	Rupees
SBL	:	Sidhartha Bank Limited
S.D.	:	Standard Deviation
SEBON	:	Securities Board of Nepal
TU	:	Tribhuvan University
viz.	:	Namely
Vol.	:	Volume

CHAPTER I
INTRODUCTION

1.1 Background of the Study

Nepal is a liberalized economy country opening up foreign investment since 2012. Almost half of its population lies under absolute poverty line, especially living in the rural areas are deprived of even basic needs and facilitates like enough calories pure drinking water sanitation facilities, electricity, road facility etc. Some of the basic human indicators like life expectancy, literacy, nutrition level etc. also show that Nepal occupies among the nation to eliminate the massive poverty persisting in the country through gradual development of the total nation and by providing and availing basic needs to poor people. Actually slow pace of developing of Nepal is due to nothing but landlocked position, poor resources mobilization and its utilization, weak infrastructure development and more over unstable eco-political environment. (Bhandari, 2005).

Commercial banks are growing very fast in Nepal. There are 27 commercial banks altogether in Nepal. Banking plays significant role in the economic development of a country. Bank is a resource for the economic development which maintains the self-confidence of various segments of society and extends credit to the people. So, commercial banks are those financial institutions mainly dealing with activities of the trade, commerce, industry and agriculture that seek regular financial and other helps from them. The objectives of commercial banks are to mobilize idle resources which contribute significantly for the formation and mobilization of internal capital and development effort (Bhandari, 2005).

The concept of the banking has developed from the ancient history with the effort of ancient goldsmiths who developed the practice of storing people's gold and valuables under such arrangement the depositors would leave their gold for safekeeping would get back their gold and valuable after paying a small amount as fee for safekeeping and serving (Adhikari, 2014).

The role of money in an economy is very important. Proper and well-planned management of money directs, determines and enhances the health and productivity of total financial sector and the performance of financial sector affect the growth of economy. Hence, Money is the topic to manage and banks are the manager. The existence of a bank is for the change in every aspect of human being and its presence is for the upliftment of people. Banks are the back bone of the economy. They act as intermediaries to channel funds to productive business companies and projects. Commercial Banks, Development Banks, Finance companies, Microfinance, Savings and Credit Associations, Mutual Saving Banks, Credit Unions, Insurance Companies, Pension Funds, Investment Companies, Investment Bankers, Securities Brokers and Dealers.

Banks grants loan and advances to industries, people and companies that result in the increase in the productivity of nation. For example: The loan against to agricultural sector enhances the agricultural product on. The loan amount can be used by the farmers as per their need to produce their product that will promote the agriculture product on. Similarly, the loan and advances to different people and corporate bodies help to increase their income and profits. They can use the amount as per their need at right place at the right time. Bank is a business organization where monetary transaction occurs. It creates fund from its clients saving and lends the same to needy person or business companies in term loans, advances and investment. So proper financial decision making is more important in banking transactions for its efficiency and profitability. Most of the financial decision making loan management it plays the vital role in the business succession, so efficient management of lending policy is needed. (Dangol, & Prajapati, 2071).

The source of finance is the most essential element for the establishment and operation of any profit and non-profit institutions. Profit oriented institutions usually obtain these sources through ownership capital, public capital through the issues of shares and through financial institutions such as banks, in the form of credits, overdrafts etc Commercial banks, others banking institutions (OBIs), Non-Bank Financial Institutions occupy important role in mobilizing financial resources. There are about 19 insurance companies including deposit insurance and Credit Guarantee Corporation, one Employee Provident Fund and one Citizen Investment Trust belong to this type of financial institutions. Apart from this, securities such as corporate shares debentures and bonds (Dangol, & Prajapati, 2071).

Banking plays a significant role in the economic development of a country. Nepal Bank Limited (NBL) is the first commercial bank of the country. Commercial banks are the heart of the financial institutions. They hold the deposits of many persons, government establishments and business units. They made funds available through their lending and investing activities to borrowers, individuals, business firms and government establishments.

In doing so, they assist both the flow of goods and services from the procedures to consumers and financial activities of the government, they provide a large proportion of the medium of exchange they are the media through which monetary policy is affected. These facts show that the commercial banking system of the nation is important to the functioning of the economy. Bank is a resource for the economic development, which maintains the self-confidence of various segments of society and extends credit to the people (Adhikari, 2014).

The more developed financial systems of the world characteristically fall into three parts. The Central Bank, The Commercial Banks and other financial institutions. They are known as financial intermediaries. The banking business has its genesis from its function of lending. Lending is the most fundamental function of a bank. The importance of Lending in banking business is undoubtedly unchanged and remains vital as it was early days of this business. Lending has its different forms. It can be divided into fund based and non-fund based Lending. The fund based Lending can be further divided into cash credit, Overdrafts, demand and term credits, bills purchased and discounted and export packing credit, project loan, etc. Similarly, non-fund based credit can be classified into documentary credit, guarantees and bill co-acceptance facility (Adhikari, 2014).

1.2Brief History Sample Organization under Study

1.2.1Introduction of Laxmi Bank Limited (LBL)

Laxmi Bank was incorporated in April 2002 as the 16th commercial bank in Nepal. In 2004 Laxmi Bank merged with HISEF Finance Limited, a first generation financial company which was the first and ever merger in the Nepali corporate history. Laxmi Bank is a Category ‘A’ Financial Institution and re-registered in 2006 under the “Banks and Financial Institutions Act” of Nepal. The Bank’s shares are listed and actively traded in the Nepal Stock Exchange (NEPSE). We are a technologically driven progressive Bank with strong risk and corporate governance foundations. We are known for our innovation and claim to many “firsts” in the Nepalese financial market. We have the best asset quality among all financial institutions in the country and our technology has been rated “Highly Secure” by an independent internationally accredited information system auditor. Laxmi Bank’s award winning Annual Reports has set the standards for quality, presentation and disclosure for the Nepalese corporate sector to follow since 2005. Laxmi Bank promotes a separate life insurance company-Prime Life Insurance Limited which came into operation in 2009. Laxmi Bank is a Category ‘A’ Financial Institution and re-registered in 2006 under the “Banks and Financial Institutions Act” of Nepal. The Bank’s shares are listed and actively traded in the Nepal Stock Exchange (NEPSE).

Table 1.1: Share Capital

Authorized Capital	10,500,000,000
Issued Capital	8,920,508,642
Paid up Capital	8,920,508,642

(*Source: http://laxmi.laxmibank.com*)

The bank is committed to excellence in delivery of entire gamut of financial services in order to achieve sound business growth and maximize stakeholder values by embracing team spirit, progressive technology and good corporate governance.

The bank values are built around high standards of good corporate governance. Transparency, professionalism and high ethical tone at the leadership are foundations on which our actions are based. Laxmi Bank’s Code of Conduct encapsulates international best practices applicable to Nepali context. The level of commitment of our people to take Laxmi Bank to greater heights has been a huge catalyst. The team spirit within the organization is something we are proud of. Provider of most integrated financial services, Key player and a thought leader in the retail financial services, A bank with the best asset book, Best IT capability And Preferred employer in the financial sector.

1.2.2 Introduction of Siddhartha Bank Limited (SBL)

Siddhartha Bank Limited (SBL) commenced operations in 2002. The Bank was promoted by a group of highly reputed Nepalese dignitaries having wide commercial experience. This bank provides a full range of commercial banking services through its 41 branches established in Kathmandu and outside the Kathmandu. The environment of Nepalese banking sector is undergoing a rapid transformation. With liberalization in financial markets and integration of domestic market with external markets, bank operations have become more complex and dynamic. It geared to meet the challenges and keep abreast with the changes. The Vision statement of the Bank describes the core values and purposes that guide the Bank as well as an envisioned future. Fundamentally, in all dealings SBL earnestly believes in transparency, financial soundness, efficiency and better technology. Similarly, the Bank has established a dedicated payment solutions department to look into alternative delivery channels such as Card Services, Internet Banking, ATMs and Mobile Banking. With this set-up, the Bank has been able to delivery technologically driven products and services to its Customers.

Table 1.2: Share Capital Structure

Authorized Capital	10,000,000,000
Issued Capital	8,88,76,04,540
Paid up Capital	8,88,76,04,540

(*Source: https://www.siddharthabank.com*)

1.3 Focus of the Study

Although the Laxmi Bank Limited and Siddhartha Bank have managed credit than other commercial banks within short period of time, they have been facing cut throat competition against one another. In Nepal there are 27 commercial banks. The study focus on evaluating the deposits utilization of the bank in terms of loans and advances and investments and its contribution in the profitability of the bank. Commercial banks hold deposit of many persons, government establishment and business units. They make fund available through their lending and investing activities to borrowing individual’s business firms and government establishment.

Here researcher has focused this resource mainly to highlight and examine the credit management of the selected bank ignoring other aspects of bank transaction. To highlight the credit management of the bank, the research is based on the certain statistical tools i.e. mean, standard deviation, coefficient of variance, coefficient of correlation, coefficient of determination and trend analysis with a view to find out the true picture of the bank. The main objective of this research is to analyze the credit management through the use of appropriate financial tools.

1.4 Statement of the Problem

Most major banking problems have been caused by weakness in credit management. Banks should now have a keen awareness of the need to identify measure, monitor and control credit as well as to determine that they hold adequate capital against it. These risks that they are adequately compensated for risks incurred. So, to establish creditability position is a major issue in commercial banking sector during these days. (Regmi, 2015).

It is no debate that high profitable or successful organization can easily fulfill every need of the organization, customers and can serve the society. To improve the profitability situation of the bank, it is necessary to establish the higher creditability position of the bank. Thus, the creditability is the major source and building better creditability position is the major strategy of every commercial bank. Credit is the most effective and sincere area in commercial bank. It is regarded as the heart of every commercial bank. But the banking sector is far from this fact. Thus, Credit management is considered as the heart issues in Nepalese Commercial banking sector. (Regmi, 2015).

Credit management concept has appeared as a major research gap in Nepalese Commercial banking sector. There is lack of such scientific and empirical research that could identify the issues of credit management in Nepalese commercial banks. In this regard, the performance of Nepalese commercial banks is to be analyzed in terms of their credit. Some research questions regarding to the credit practices, credit efficiencies, liquidity position, industrial environment, management quality, organization climate, are considered as a clear evident in present situation. Thus, the specific research questions regarding credit management in Nepalese commercial banking sector are identified as follows:

i) Is the credit practice adopted by commercial banks in good position?

ii) What is the credit efficiency of the Nepalese Commercial banks?

iii) Is there any relationship between credit position and profitability situation?

iv) What is the status of credit portfolio of commercial banks in term of?

Nepal is a small country with small market economic condition of the country is degrading due to conflict since 2052 B.S. But the situation has been changed peace process is going on. Overall economic sectors either manufacturing or commercial sectors have undergone heavy losses. However, the financial institutions are increasing regularly. Liquidity is maximum with the financial institutions are competing among themselves to advance credit to limited opportunity sectors. Non-performing credits of the banks are increasing year by year. To control such type of state, the regulatory body of the bank and financial institutions Nepal Rastra Bank (NRB) has renewed its directives of the credit loss provision.

1.5 Objectives of the Study

There is no doubt that the role of the commercial banks is significant in the development of the country. Banks help in the development of the country by providing credit to the necessary sectors.

Objectives of the study are as follows:

i) To analyze the lending portfolio of Laxmi Bank and Siddhartha Bank.

ii) To analyze the credits and advances provided by Laxmi Bank Limited and Siddhartha Bank Limited.

iii) To analyze the recovery status with comparing strength and weakness of the credit disbursed by Laxmi Bank Limited and Siddhartha Bank Limited.

1.6 Significance of the Study

There are few researches in commercial banking and especially on their Lending practice, insufficient books for the study. Lending is one of the essential and main functions where the whole banking business is rested upon. Thus, a study on the commercials banks and especially in their Lending and investment practices carry a great significant to various groups but in particular is directed to a certain groups of people/organization, which are:

i) Importance to shareholders.

ii) Importance to the management bodies of these banks for the evaluation of the performance of their banks and in comparison with other banks.

iii) Importance to "outsiders" which are mainly the customers, financial agencies, stock exchanges

iv) Importance to the government bodies or the policy makers such as the central bank.

v) This study would be important for the students as it provides theoretical as well as conceptual frame work of different aspect of credit management.

1.7 Limitations of the Sstudy

i) This study conducted to fulfil the requirements of Master's Degree in Business Studies (MBS) so the study cannot cover all the dimensions of the credit management.

ii) This study based on the period of five years (2015/16 to 2019/20) period.

iii) This study based on the secondary data published from concerned commercial banks.

1.8 Organization of the Study

The study will be organized in five chapters. Which are:

Chapter I: Introduction

The first chapter deals with introduction, problem of the study, and objective of study, limitation of study, need of the study, research methodology and method of analysis.

Chapter II: Review of Literature

The second chapter consists of review of literature. This chapter is subdivided into various sections such as conceptual framework, review from different studies, review from journal and articles and magazine and review from master's thesis for the concerned topic.

Chapter III: Research Methodology

The third chapter presents methodologies adopted for the research. It comprises research design, sources of data method of analysis and its descriptive presentation.

Chapter IV: Presentation and Analysis of Data

The fourth chapter deals with the techniques used in analyzing the collected data and its presentation in the descriptive and analytical manner.

Chapter V: Summary, Conclusions and Recommendations

The fifth chapter consists of summary, conclusion and recommendation about the topic concern.

CHAPTER II
REVIEW OF LITERATURE

The review of literature is a crucial aspect because it denotes planning of the study. The main purpose of literature review is to find out what works have been done in the area of the research problem under study and what has not been done in the field of books, reports, journals and research studies published by various institution unpublished dissertations submitted by master of Business Studies. It is divided into three headings:

i) Conceptual Review
ii) Theoretical Review
iii) Empirical review

2.1 Conceptual Review

The review of textbook and other reference materials such as: newspaper, magazines, research articles, journals and past thesis have been included in this topic. Credit administration involves the creation and management of risk assets. The process of lending takes in to consideration about the people and system required for the evaluation and approval of loan requests, negotiation of terms, documentation, disbursement, administration of outstanding loans and workouts, knowledge of the process and awareness of its strength and weakness are important in setting objectives and goals for lending activities and for allocating available funds to various lending functions such as commercial, instalment and mortgage portfolios (Johnson, 1940: 132).

Bajracharya (1991), in his article "Monetary policy and deposit mobilization in Nepal" has concluded that mobilization of the domestic saving is one of the prime objectives of the monetary policy in Nepal. And commercial banks are the most active financial intermediary for generating resources in the form of deposit of private sector and providing credit to the investors in different sectors of the economy.

Book named "Banking Management" say that in banking sector or transaction, an un avoidableness of loan management and its methodology is regarded very important. Under this management, many subject matters like the policy of loan flow, the documents of loan flow, loan administration, audit of loan, the condition of loan flow the provision of security, this management plays a great role in healthy competitive activities (Bhandari 2003:170).

It is very important to be reminded that most of the bank failures in the world are due to shrinkage in the value of loan and advance. Hence, risk of non-payment of loan is known as credit risk default risk (Dahal, 2002:114). Portfolio management helps to minimize or manage the credit risks by spreading over the risk to various portfolios. This method of managing credit risk is guided by the saying do not put all the eggs in a single basket (Bhandari, 2004:300).

2.1.1 Concept of Commercial Bank

Before defining the term commercial bank, let us define the meaning of bank and commercial. According to S. and S. s definition of bank, a banker or bank is a person or company carrying on the business of receiving money and collecting drafts, for customer’s subject to the obligation of honoring cheque drawn upon them from time to time by the customers to the extent of the amount available on their customer (Shekher & Shekher, 1999:4).

Paget (1987) states that no one can be a banker who does not take deposit accounts take current accounts, issue and pay cheque of crossed and uncrossed, for his customers. He further adds that if the banking business carried on by any person is subsidiary to some other business; he cannot be regarded as a banker (Page, 1987:2).
Commercial banks act as an intermediately; accepting deposits and providing credits to the needy area. The main source of the commercial bank is current deposit, so they give more importance to the liquidity of investment and as such they specialize in commercial banks are restricted to invest their funds in corporate securities. Their business is confined to financing the short-term needs of trade and industry such as working capital financing. They cannot finance in fixed assets. They grant credits in the form of cash credits and overdrafts. Apart from financing, they also render services like collection of bills and cheque, safe keeping of valuables, financial advising, etc to their customers (Vaidhya, 1999:24).

Commercial banks are organized as a joint stock company system, primarily for the purpose of earning profit. They can be either of the branch banking types as we see in most of countries, with a large network branches like in Nepal or of the unit banking type, as we see in the United States where a bank's operations are confined to a single office or to a few branches within a strictly limited area (Shekher & Shekher, 1999:4).

2.1.2 Functions of Commercial Banks

The business of commercial bank is primarily to hold deposit and make credits and investments with the object of securing profits for its shareholders. Its primary motive is profit; other consideration is secondary (Sudharsanam, 1976:123).The major functions of commercial banks are as follows.

Accepting Deposit

Accepting Deposit, Advancing Credit, Agency Services, Credit Creation, Financing of Foreign Trade, Safekeeping of Valuable, Making Venture Capital Credits, Financial Advising, Security Brokerage Services. (Shekher & Shekher, 1999:4).

Assist in Foreign Trade

The bank assist the traders engaged in foreign trade of the country. He discounts the bills of exchange drown by exports to receive money in the home currency. Similarly, he also accepts the bills drown by foreign exports (Vaidhya, 1999:29)

Offers Investment Banking and Merchant Banking Services

Banks today are following in the footsteps of leading of financial institutions all over the globe in offering investment banking and merchant banking services to corporations. These services include identifying possible merger targets, financing acquisitions of other companies, dealing in security underwriting, providing strategic marketing advice and offering hedging services to protect their customers against risk from fluctuating world currency prices and changing interest rates, (Vaidhya, 1999:29). Further, they support the overall economic development of the country by various modes of financing.

2.1.3 Concept of Credit

Credit is the amount of money lent by the creditor (bank) to the borrower (customers) either on the basis of security or without security. Sum of the money lent by a bank, is known as credit (Oxford Advanced Learners Dictionary 1992:279). Credit and advances is an important item on the asset side of the balance sheet of a commercial

bank. Bank earns interest on credits and advances, which is one of the major sources of income for banks. Bank prepares credit portfolio, otherwise it will not only add bad debts but also affect profitability adversely, (Varshney and Swaroop, 1994:6)
Credit is financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for an obligation of repay on specified date on demand. Banks generally grants credit on four ways (Chhabra and Taneja, 1991:4)
Overdraft: Cash Credit, Direct Credit, Discounting of Bills.

2.1.4 Types of Credit

Overdraft:

It denotes the excess amount withdraw over their deposits.

Cash Credit:

The credit is not given directly in cash but deposit account is being opened on the name of credit taker and the amount credited to that account. In this way, every credit creates deposit.

Term Credit:

It refers to money lent in lump sum to the borrowers. It is principal form of medium term debt financing having maturities of 1 to 8 years. Barely and Myers urge that bank credits with maturities exceeding 1 years are called term credits. The firm agrees to pay interest based on the bank’s prime rate and to repay principal in the regular instalments. Special patterns of principal payments over time can be negotiated to meet the firm’s special needs (Richard, 1996:80).

Working Capital Credit:

Working capital denotes the difference between current assets and current liabilities. It is granted to the customers to meet their working capital gap for supporting production process. A natural process develops in funds moving through the cycle are generated to repay a working capital credit.

Priority or Deprived Sector Credit:

Commercial banks are required to extend advances to the priority and deprived sector.12% of the total Credit must be towards priority sector including deprived sector. Rs. 2 million for agriculture cum service sector and Rs. 2.5 million for single borrows are limit sanctioned to priority sector. Institutional support to ‘Agriculture Development Bank’ and ‘Rural Development Bank’ are also considered under this category, deprived sector lending includes:

i) Advances to poor/downtrodden /week/ derived people up to Rs. 30,000 for generating income or employment.
ii) Institutional Credit to Rural Development Bank.
iii) Credit to NGOs those are permitted to carryout banking transaction for lending up to Rs. 30, 000.

Hire-purchase Financing (Instalments Credit)

Hire-purchase credits are characterized by periodic repayment of principal and interest over the maturity of the credit. Hirer agrees to take the goods on hire at a stated rental including their repayment of principal as well as interest with an option to purchase. A recent survey of commercial banks indicates those bank are planning to offer instalment credits on a variable rate basis. It can be secured and unsecured as well as direct and indirect instalment credit.

Housing Credit (Real Estate Credit)

Financial institutions also extend housing credit to their customers. It is different types, such as: residential building, commercial complex, construction of warehouse etc. It is given to those who have regular income or can earn revenue from housing project itself.

Project Credit

Project Credit is granted to the customers as per project viability. The borrowers have to invest certain proportion to the project from their equity and the rest will be financed as project credit. Construction credit is short- term credits made to develops for the purpose of completing proposed projects. Maturities on construction credits range from 12 months to as long as 4 to 5 years, depending on the size of the specific project (Johnson, 1940:242). The basic guiding principal involved in disbursement policy is to advance funds corresponding to the completion stage of the project. Hence, what percent of the credit will be disbursed at which stage of completion must be spelled in disbursement policy? Term of credit needed for project fall under it.

Consortium Credit

No single financial institution grant credit to the project due to single borrower limit or other reasons and two or more such institution may consent to grant credit facility to the project among them. Financiers bank equal (or Likely) charge on the project's assets.

Credit cards and Revolving lines of Credit

Banks are increasingly utilizing charge cards and revolving lines of credit to make unsecured consumer credit. Revolving credit line lowers the cost of making credit since operating and processing cost are reduced. Due to standardization, centralized, department processes revolving credits resulting reduction on administrative cost. Continued borrowing arrangement enhances cost advantages. Once the credit line is established, the customer can borrow and repay according to his needs and the bank can provide the fund to the customer at lower cost charge cards and credit lines tied to demand deposit accounts are the two most common revolving credit agreements. It can be further divided into credit cards, automatic overdrafts lines and large credit lines.

Off-Balance Sheet Transaction

In fact, bank guarantee and letter of credit refer to off balance sheet transactions of financial institution. It is also known as contingent liability. Contingent liability pinpoints the liability which may or may not arise during the happening of certain event. Footnotes are kept as reference to them instead of recording in the books of accounts. It is non funded based remunerative facilities but riskier than the funded until adequate collateral are not taken. Lets its two varieties be described separately.

Bank Guarantee

It is used for the sake of the customers in favour of the other party (beneficiary) up to the approved limit. Generally, a certain percent amount is taken as margin from the customer and the customer's margin account is credited.

Letter of credit (L/C)

It is issued on behalf of the customer (importer) in favour of the exporter (Seller) for the import of goods and services stating to pay certain sum of money on the submission of certain documents complying the stipulated terms and conditions as per as the agreement of L/C. It is also known as importers letter of credit since the bank of importer do not open separate L/C for the trade of sum commodities.

2.1.5 Objectives of the Sound Credit Policy

The purposes of a written credit policy are

i) To assure compliance by lending personnel with the bank's policies and objectives regarding the portfolio of credits and

ii) To provide personnel with a framework of standards within which they can operate.

2.1.6 Lending Criteria

While screening a credit application, 5-cs to be first considered supported by documents. They are:

1. Character

Character is the analysis of the applicant as to his ability to meet the obligations put forth by the lending institution. For this analysis, generally the following documents are needed. Memorandum and articles of association, registration certification, tax registration certificate (renewed), resolution to borrow, authorization-person authorizing to deal with the bank. (Bajracharya, 2071).

2. Capacity

Describes customer's ability to pay. It measured by applicants past performance records and followed by physical observation. For this, an interview with applicant's customers/suppliers will further clarify the situation, Documents relating to this area were: Certified balance sheet and profit loss account for at least past 3 years. In case of the personal loan they have to summit the proof source of income. References or other lenders with whom the applicant has dealt in the past or bank A/C. (Bajracharya, 2071).

3. Capital

This indicates applicant's capacity to inject his own money. By capacity analysis, it can be concluded that whether borrower is trying to play with lender's money only or is also injecting his own fund to the project. For capital analysis, financial statements, like certified balance sheet, profit and loss account is the only tools. (Bajracharya, 2071).

4. Collateral

Collateral is the security proposed by the borrower. Collateral may be of either nature movable or immovable. Movable collateral comprises right from stock, inventories to plying vehicles. In case of immovable it may be land with or without building or fixtures, plant machineries attached to it. (Joshi, 2066)

5. Conditions

Once the funding company is satisfied with the character, capacity, capital and collateral then a credit agreement (Sanction letter) is issued in favour of the Borrower stating conditions of the credit to which borrower's acceptance is accepted. (Bajracharya, 2071).

2.1.7 Principles of Sound Lending Policy

Lending constitutes the main business of a banking company. A major chunk of the profits of a bank comes out of this function. But no lending can take place without some inherent risks. As bankers are trustees of the depositors' money, they cannot take undue risks. A banker has to follow a cautious policy and conduct the business of lending on the basis of certain sound principles. Here are some of the important principles of sound lending.

Safety

The main business of banking consists in borrowing various types of deposits such as current, saving and fixed deposits and lending such deposits to needy borrowers in the form of advances and discounting of bills. This obviously implies that safety of such funds should be ensured. Otherwise the banker will not be in a position to repay his deposits and once the confidence of the depositors is shaken, he cannot carry on the banking business.

If the banker has to ensure safe lending, he has to look to the three C's of the borrower namely Character, Capacity and Capital. Character of the borrower is important because that determines his willingness to repay the loan. His capital and capacity to run the business successfully determine his capacity to pay. The safety of the loan depends on both his capacity to repay and willingness to repay.

Banks will have to keep a portion of the deposits received for honouring the demands made by the customers. Only the balance can be safely. The bank's endeavour is of course to lend as much of the deposits as possible, without which he will not be in a position to meet his interest, obligations and the maintenance of establishment. Therefore, he has to lend with a view to earn interest but lend it safe.

Liquidity

By liquidity is meant the readiness with which the bank can convert the assets into cash. Liquidity means short-term solvency of the borrower. A banker is essentially the lender of short-term funds because he knows that the bulk of his deposits are repayable on demand or at short notice. As the banker's deposits are subject to the legal obligation of being repayable on demand and at short notice, he must ensure liquidity also while lending, so that in times of need, he will be able to convert the assets into cash.

Bank can ensure high liquidity by keeping all deposits in the form of cash only. In such a case, he will not be in position to meet the interest obligations and expenditure of the establishment. From experience, he has learnt that he can safely lend out a substantial portion of the funds. But while lending he should try to ensure liquidity, i.e. in times of need, he must be able to obtain repayment of the money within a reasonably short time. Liquidity also implies that the assets can be sold without any loss. Thus the concept of liquidity has twin aspects namely quick sale ability or convert ability of the assets and the absence of risk of loss in such conversion. (Bhattarai, 2061).

Profitability

Commercial banks obtain funds from shareholders and naturally if dividend is to be paid on such shares it can only be paid by earning profits. Even in the case of public sector banks although they are service motivated they will have to justify their existence by earning profits. This is not possible unless the funds are employed profitably. From out of the revenue earned, the banker has to pay interest on deposits, salary to the staff, meet other establishment expenses, build-up reserves and the balance must permit the payment of dividend to shareholders. So for the bank to sustain on a long run, it has to seek many profitable sectors where it can mobilize its collected fund. Before lending, a banker has to see that the advance and credit is on the whole profitable. Lending rates are affected by banks' internal policy like credit rating of the borrower, bank rate of NRB, inter-bank competition and NRB's guidelines on lending rates. (Dangol & Prajapati, 2071).

Purpose of Loan

Nowadays, the purpose for which loans are granted has acquired precedence over the principle of security. If a loan is required for a non-productive or speculative purpose, a banker will be reluctant to entertain the proposal. Loans for social functions, ceremonies, pleasure trips or for repayment of prior loans are not favoured by a banker, as they are unproductive in nature. But it is very difficult for the bank to ensure that the advance has been used for the purpose for which it was taken. A person may take a loan obviously for a productive use, but may spend it on speculation. The central bank through its directives, also determines the policy to be followed by the banks with regard to the purpose for which advances may not be granted. So a banker should enquire the purpose for which it is taken for safe lending. (Shrestha, 2011).

Security

Traditionally, bankers have been security oriented. The security offered against a loan can be of various types. It may vary from a piece of land or a building to a commercial paper or bullion. Whatever may be the security, a banker has to realize that it only a cushion to fall back upon in case of need and its adequacy alone should not form the sole consideration for advance. It must be ensured that the security when accepted must be adequate, readily marketable, easy to handle and free from encumbrances. (Thapa, 2018).

Diversification of Loans

There is a very familiar saying that "Do not put all the eggs in the same basket." Banker should try to diversify loans as far as possible, so that he may minimize his risks in lending. If the banker lends only to one industry or only to few big firms or concentrates in a certain geographical area, the risk is great. He should diversify lending, so that he may not affected by the failure of one industry or of a few big borrowers. A banker who puts all his eggs in one basket is not a prudent banker. (Bhattarai, 2061).

National Interest and Suitability

Bankers must ascertain on what type of business the customer is involved whether it serves the national interest or not, whether the firm is acting responsibly towards the society that it is operating in like brick industry or the cement industry and the precautions taken by it against environment pollution. Central bank issues directives, prohibiting banks to invest in various sectors such as the import of arms and ammunitions etc. Also bankers must remain vigilant of the law and order situation where borrower carries its business. (Adhikari, 2017).

2.1.8 Some Important Banking Terms

The study in this section comprises of some important banking terms for which efforts have been made to clarify the meaning, which are frequently used in this study, which are given below.

A. Deposits

Deposit is the most important source of liquidity for a commercial bank. It is also the main source of fund that a bank usually uses for the generation of profit. Therefore, the efficiency depends on its ability to attract deposits. Banks collects the scattered savings of the public through various accounts type like saving, current, fixed etc.

Deposit being the borrowed amount from the depositors or from general public and institutions, it constitutes the liability of a bank. The management of a bank is always influencing it through deliberate policy action; the deposits of a bank are affected by various factors. They are as follows. Types of customers, Physical facilities of bank, Management accessibility of customers, Types and range of services offered by the bank. Interest rate paid on deposits. Goodwill and financial position of the bank.

In addition to the above, the prevailing economic conditions exert a decisive influence on the amount of deposit the bank receives. (Bhandari, 2005).

B. Loan and Advances

Loan, advance and overdraft are the main sources of income for a bank. Bank deposits can cross beyond a desired level but level of loans, advances and overdraft will never cross it. The facilities of granting loan, advances and overdrafts are the main services in which customer of the bank can enjoy.

Fund borrowed from bank are much cheaper than those borrowed from unorganized money lenders. The demand for loan has excessively increased due to cheaper interest rate. Furthermore, an increase in an economic and business activity always increases the demand for the fund. Due to limited resources and increasing loans, there is some fear that commercial banks and other financial institutions too may take more preferential collateral while granting loans causing unnecessary trouble to the general customers.

In addition to this, some portion of loan advances and overdraft includes that amount which is given to staff of the bank for house loan, vehicle loan, personal loan and others. In mobilization of commercial banks fund, loan advance and overdrafts have occupied a large portion. (Thapa, 2018).

C. Investment on Government Securities, Share and Debenture

"Though a commercial bank can earn some interest and dividend from the investment of government securities, share and debenture, it is not the major portion of income, but it is treated as a second source of banking business. A commercial bank may extend credit by treating it as a second source of banking business. A commercial bank may extend credit by purchasing government securities bonds and shares for several reasons.

Some of them are given as:

i) It may want to space it maturates so that the inflow of cash coincides with expect withdrawals by depositors or large loan demands of its customers.

ii) It may wish to have high grade marketable securities to liquidate if its primary reserve becomes inadequate.

iii) It may also be forced to invest because the demand for loans has decreased or is not sufficient to absorb its excess reserves.

However, investment portfolio of commercial bank is established and maintained primarily with a view of nature of banks liabilities that is since depositors may demand fund in great volume without previous notice to banks. The investment must be of a type that can be marketed quickly with little or no shrinkage in value. (Bhandari, 2005).

D. Investment on other Company's Share and Debentures

Most of commercial banks invest their excess fund to the share and debenture of the other financial and non-financial companies. Due to excess funds but least opportunity to invest those funds in much more profitable sector and to meet the requirement of NRB directives, the commercial banks purchase shares and debenture of regional development bank, NIDC and other development banks. (Thapa, & Rana, 2011).

E. Liquidity

Liquidity is the ability of bank to meet its obligations on time, especially in relation to repayment of inter-bank borrowings and customer deposits. Liquidity management is a very crucial job of commercial bank and the bank should maintain adequate amount of cash in its vault and NRB for its daily operation and administrative purpose. As per the arrangement of NRB effective from fiscal year 2008/09, the commercial banks are required to maintain cash reserve of 5% with NRB of its total deposit liability with NRB. The previous provision of cash in vault maintenance has been withdrawn now. (Bhandari, 2005).

F. Capital Adequacy

Capital is the blood of any business without which business cannot be run or established. In financial term, capital is the excess of assets over liabilities and can be defined as the wealth, which is employed for the production. Capital is required by a bank as a cushion to absorb losses, which should be borne by shareholders rather than depositors and to finance the infrastructure of the business. Capital adequacy is to maintain adequate amount of capital or fund to safeguard the money of the depositors against any possible loss. NRB requires banks to maintain a certain capital adequacy ratio based on the total risk weighted assets and the banks are supposed to meet the minimum requirement of CAR. (Joshi, 2066).

G. Off-Balance Sheet Activities

Off balance sheet activities involve contracts for future purchase or sale of assets and all these activities are contingent obligations. These are not recognized as assets or liabilities on balance sheet. Some examples of these items are letter of credit, letter of guarantee, bills of collection etc. These activities are very important, as they are the good source of profit of bank though they have risk. Nowadays, some economists and finance specialists to expand the modern transactions of a bank stressfully highlight such activities. (Bhattrai, 2061).

H. Banking Risks

Normally, banks confront different kinds of risks, which are categorized as follows:

Credit Risk: Credit risk arises whenever another party enters into an obligation to make payment or deliver value to the bank. This risk is mostly associated with the lending.

Liquidity Risk: Liquidity risk arises when bank itself fail to meet its obligation. The bank required to make payments to the different parties at different times, when they fall due to other parties, it is the liquidity risk.

Yield Risk: It is the risk that bank's assets may generate less income than expense generated by its liabilities.

Market Risk: The risk of loss resulting from movements in the market price of financial instruments in which the bank has a position is the market risk. Such instruments include bonds, equities, foreign exchange and associated derivative products.

Operational Risk: The risk of failure in the banks procedures or controls, whether from external or internal causes or as a result of error or fraud within the institution is the operational risk.

Ownership/Management Risk: The risk that shareholders directors or senior management be unfit for their respective positions or dishonest.

2.1.9 Project Appraisal

Before providing credit to the customer, bank makes analysis of project from various aspects and angles. It will help the bank to see whether project is really suitable to invest. The purpose of project appraisal answers the following questions: Is the project technically sound? Will the project provide a reasonable return? Is the project in line with the overall economic objectives of the economy?

Generally, the project appraisal involves the investigation from the following aspects (Gautam, 2004: 258): Financial aspect, Economic aspect, Management/Organizational aspect, Legal aspect.

2.1.10 Provision of NRB for Extending Advances & Investment in Productive, Priority and Deprived Sector

Productive Sector

Productive Sector include advances to Priority Sector and Other Productive Sector which includes advances and investment in shares and debentures of small, medium and large industries as defined in industrial enterprises act; pre-shipment credit like purchase of merchandise, processing, assembling, packaging etc.; export bill financing, advances for purchase of public transport like truck, bus, tempo etc. and agricultural /farm equipment; investments on shares and debentures of government/ semi-government or private sector agricultural insurance, go down, banking or like companies etc. As per NRB regulation, commercial banks are required to extend 40% of the total advances to productive sector, which also includes 12% to priority sector including deprived sector.

Priority Sector Credit Program

"Priority sector" is defined to include micro and small enterprises which help increase production, employment and income as prioritized under the national development plans with an objective to uplift the living standard of general public particularly the deprived and low income people by progressively reducing the prevalent unemployment, poverty, economic inequality and backwardness. Micro and small enterprises are classified into agricultural enterprises, cottage and small industries and services. In addition, other businesses as specified by NRB from time to time are also

included under Micro and small enterprises. All credits extended to priority sector up to the limit specified by NRB are termed as "Priority Sector Credit."
NRB has provided the requisite proportion of Priority Sector lending as follows:

Table 2.1: NRB Requirement of Priority Sector Investment

Fiscal Year	**Minimum percent of Total Credit to be invest in Priority Sector from commercial bank (%)**
2013/14	20
2014/15	20
2015/16	20
2016/17	25
2017/18	25
2018/19	25
2019/20	25
2020/21	25
2021/22	25
2022/23	25

(*Source: NRB Directives*)

Nepal Rastra Bank (NRB) has been promoting micro financing and expanding financial access and inclusion to achieve its objectives of economic stability and sustainable development. In 1974, NRB introduced small sector lending as a directed credit. It was a special type of lending designed for the economic upliftment of the deprived sector and was later renamed priority sector lending. Some two decades after priority sector lending was launched, NRB issued a directive to banks to extend certain a percentage of credit to the deprived sector. Likewise, replicating the Grameen Credit Model, the government of Nepal established five Grameen Bikash Banks in partnership with NRB between 1990 and 1996. A wholesale lending micro financing model was set up with the establishment of Rural Microfinance Development Centre in 1998.

Deprived Sector Lending

"Deprived Sector" includes low income and particularly socially backward women, tribes, lower caste, blind, hearing impaired and physically handicapped persons and squatters (sukumbasi) family. All credits extended for the operation of self-employment oriented micro-enterprises for the upliftment of economic and social status of deprived sector up to the limit specified by NRB is termed as "Deprived Sector Credit". "Deprived Sector Credit" is considered as integral part of priority sector credit and this credit comprise micro-credit programs and projects also.

The businesses under the Priority Sector Credit Program have been classified under the following four major heads: Agriculture and Agro-bases business, Cottage and small industries, Services, Other business.

The ratio of loans extended by commercial banks, development banks and finance companies to the deprived sector was maintained at a minimum of 5 percent, 4.5 percent and 4 percent respectively. From the fiscal year 2017-18, the ratio was raised to 5 percent. Banks and financial institutions (BFIs) are incentivized to go to remote areas outside the district headquarters without bank branches. Microfinance institutions are encouraged to expand their branches in the high hill and mountain regions. Special refinance facility has been continued for cottage and small industries, Dalits, differently-able individuals, disadvantaged and minority communities who run small business.

Lending in Deprived Sector will be included in Priority Sector for the purpose of compliance test for 12% credit to Priority sector.

Deprived sector credit is advances up to Rs. 30, 000 per borrower family meant for weak, poor and deprived people extended in the following manner by the commercial banks shall qualify to be included under deprived sector credit:

i) Direct investment made by the commercial banks themselves in income generating employment oriented programs.
ii) Investments made by commercial banks in share capital of Rural Development Banks, Rural Micro Finance Development Centre and other Development Banks established with an objective to extend credit to deprived sector.
iii) Advances to the Rural Development Banks and other Development Banks engaged in the similar poverty alleviation programs.
iv) Advances to Cooperatives, Non-governmental Organization and Small Farmers Cooperatives approved by NRB for carrying out banking transactions.
v) Advances to Micro-Finance Institutions/(Rural Development Banks and other

financial institutions, cooperatives and non-governmental organizations approved by NRB for intermediation) stipulating the condition to disburse such credit to deprived sector only.

vi) Loans extended by commercial banks to development banks engaged in micro credit activities with stipulated condition to disburse the credit only to the deprived sector up to Rs. 30,000 a family shall be eligible for the purpose of inclusion under Deprived Sector Credit.

Effective from FY 2000/01, Nabil and HBL shall compulsorily extend advances to the deprived sector by 3% of its total outstanding credit while new commercial banks are required to invest 0.25% of total outstanding credit to the deprived sector (Source: NRB Directives, (074/75).

Regulation relating to Loan Classification and Loan Loss Provisioning

With an objective to minimize the possible loss of credits extended by commercial banks as provided under section 23 (1) of Nepal Rastra Bank Act 2058 (with amendment) relating to development and regulation and banking system. This directive in respect of loan classification & provisioning has been issued in exercised of authority under section 56 of bank and financial institutions act 2073.

Classification of Outstanding Loan and Advances on the Basis of Aging

Banks shall classify outstanding principal amount of loan and advances on the basis of aging.

Classification of Loans and Advances

Loan and advance shall be classified into the following 4 categories:

2.1.11 PASS

Loans and Advances whose principal amount are not past due for a period up to 3 (three) months shall be included in this category. These are classified and defined as performing Loans.

Watch list

All loans and advance that overdue up to 3 months shall be included in this category.

Substandard

All loans and advances that are past due for a period of 3 months to 6 months shall be included in this category.

Doubtful

All loans and advance which are past due for a period of 6 months to 1(one) year shall be included in this category.

Loss

All loans and advances which are past due for a period of more than 1(one) 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.

Loans and advances failing in the category of sub-standard doubtful and loss are classified and defined as Non-Performing Loan.

Note:

i) If it is appropriate in the views of the Bank management, there is not restriction in classifying the loan and advances from low risk category. For instance, loan falling under sub-standard may be classified into Doubtful or loss and loans falling under Doubtful may be classified into loss category.

ii) The term loan and advances also includes Bills purchased and Discounted.

Submission of Return Relating to Classification of Loan and Advances

Bank shall, as of the Mid of October, January, April and July, prepare the statement of outstanding loans & advances classified on the basis of aging & submit the particulars as per the enclosed Directives Form No. 3 to the Banking Operation Department & Inspection & Supervision Department of Nepal Rasta Bank within 1(one) month from the end of each quarter. Classified Loans and Advances under the currently existing arrangement are required to be classified as per the Time Table in four phases:

Relating to Collateral

All collateral used back loan & advance shall be adequate to cover up the principal and interest and shall also be legally secured. In the event of non-realization of principal and interest of loan, there must be no difficulty in acquiring the title of the collateral asset.

Additional Arrangement in Respect of Pass Loan

Loans & advances fully secured by gold, silver, fixed deposit receipts and NG securities shall be included under “pass” category.

However, where collateral of fixed deposit receipt or NG securities or NRB Bonds is placed as security against loan for other purposes, such loans has to be classified on the basis of aging per clause 2.

Additional Arrangement in Respect of "Loss Loan"

Even if the loan is not past due, loans giving any or all of the following discrepancies shall be classified as "Loss".

i) No security at all or security that is not in accordance with the borrower's agreement with the bank,

ii) The borrower has been declared bankrupt,

iii) The borrower is absconding or cannot be found,

iv) Purchased or discounted bills are not realized within 90 days from the due date.

v) The credit has not been used for the purpose originally intended.

vi) Owing to non- recovery, initiation as to auctioning of the collateral has passed six months and if the recovery process is under litigation.

vii) Loans provided to the borrowers included in the black list and where the Credit Information Bureau blacklists the borrower.

viii) Additional Arrangement in Respect of Term Loan

In respect of term loans, the classification shall be made against the entire outstanding loan on the basis of the past due period of overdue instalment In the event of conversion of continent liabilities of the bank e.g. letters of credit, un-matured guarantees, in to the liability of the bank, such amount becomes recoverable from the customers. Hence, such amount shall also be classified as per the classification norms applicable to loans & advances & accordingly be provided with requisite provisioning.

Prohibition to Recover Principal and Interest by Overdrawing the Current Account & Exceeding the Overdraft Limit Principal and interest on loans & advances shall not be recovered by overdrawing the borrower's current account or where overdraft facility has been extended, by overdrawing such limit. However, this arrangement shall not be construed as prohibitive for recovering the principal & interest by debiting the customer's account & recovery is made as such resulting in overdraft, which is not settled within one month, such overdrawn principal amount shall also b liable to be included under the outstanding loans & such loans shall be liable to be included under the outstanding loan and such loan shall be downgraded by one step from its current classification. In respect of recognition of interest, the same shall be as per the clause relating to income recognition mentioned in Directives No. 4. NRB Directives, (2075).

Loan Loss Provisioning

The Loan loss provisioning, on the basis of the outstanding loans & advances and purchase classified as per this Directives, shall be provided as follows:

Classification of Loan	Time Period	Loan Loss Provision
Pass	Not overdue/overdue up to 1 month	1 percent
Watch List	Overdue up to 3 months	5 percent
Substandard	Overdue up to 6 months	25 percent
Doubtful	Overdue up to 1 year	50 percent
Loss	Overdue for more than 1 year	100 percent

Loss loan provision set aside for performing loan is defined as "general loan loss provision" and loan loss provision set aside for Non-performing loan is defined as "Specific Loan Loss Provision". NRB Directives.

Additional Provisioning in the case of Personal Guarantee Loans

Where the loan is extended only against personal guarantee, a statement of the assets equivalent to the personal guarantee amount not claimable by any other shall be obtained. Such loans shall be classified as per above and where the loans fall under the category of Pass, Substandard and Doubtful, in additional to the normal loan loss provision applicable for the category, an additional provision by 20% point shall also be provided. Classification of such loans and advances shall be prepared separately.

Rescheduling and Restructuring of Loan

In respect of loans & advances falling under the category Substandard, Doubtful or Loss, banks may reschedule or restructure such loans only upon receipt of a written Plan of Action from the borrower citing the following reason:

i) The internal and external causes contributing to deterioration of the quantity of loan.
ii) The reduced degree of risk inherent to the borrower/enterprise, determined by analyzing its balance sheet and profit & loss account in order to estimate recent cash flows & to project future ones, in addition to assessing market conditions.
iii) Evidence of existing of adequate loan documentation.
iv) An evaluation of the borrower/ enterprise's management with particular emphasis on efficiency, commitment & high standards of business ethics.

In addition to written Plan of Action for rescheduling or restructuring of loan per Clause (13.1) above, payment of interest according to the loan contract as originally specified should have been collected. The loan loss provisioning, in respect of rescheduled, restructured and swap loans, shall be provided at minimum 12.5%. Separate statement shall be prepared for loans classified & provision made as per Clause 13.3 above.

Provisioning against Priority Sector Credit

Full provisioning as per clause (11) shall be made against the uninsured priority and deprived sector loans. However, in respect of insured loans; the requisite provisioning shall be 25% of the percentage state under clause (11).

Adjustment in Provisioning

Except in the following cases, banks are prohibited from making any adjustments in their loan loss provision amount:

i) The loan has been completely written off:

ii) The principal amount of loan and interest has been fully settled by the borrower.

iii) Loan has been classified or reclassified and vision for loan loss is made.

However, no such adjustments shall be made in the case of reclassified loan by way of rescheduling or restructuring.

Action to be taken in cases of Noncompliance

In cases where a bank has been found not complying the regulations in respect of loan classification and provisioning, Nepal Rastra Bank may ask for clarification. If the bank's response is not satisfactory, Nepal Rastra Bank shall initiate following action in exercise of its authority under section 23 (1) of Nepal Rastra Bank Act. 2012.

Require reclassification of loan and advances and accordingly adjust the loan loss provisioning within 3 months. If the banks do not comply to the directive issued as per Sub-Clause 16.1 above, the following additional action shall be initiated in exercise of the authority under section 32 of Nepal Rastra Bank Act 2012 with amendment:

i) Suspend declaration and distribution of dividends (including bonus shares)

ii) Suspend extension of loans

iii) Suspend acceptance of deposits

All earlier circulars issued by Nepal Rastra Bank relating to loan classification and loan loss provisioning have been repealed.

2.2 Theoretical Review

A theoretical framework consists of concept and, together with their definitions and reference to relevant scholarly literature, existing theory that is used for your particular study. The theoretical framework must demonstrate an understanding of theories and concepts that are relevant to the topic of your research paper and that relate to the broader area of knowledge being considered.

Credit is the amount of money lent by the creditor (bank) to the borrower (customers) either on the basis of security or without security. Sum of the money lent by a bank, is known as credit (Oxford Advanced Learners Dictionary, 1992:279). Credit and advances is an important item on the asset side of the balance sheet of a commercial bank. Bank earns interest on credits and advances, which is one of the major sources of income for banks. Bank prepares credit portfolio, otherwise it will not only add bad debts but also affect profitability adversely, (Varshney and Swaroop, 1994:6).

2.2.1 Credit Risk

Risk means the exposure to a change of loss or damage. Risk is the element of uncertainty or possibility of loss that exist in any business transaction. Credit risk is the likelihood that a borrower or counter party will be un successful to meet its Obligation in accordance with agreed and conditions. Wikipedia dictionary

Credit Risk means the risk of credit loss those results from the failure of a borrower to honor the borrower's credit Obligation to the financial institution. (Guideline on credit risk management, Bank of Mauritius). Credit risk is most simply defined as the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms. Basel Committee on Banking Supervision, 2002.

2.2.2 Credit Risk Management

A bank's risk have to be identified before they can be measured and managed. Typically banks distinguish the following risk categories: Credit risk, Market risk, Operational risk.

Measurement

The consistent assessment of the three type of risks is an essential prerequisite for successful risk management. While the development of concepts for the assessment of market risks has shown considerable progress, the method to measure credit risks and operational risk are not as sophisticated yet due to the limited availability of historical data.

Calculation of credit risk

Credit risk is calculated on the basis of possible losses from the credit portfolio. Portfolio losses in the credit business can be divided into expected losses and unexpected losses. Credit Approval Process and Credit Risk Management, 2005, Oesterreichische National Bank.

Expected losses are derived from the borrower’s expected probability of default and the predicted exposure at default less the recovery rate, i.e. all expected cash flows, especially from the realization of collateral. The expected losses should be accounted for in income planning and included as standard as risk costs in the credit conditions.

Unexpected losses result from deviations in losses from the expected loss. Unexpected losses are taken into account only indirectly via equity cost in the course of income planning and setting of credit conditions. They have to be secured by the risk coverage. Credit Approval Process and Credit Risk Management, 2005, Oesterreichische National Bank.

2.3 Empirical Review

The empirical study of literature attracts scholarship particularly in the areas of reception and audience studies and in cognitive psychology when it is concerned with questions of reading. In these two areas research and studies based on the framework are steadily growing. Further fields where the framework in various revised and expanded versions attracts scholarship is (comparative) cultural studies and pedagogy. (Wikipedia)

Despite the doom and gloom associated with new technology, people will never be completely replaced but as the world of work changes we will have to make sure that the people we do have in our teams are retained, developed and engaged otherwise as the world gets smaller and the working population decreases, as the 'Baby Boomers' retire, competition for our people will increase as they search for the ‘making a difference’, ‘more fulfilling’ job. If we don't do more the credit profession will slowly become back-office once again. (Sanders, 2018)

2.3.1 Review of Related Studies

2.3.2 Review of Journals and Articles

Berrios (2015) in his research article on *"The Relationship between bank credit risk and profitability and liquidity"* has analyze the relationship between bank credit risk and financial performance and the contribution of risky lending to lower bank profitability and liquidity. The sample data comes from the Emergent Online database, which stores ownership, executive, and financial information about public and private companies. The methodology adopted in this study was covariance models include net interest margin, return on assets, return on equity, and cash flow to assets. The study found that a negative relationship between less prudent lending (which may be interpreted as a positive effect of more prudent lending) and net interest margin. However, findings were only statistically significant when the normality assumption was relaxed through the robust regression method. Insider holdings and longer chief executive officer tenure were negatively related to bank performance. This may be a consequence of an adverse effect of the agency problem.

Kagoyire and Jomo (2016) conducted an Article of *"Effect of Credit Management on Performance of Commercial Banks in Rwanda (A Case Study Of Equity Bank Rwanda LTD)",* He emphasized Credit management is one of the most important activities in any company and cannot be overlooked by any economic enterprise engaged in credit irrespective of its business nature. Sound credit management is a prerequisite for a financial institution's stability and continuing profitability, while deteriorating credit quality is the most frequent cause of poor financial performance and condition. As with any financial institution, the biggest risk in bank is lending money and not getting it back. The study sought to determine the effect of credit management on the financial performance of commercial banks in Rwanda. The study adopted a descriptive survey design. The target population of study consisted of 57 employees of Equity bank in credit department. Entire population was used as the sample giving a sample size of size of 57 employees. Purposive sampling technique was used in sampling where the entire population was included in the study. Primary data was collected using questionnaires which were administered to the respondents by the researcher. Descriptive and inferential statistics were used to analyze data. The study found that client appraisal, credit risk control and collection policy had effect on financial performance of Equity bank. The study established that there was strong relationship between financial performance of Equity bank and client appraisal, credit risk control and collection policy. The study established that client appraisal, credit risk control and collection policy significantly influence financial performance of Equity bank. Collection policy was found to have a higher effect on financial performance and that a stringent policy is more effective in debt recovery than a lenient policy. The study recommends that Equity bank should enhance their collection policy by adapting a more stringent policy to a lenient policy for effective debt recovery.

Pradhan (2016) in his article on *"Impact of Liquidity on Bank Profitability in Nepalese Commercial Banks"*. Has examines the effect of liquidity on the performance of Nepalese commercial banks. Investment ratio, liquidity ratio, capital ratio and quick ratio are the independent variables used in this study. The dependent variables are return on equity (ROE) and return on assets (ROA), while one year lagged variables for independent variables are also used to determine the more specific result of the previous year’s effect on the current years ROE and ROA. The secondary sources of data have been used from annual reports of the banks and supervision report of Nepal Rastra Bank. The regression models are estimated to test the significance and effect of bank liquidity on performance of Nepalese commercial banks. Correlation between capital ratio and return on equity found to be positive indicating higher the capital ratio higher would be the return on equity. However, the correlation between return on equity and liquidity ratio is found to be negative indicating higher the liquidity in the bank lower would be the return on equity. Further, the correlation is found to be negative for quick ratio with return on equity. Beta coefficients for investment ratio and capital adequacy are positively significant with bank performance, which indicate that increase in investment ratio and capital ratio leads to increase the performance of the banks. However, beta coefficients for liquidity ratio and quick ratio are negative with return on assets and return on equity indicating increased liquidity ratio and quick ratio decreases the return on assets and return on equity of the bank.

Malla (2017) in his article on "Credit Portfolio Management in Nepalese Commercial Banks" has describe Credit portfolio management as a key function for banks (and other financial institutions, including insurers and institutional investors) with large, multifaceted portfolios of credit, often including illiquid loans (Nario, Pfister, Poppensieker & Stegemann, 2016). After global financial crisis of 2007-2008, the credit portfolio management function has become most crucial functions of the bank and financial institutions. The Basel III, third instalment of Basel accord was developed after crisis to strengthen bank capital requirements by increasing bank liquidity and decreasing bank leverage that encourages banks to measure credit risk of bank's portfolios. The Basel committee also raises an issue concerning the application of the risk weights used in the capital adequacy framework to determine exposure to risk assets for the purpose of determining large credit exposure. The portfolio management of the Nepalese banking sector has been improved remarkably during last 10 years due to the strict regulation of Nepal Rastra Bank. This journal will try to describe the present credit portfolio management practice of Nepalese commercial banks by using qualitative and quantitative methods. In this study, concentration of banks for credit portfolio management has been studied by analyzing security wise loan, product wise loan and sector wise concentration of loan where the researcher has found assorted outcomes. This research also aims to provide some suggestions to overcome with problems associated with credit portfolio.

Subedi (2017)in his article titled "Growth in Major Commercial Banks" has compared between the first six month of the fiscal year 2002-03 and 2003-04, has shown that there has been noticeable increase in credit outflow by the commercial banks except of Nepal Bank Ltd (NBL) and Rastriya Banijya Bank (RBB) (the government owned banks). There has been increase in credit-deposit (CD) ratios of all commercial banks except of NBL and RBB in which case it has gone down by 10.41% and 5.99% respectively. It may be because their concentration was only on recovery of the huge Non Performing Assets (NPA). However, Mr. Subedi pointed out that no matter what the size of NPA is and the circumstances are, each bank has to collect the deposit in order to create a lending and to invest in the new ventures. Except RBB all banks have increment in deposit collection.

2.3.3 Review of Previous Thesis

Gautam (2012) conducted on *A Study on Financial Performance of Nepal Bank Limited.* has made following objectives and major findings.

Objectives

- To evaluate the bank's efficiency to face the challenges and measure the comparative financial strengths and weakness.
- To analyze the bank's performance under priority sectors of government.
- To analyze income and expenditure and to provide suggestions and recommendations to the bank.

Major Findings

The bank is seemed to be unable to utilize its high cost resources in high yielding investment portfolio. The only positive aspect is, if risk can be managed, percentage of loans and advances on total deposits has increased. Long -term debts, total debts and total deposit ratios have gradually decreased. It indicates that bank has not followed any policy regarding these items. The bank has experienced negative EPS and P/E ratios which have also heavily fluctuated during the study periods. Thus, it can be said that the financial position of the NBL is worse due to its failure to utilize its resources efficiently and due to its inefficiency in risk management.

Rouniyar (2013) conducted on *Liquidity & profitability Analysis of Listed of Four Commercial Banks (with reference to NABIL, SCBNL, EBL and SBI).* has made following objectives and major findings:

Objectives:

- To assess the profitability and liquidity position of the commercial banks,
- To evaluate the relationship between selected dependent and independent variables regarding liquidity and profitability of the banks.

Major findings:

From the ten years' analysis i.e. fiscal year 2001/02 to 2010/11 return on equity is highest of SCBNL and lowest of SBI among the four sample banks. SBI has riskier than other sample banks. In the same way, return on capital fund or employed to risked assets for SBI is more volatile than other sample banks. SBI has not managed its profitability to maintain capital adequacy than other sample banks. NABIL is more uniformity which has less CV than others. Net profit to total deposit ratio for the bank is satisfactory i.e. well management in earning profit. Net profit to total loan and advances ratio is highest of SCBNL.

Shrestha (2014) conducted on *"Liquidity and Credit Management Practices of Commercial Banks In Nepal"*. Researcher has taken two sample of banks Viz; Nepal Investment bank Ltd. and Nepal Credit and Commerce bank Ltd. and had made following objectives and major findings.

Objectives :

- To analyze the trend of liquid assets maintained by the commercial banks.
- To evaluate the cash reserve ratio maintained by the NIBL and NCC.
- To analyze the credits and advances provided by the NIBL and NCC.
- To find out the strengths and weaknesses in the credit position of NIC and NCC.

Major Findings:

- The analysis of the trend of liquid assets maintained by banks shows NIBL in a better position than NCC.
- The analysis of the credit management of the commercial banks shows the overall strength of the department in maintaining a healthy relationship between various variables in the credit sector. This includes the relationship of the total loans and advances with total deposits, net profit, total liquid assets and total non-performing loans. These relationships are measured by their correlation coefficients.
- The relationship between total credit and total deposit shows highly significant positive correlation. This indicates that the total deposit has increased with the increase in the total credit provided by the commercial banks, thus, strengthening their credit and liquidity positions.
- The relationship between total credit and net profit also shows a significant positive correlation. This indicates that the total credit provided has been contributing in increasing the net profit of the company. This, in turn, suggests the effective management of credit in earning high interest income and reducing the chances of credit defaults.
- The relationship between the total credit and total liquid assets also shows a highly significant positive correlation among them. This indicates that the banks have been effective in balancing the liquidity of the banks with their need to

provide loans and advances.

Nepal (2015) has conducted on the topic of *Credit Management of Commercial Banks in Nepal* has following objectives and major findings:

Objectives:

- To assess the credit practices of selected Nepalese commercial banks.
- To explore the credit efficiency, analyze the industry environment and management quality in terms of credit practices
- To explore the relationship with loan and advances, NPA and Net profit

Major findings:

- Repayment is satisfactory in agro based industry and production sector compared to other sectors.
- Management quality and credit efficiency of selected banks found satisfactory as they have standard credit practices
- Credit disbursement and repayment has significant relationship. Flow of new credit depends upon the recovery status.

Maharjan (2016) conducted on *Financial Performance analysis of Commercial Banks of Nepal* has made the following objectives and major findings.

Objectives:

- To analyze the trend of liquid management by the commercial banks.
- To evaluate the cash reserve ratio maintained by the NABIL and HBL.
- To analyze the total loan and advances, total investment provided by the NABIL and HBL.

Major Findings:

- The liquidity position of NABIL is very strong while HBL have strong capacity to meet the short term obligations.
- HBL have invested significant portion of deposit to total investment than other.
- Total deposit, investments and loans and advances of all banks are in increasing trend.
- The trend line of loan and advances for both banks is upward slopping which refers to the increase in the disbursement of loan and advances.
- NABIL is successful in optimizing the assets mobilization due to its highest ROA than HBL.
- Liquidity management practice is still in developing phase in Nepal.

Khadka (2017) conducted on *A Study on Lending Performance (with reference to NABIL, and SCBNL Bank).* has made following objectives and major findings:

- To evaluate the portion of nonperforming loan and the level of NPAs in total deposit and total lending of selected commercial banks.
- To analyze the impact of nonperforming assets in the profit of commercial banks.
- To study the loans amount provided by the commercial banks.

Major Findings:

- The ratio NPL to loan and advances of both banks is defining but the rate of declining in the same ratio in NABIL and SCBNL. Likewise, the management of NABIL has been able to reduce NPL sharply than SCBNL even though the average loan and advances of NABIL bank is higher than SCBNL.
- This NPL to total deposit ratio is also gradually decreasing. This ratio of SCBNL is lower than the NABIL. Average deposit collection of SCBNL is higher than the NABIL.
- The LPP to total NPL ratio of both banks are fluctuating. It means increasing some year then decreasing. The greater fluctuation is seen in NABIL bank than SCBNL.
- The major profit of commercial banks is earned from the interest by disbursing loan and advances. It means that net profit indicates the performance of loan. the ratio of net profit to total loan and advances of SCBNL is higher than NABIL.

Dhakal (2018) has conducted his study entitled *"A Study on Credit Risk Management of Standard Chartered Bank Nepal Limited and Rastriya Banijya Bank".* has made following objectives and major findings:

- To find the status and growth of non performing loan, total loan and loan loss provision of the respective bank
- To see the investment and loan and advance system of Standard Chartered Bank Nepal Limited and Rastriya Banijya Bank.
- To analyze the profitability of banks in receptiveness of liquidity assets and management efficiency.
- To see the credit practices of banks.

Major Findings:

- Industrial development in Nepal is not good due to load shedding at this time. So, it has directly affected the lending policy of commercial banks.
- For effective credit management and consumer's service, both banks have been making great effort for the development and empowerment of employees by conducting various training related to credit management and customer service.
- SCBNL has maintained higher credit and advances to total deposit. It shows that the bank seems to be strong to mobilize its total deposit as credit and advance.

Ghimire (2019) has submitted a thesis entitled *"A Study on Credit Management of Joint Venture Commercial Bank with reference to NIBL and BOK".*has made following objectives and major findings:

- To see the credit practices of the sample banks.
- To examine the efficiency of the bank.
- To find out the strength and weakness in the credit administration of the two banks.

Major Findings:

- Cash and bank balance to total deposits ratio of NIBL and BOK is 11.9% and 9.4% respectively.
- BOK has maintained higher credit and advances to total deposit. It shows that BOK seems to be strong to mobilize its total deposit as credit and advances.
- The correlation coefficient of total deposits with total credit and advance is found highest degree of positive correlation for both banks.
- NIBL and BOK both banks have position of decreasing the utilization of loan and going toward utilization of its own equity and minimizing the risk.
- P/E ratio of both banks is in increasing-up rate. The average P/E ratio of NIBL is higher than BOK.

Karki (2020) has conducted a thesis entitled *"A Study on Credit Management and Analysis of Commercial Banks (Everest Bank Limited)"* To study the credit policy and credit analysis systems prevailing in the bank. has made following objectives and major findings:

Objectives :

- To gain acquaintance of loan recovery process regarding credit management.
- To examine lending efficiency and its contribution to profit.
- To make suitable suggestions based on the findings of this study.

Major Findings:

- Total credit of FY 2015/016 and FY 2019/020 has been divided into performing and non-performing assets. Increment in performing assets by NPR 1780.2 million and decline in sub-standard loan and doubtful loan by NPR 6.67 million and NPR 38.51 million respectively as compared to FY 2005/06 which can be interpreted as a positive sign. However bad loan has increased by NPR 69.24 million. Therefore Bank must focus and concentrate in reducing such bad loan**.**
- Liquidity of EBL is not adequate. It is unable to maintain its liquidity position at standard level as the current ratio in last two years is below the required standard level i.e. 2:1.
- Debt equity ratio of EBL shows that it is moving towards higher trend, which indicates owners are investing less resource of their own. This reveals danger to the creditors, as during period of low profit, a highly debt-financed company cannot even pay the interest of creditors.
- Return on equity of EBL is the highest in the year 2015/020 which means the effectiveness of the bank and also depicts that bank has been successful in mobilizing its owner’s fund in an efficient manner.

2.4 Research Gap

Since the above mentioned studies offer limited findings, more extensive testing , and adjustment of necessary variables are needed in ordered to be more conclusive about the credit Management. Previous studies were directed to find the effect of the credit management of different commercial banks. Similarly, Joshi's study is unable to present the exact condition of credit management in Nepalese banking sector Nepal.

Presently, this study aims to attempt to study about credit management of Nepalese commercial banks in Nepal. The previous relevant literature related to banking business has just reviewed to support the study. In Joshi's study, he failed to study the perfect credit management of Nepalese commercial banks. This study tries to fulfill this weakness. And there is also less research made in this topic especially in banking sector. Credit Management has very big role to sustain any banking business. It is equally important to identify the relation of performance of the banking business. So, it tries to assess the credit management of banking sector and by providing the proper atmosphere for the banking market in our country. The present study is based on five years data of commercial banks, which tries to achieve its objectives by analyzing secondary source of data. Thus, the earlier studies on these issues need to be updated and validated because of the many changes taking place in Nepalese banking sector.

CHAPTER III
RESEARCH METHODOLOGY

3.1 Introduction

Research simply means to search again and again. It is a systematic activity to achieve truth or finding solution to a problem. It is a process of a systematic and in-depth study or research of any particular topic, subject or area of investigation backed by the collection, compilation, presentation and interpretation of relevant details or data. Methodology is the research method used to test the hypothesis. So the research methodology refers to the overall research process, which a researcher conducts during his/her study. "The purpose of research is to discover answers to questions through the application of scientific procedures. The main aim of research is to find the truth which is hidden and which has not been discovered at yet." (Kothari, 2007:7) The basic framework of this study is descriptive as well as exploratory. In order to reach and accomplish the objectives of this 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. (Kothari, 2007:7).

3.2 Research Design

This study is based on recent historical data. Mostly, secondary data and information were collected, evaluated, verified and synthesized to reach a conclusion. To achieve the objective of this study descriptive data different journals and articles relevant with the study, annual reports of different fiscal years of concerned banks, NRB Directives, banking and financial statistics report published by NRB and other related materials were collected and studied. The help of study adopts descriptive research design.

3.3 Population and Sample

There are altogether 27 commercial banks functioning all over the country at present, which are taken as a population of this study work. Among them, this study comprises only two commercial banks namely; Laxmi Bank Limited Ltd and Siddhartha Bank Limited, which have been selected as a sample by using random sampling method for this study.

3.4 Sources of Data

This study is based on secondary data. Secondary data are extracted from published annual reports of the bank, published articles, journals, reports, books, documents, news paper, thesis, previous related studies etc.

3.5 Method of Data Analysis

In this study, various financial, mathematical as well as statistical tools have been used to make the analysis more convenience, reliable and authentic too.

3.5.1 Financial Tools

Financial tools are used to examine the financial strength and weakness of the bank. In this study, following financial tools are used:

Loan Classification and Provisioning:

The amount of loans in the various categories has been calculated by using the models of NRB. Likewise, for each category, the actual loan loss provisioning amount has also been calculated according to the directions laid down by NRB.

Liquidity Ratio:

Liquidity ratios measure the firm's ability to meet current obligations. In fact, analysis of liquidity needs the preparation of cash budgets and cans and fund flow statements; but liquidity ratios, by establishing a relationship between cash and other current assets to current obligations, provide a quick measure of liquidity. A firm should ensure that it does not suffer from lack of liquidity, and also that it does not have excess liquidity. According to the NRB requirement, the bank has to maintain at least 5% of its total deposit liability as a balance with NRB. The prior provision of Statutory Liquidity Ratio (SLR) and vault reserve has been fully removed now.

The following ratios are evaluated under liquidity ratio:

1) Current Ratio = $\frac{\text{Current Assets}}{\text{Current Liabilites}}$

2) Cash & Bank Balance to Current Assets Ratio = $\frac{\text{Cash \& Balance Balance}}{\text{Current Assets}}$

3) Loans & Advances to Current Assets Ratio = $\frac{\text{Loan \& Advances}}{\text{Current Assets}}$

4) Investment on Govt. Securities to Current Assets Ratio

$$= \frac{\text{Investment on Goverment Securities}}{\text{Current Assets}}$$

Investment Portfolio and Policy:

In order to make profits, banks must invest the funds collected from depositors in various productive sectors and different form of earning assets. Though the bank may have its own policy and theory of investment, it also has to look upon the criteria or requirement defined by NRB before making any investment decisions. Just like minimum requirement of investment to be made in productive, priority and deprived sector, regulation relating to investment in shares and securities by commercial banks etc.

The following ratios are evaluated for finding out investment portfolio and investment policy of subjected banks:

1) Total Investment to Total Deposit Ratio = $\frac{\text{Total Investment}}{\text{Total Deposits}}$

2) Loan & Advances to Total Deposit Ratio = $\frac{\text{Loan \& Advances}}{\text{Total Deposit}}$

3) Loans & Advances to Total Working Fund = $\frac{\text{Loan \& Advances}}{\text{Total Working Fund}}$

4) Total Investment to Total Working Fund = $\frac{\text{Total Investment}}{\text{Total Working Fund}}$

3.5.2 Statistical Tools

Several numbers of statistical tools can be employed to examine the financial data of SBL and LBL. Some of the statistical tools that are used for the purpose of this study are presented below;

Arithmetic Mean

Most of the time when we refer to the "average" of something, we are talking about its arithmetic mean. To find out the arithmetic mean, we sum the values and divide by the number of observations. The mean can be calculated as;

$$\text{Mean } (\overline{X}) = \frac{\sum X}{N}$$

Where, $\overline{X}$ = Mean

$\sum X$ = Sum of all variables

N = Number of variables involved

Standard Deviation

The standard deviation is the square root of the average of the squared distances of the observations from the mean. It enables us to determine, with a great accuracy, where the values of a frequency distribution are located in relation to the mean. To compute the sample standard deviation, we use the following formula;

$$\text{Standard deviation } (\sigma) = \sqrt{\frac{S(X - \overline{X})^2}{N}}$$

Where,

σ= Standard deviation

$\sum (X - \overline{X})^2$= Sum of squares of the deviations measured from arithmetic average.

N = Number of items.

Karl Pearson's Correlation Coefficient

The Karl Pearson's correlation coefficient is one of the widely used mathematical methods of calculating the correlation or relationship between two different variables. These method summaries in one figure the degree of relationship as well as direction. It is simply denoted by "r" and it can be calculated by using the following formula;

$$r_{XY} = \frac{NSXY - (SX)(SY)}{\sqrt{NSX^2 - (SX)^2}\sqrt{NSY^2 - (SY)^2}}$$

Where, N = Number of observation in series X and series Y

$\sum XY$ = Sum of the product of the observations in series X and series Y

$\sum X$ = Sum of the observations in series X

$\sum Y$ = Sum of the observations in series Y

$\sum X^2$ = Sum of the square of observation in series in X

$\sum Y^2$ = Sum of the square of observation in series in Y

r_{XY} = Karl Pearson’s coefficient of correlation

The coefficient of correlation is indicate following relationship

i) When r = +1, there is prefect positive relationship

ii) When r is close to 1, there is strong positive relationship.

iii) When r is close to 0 but positive, there is low degree of positive relationship.

iv) When r is equal to 0, there is no relationship.

v) When r is close to 0 but negative, there is low degree of negative relationship.

vi) When r is close to –1, there is strong negative relationship.

vii) When r = –1, there is perfect negative relationship.

A correlation coefficient of 1 means that for every positive increase in one variable, there is a positive increase of a fixed proportion in the other. A correlation coefficient of –1 means that for every positive increase in one variable, there is a negative decrease of a fixed proportion in the other. Zero means that for every increase, there isn’t a positive or negative increase. (Shrestha, 2014).

g) t-Test

t-test is popularly known as small or exact sample test. A sample is said to be small if the sample size is less than 30 i.e. n<30. t-test is based on t distribution. t-test is also call students t-test as t distribution was first developed by statistician W.S. Gosset in 1908. There are two forms of t-test. One form is used with independent samples and the other is used with dependent samples.

Assumptions of t-test:

- Sample size is less than 30 and population standard deviation is unknown.
- The parent population from which sample is drawn is normal
- The sample is random i.e. sample observations after independent.

  Applications of t-Test

- To test the significance of single mean and the difference between two independent sample mean.
- To test the significance of difference between two dependent sample mean.
- To test the significance of an observed sample correlation coefficient.

t - Value $|t| = \frac{r}{\sqrt{1-r^2}} \text{X} \sqrt{n-2}$

where, r = the sample correlation coefficient

n = Sample size

- Degree of freedom: The degree of freedom (d.f.) is n-2
- Decision: If the calculated value of ‘t’ is less or equal to the tabulated value ‘t’, then we accept Ho and if calculated value is greater, then we reject Ho.

CHAPTER IV

PRESENTATION AND ANALYSIS OF DATA

Presentation and analysis of data is very important stage of research study. Its main purpose is to change the unprocessed data into understandable form. It is the process of organizing the data by tabulating and then placing that data in presentable form by using various tables, figures and sources. (Shrestha, 2011).

Credit management is one of the most important factors that has been developed to facilitate effective performance of bank management. Credit management is the formal expression of the commercial banks goals and objectives stated in financial term for specific future period of time. Credit is the very basic indicator for determining profit. (Rouniyar, 2013).

The main purpose of the objective is to assess the credit management in selected commercial banks. Present chapter will discuss the various aspects of credit management and their actual accomplishment. Actually, credit management is a fundamental managerial tool, which is applied in commercial banks. For this respect, it will analyze the data by using various financial and statistical tools to meet the stated objectives of the study. It also compares the data between selected banks. Besides, it also presents the various funding generated from data analysis. (Shrestha, Nepal, 2015).

4.1 Financial Condition of Selected Nepalese Commercial Banks

Financial analysis assists in identifying the major strengths and weaknesses firm. It indicates whether a company has enough cash to meet its obligations ability to utilize properly their available resources. Financial analysis can also used to assess the company's liability as an ongoing enterprise and determine whether a satisfactory return is being earned for the risks return. The necessary to find out the comparative financial condition of the banks in terms of credit practices necessary to find out the comparative credit practices in those banks. For research purpose, financial condition of both the banks in terms of credit practices, credit efficiency has analyzed the comparative credit position selected commercial banks.

4.2 Credit Practices in Laxmi Bank Limited and Nepal Investment Bank

Credit practices show the lending policies and practices adopted by the selected commercial banks during the study period. It measures the ability of the organization in terms of credit practices by using historical data.

4.2.1 Total loans to deposit ratio

The main source of bank's lending depends on its deposit. This ratio is calculated to find out how successfully the banks are utilizing their deposits on loan and advances for profit generating activities greater ratio indicates the better utilization of total deposits. The ratios are presented in the following table.

Table 4.1: Total loans to deposit ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.501	0.553	0.543	0.478	0.523	0.520
SBL	0.793	0.821	0.860	0.896	0.890	0.852

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

The table 4.1 shows that he ratio of credit deposit ratio in SBL was 0.793, 0.821, 0.860, 0.890 and 0.852 in the fiscal year 2015/16 to fiscal year 2019/20 respectively. Similarly the ratio of LBL was 0.501, 0.553, 0.543, 0.478 & 0.523 respectively. In overall comparison, SBL has the highest ratio in F/Y 2018/19 i.e. 0.896 and LBL has observed the lowest ratio in F/Y 2018/19 with 0.478.

For mean point of view, SBL has maintained higher loan & advances to total deposit. In this way, it shows that SBL seems to be strong to mobilize its total deposit as loan & advances. However higher ratio does not mean it is always better from the point of liquidity. Both banks are capable to use more than 50% of deposit on loan and advances. If maintained this, it helps to make consistency on the profitability of the banks.

4.2.2 Interest Income to Loans & Advances

Interest income to loan & advances is one of the major sources of income for a commercial bank. The high volume of interest income is indicator of good performance of lending activities.

Table 4.2: Interest income to loan & advances

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.108	0.111	0.098	0.156	0.168	0.128
SBL	0.093	0.095	0.120	0.123	0.107	0.107

(Source: Annual reports of the companies (FY2015/16 to FY 2019/20))

Table 4.2 shows the ratio of interest income to loan and advances of the selected companies over the study period. Interest income to loan and advances ratio of LBL ranges from the highest of 0.168 and to the lowest of 0.098 in the fiscal year 2019/20 and 2017/18 respectively. The mean ratio is 0.128, ratio of last two years are above the mean and the ratio the of fiscal year 2013/14, 2014/15 and 2015/16 are below the average. The mean interest income to loan and the advances of the SBL is 0.107. Ratio of SBL does not show clear direction. Highest ratio is in the fiscal year 2018/19 is 0.123 and lowest in the fiscal year 2015/16 is 0.093. The mean interest income to loan and advances ratio of LBL is higher, it terms of the ratio LBL has best performance.

4.2.3 Non-Performing Loans to Total Loan and Advances Ratio

NRB has directed all the commercial banks to create loan loss provision against the doubtful and bad debts. But our concerned banks have not provided data on no-performing loan in Balance Sheet and Profit & Loss A/C. To measure the volume of non-performing loan to total loan & advances the main indicator of SBL and LBL has been used. This ratio shows the percentage on non-recovery loans in total loan & advances.

Table 4.3: Non-performing loan to total loan and advances (in %)

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.089	0.074	0.085	0.068	0.073	0.078
SBL	0.025	0.027	0.035	0.045	0.038	0.034

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

Table 4.3 shows the Non-performing loan to total loan and advance over the study period. Ratio of LBL ranges highest of 0.089 and lowest 0.073, it shows decreasing trend in subsequent year. Likewise the ratio of SBL ranges the highest of 0.045 and lowest 0.025, it is in fluctuating during the study period. The mean Non-performing loan to loan and advances of LBL and SBL are 0.078 and 0.034. The Ratio of LBL in the year 2018/19 and 2019/20 are above and below the average in the remaining fiscal year. Ratio of SBL in the first two are below the average and ratio of last three years is above the average. SBL has the lowest non performing loan to total loan and advances; this SBL is best performer than the LBL.

Banking sector is seriously affected by the non-performing loan. Both banks are not far from this above fact. If non-performing loan increases, the overall banking business will be affected. So provisioned amount will increase and profit will decrease. So, it is suggested that both banks (SBL & LBL) to be sincere while granting loan and to do effective follow up for recovery of non-performing loan.

4.2.4 Loans and Advances to Total Assets Ratio

Loan & advance is the major part of total assets for the bank. This ratio indicates the volume of loans & advance out of the total assets. A high degree of the ratio indicates that the bank has been able to mobilize its fund through lending function. However lending always carries a certain risk of default. Therefore a high ratio represents low liquidity and low ratio represents low productivity with high degree for safety in terms of liquidity.

Table 4.4: Loans & advances to total assets ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.483	0.497	0.521	0.472	0.498	0.494
SBL	0.622	0.726	0.562	0.578	0.582	0.614

(Source: Annual reports of the companies (FY2015/16 to FY 2019/20))

Table 4.4 shows that the ratio of loans & advance to total assets in five years for the selected companies. Loans and advances to total assets ratio of LBL ranges the highest of 0.521 in the fiscal year 2017/18 and the lowest in the fiscal year 2018/19 is 0.472. Ratio of SBL is highest in the fiscal year with 0.726 and lowest 0.578 in the fiscal year 2018/19. From the mean point of view, it can be said that mean ratio of SBL has highest than LBL. It can be concluded that higher the mean ratio it indicates good lending performance. Here LBL should focus to increase loan and advances to total assess ratio to increase lending performance.

4.2.5 Loan and Advances to Current Assets Ratio

Loans & advances is the major component in total assets, which indicates the ability of banks to canalize its current assets in the form of loan & advance to earn high return. If sufficient loan and advances cannot be granted, it should be pay interest on those utilized current assets funds and may lose earnings. So commercial banks provide loan & advances in appropriate level to find out portion of current assets, which is granted as loan & advances.

Table 4.5: Loan & advances to current assets ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	4.49	5.06	5.25	4.85	4.95	4.920
SBL	6.43	6.09	5.95	6.12	5.78	6.074

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

Table 4.5 shows the loan and advances to current assets of selected companies over the study period. Loans and advances to current assets ratio of LBL ranges highest of 5.25 times in the fiscal year 2017/18 and lowest 4.49 in the fiscal year 2015/16. Loan and advances to current assets ratio of LBL in the fiscal year 2015/16 and 2018/19 are below the average and above the average in the rest of the fiscal year. This shows the increasing trend on loan and advances to current assets ratio of LBL. The Ratio of SBL is the highest in the fiscal year 2015/16 with 6.43 and lowest 5.78 in the fiscal year 2019/20. From the mean point of view, it can be said that mean ratio of SBL has highest than LBL. It can be concluded that the higher the mean ratio indicates the good short term lending performance. LBL should focus to increase loan and advances to current assets ratio to increase short term lending performance.

4.2.6 Loans Loss Provision to Total Loan and Advances Ratio

The provision for loan loss reflects the increasing probability of non-performing loan. Increase in loan loss provision decreases in profit result to decrease in dividends. But its positive impact is that strengthens the financial conditions of banks by controlling the credit risk and reduces the risks related to deposits.

The low ratio indicates the good quality of assets in total volume of loan & advances. High ratio indicates move risky assets in total volume of loan & advances.

Table 4.6: Loan loss provision to total loan & advances

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.081	0.066	0.069	0.078	0.062	0.071
SBL	0.027	0.036	0.042	0.039	0.034	0.036

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20))*

Above table 4.6 shows the loan loss provision to total loan and advances of selected over the study period. Ratio of LBL ranges highest 0.081 in the fiscal year 2015/16 and lowest 0.062 in the fiscal year 2019/20. Average ratio of LBL is 0.071, ratio in fiscal year 2015/16 and 2017/18 are above the average and ratio in remaining fiscal years is below the average during the five year period. Ratio of SBL ranges highest 0.042 in the fiscal year 2017/18 and lowest 0.027 in the fiscal year 2015/16. Here average loan loss provision to loan and advances ratio of LBL is higher than the SBL. Higher ratio indicates the increased volume of non-performing loans and vice versa. Loan loss provision of LBL is in a decreasing trend in on the fiscal year 2016/17, so the decreasing loan loss ratio indicates efficient credit policy and gradual increment on the performance of the company. Here loan loss provision to total loan and advances of SBL is in increasing trend, which indicates increased volume of non-performing loans of SBL; we can say this is due to the ineffective credit policy and poor performance of the company.

4.3 Credit Efficiency in Laxmi Bank Limited and Sidhartha Bank Limited

It measures the effectiveness or activity of the company through establishing the relationship between the various assets and credit of that respective organization.

4.3.1 Interest expenses to total deposit Ratio

This ratio measures the percentage of total interest paid against total deposit. A high ratio indicates higher interest expenses on total deposit. Commercial Banks are dependent upon its ability to generate cheaper fund has moves the probability of generating loans and advances and vice versa.

Table 4.7: Interest expenses to total deposit ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.037	0.039	0.029	0.024	0.031	0.032
SBL	0.025	0.026	0.032	0.028	0.024	0.027

(Source: Annual reports of the companies (FY2015/16 to FY 2019/20))

Above table 4.7 shows the cost of deposit of selected banks over the study period. The Ratio of LBL ranges highest 0.039 in the fiscal year 2016/17 and lowest 0.0247 in the fiscal year 2018/19. Average ratio of LBL is 0.032, ratio in fiscal year 2015/16 and 2016/17 are above the average and ratio in rest of the fiscal year is below the average. Ratio of SBL ranges highest 0.032 in the fiscal year 2017/18 and lowest 0.024 in the fiscal year 2019/20. Here average interest expenses to total deposit ratio of LBL than higher than of SBL ratio. Higher ratio indicates the increased cost of deposit. SBL is able to collect the cheaper deposit than that of LBL.

4.3.2 Interest and Expenses to Total Expense Ratio

This ratio measures the percentage of interest paid against total expenses. The high ratio indicates the low operational expenses and vice versa. The ratio indicates the costly sources of funds.

Table 4.8: Interest expenses to total expenses ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.391	0.358	0.435	0.465	0.412	0.412
SBL	0.388	0.473	0.389	0.342	0.312	0.381

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

Above table 4.8 shows the interest expenses to total expense ratio of selected companies over the study period. Ratio of LBL ranges highest 0.465 in the fiscal year 2018/19 and lowest 0.358 in the fiscal year 2016/17. Average ratio of LBL is 0.412, ratio in fiscal year 2015/16 and 2016/17 are below the average and ratio in the rest of the fiscal year is above the average. So, this shows the increasing trend of the ratio. Ratio of SBL ranges highest of 0.473 in the fiscal year 2016/17 and lowest 0.312 in the fiscal year 2019/20. Average interest rate of SBL is 0.381, and the ratio in fiscal year 2018/19 and 2019/20 are below the average and the ratio in the remaining year above the average. Average interest expenses to total expenses ratio of LBL is higher.

SBL has low interest expenses to total expenses ratio, which shows that decrease in cost of deposit as decrease in the interest expenses to total expenses ratio decrease.

4.3.3 Non-interest bearing deposits to total deposit ratio

This ratio measures the volume of non-interest bearing deposits to total deposit. The volume of interest expenses in total expenses represents a large portion of the total expenses. How efficiently the deposits were managed affectively in the total volume of expenses. The higher ratio is favorable but in practices, interest bearing deposits always plays a significant role in the mix of deposit liability.

Table 4.9: Non-interest bearing deposits to total deposit ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.21	0.34	0.29	0.26	0.31	0.282
SBL	0.13	0.1	0.16	0.12	0.11	0.124

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

Above table 4.9 shows non-interest bearing deposits to total deposit ratio of selected companies over the study period. Ratio of LBL is fluctuating trend, ranges the highest 0.34 in the fiscal year 2016/17 and the lowest 0.21 in the fiscal year 2015/16. Average ratio is 0.282, the ratio of the fiscal year 2016/17 and 2017/18 are above the average and the ratios of remaining fiscal year are below the average. Non - interesting bearing deposits to total deposit ratio of SBL ranges highest 0.16 in the fiscal year 2017/18 and lowest 0.10 in the fiscal 2016/17.

From the mean point of view, it can be said that LBL has highest mean ratio. In this way; the deposit mixture of LBL carries the highest level of interest bearing deposits in its deposit mixture. This major portion of non-interest bearing deposit consists of current deposits and this deposit is particularly maintained by business enterprises.

4.3.4 Interest income to total income ratio

This ratio measures the volume of interest income in total income. The high ratio indicates the high contribution made by lending and investment whereas low ratio indicates low contribution made by lending & investment and high contribution by other fee based activities in total income.

Table 4.10: Interest income to total income ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.822	0.795	0.856	0.725	0.812	0.802
SBL	0.774	0.809	0.789	0.768	0.757	0.779

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

Table 4.10 shows the interest income to total income ratio of selected companies over the study period. The ratio of LBL ranges highest 0.856 in the fiscal year 2017/18 and lowest 0.725 in the fiscal year 2018/19. The average ratio is 0.802, the ratio in the fiscal year 2016/17 and 2018/19 are below the average and ratio in the rest of the fiscal year above the average. The ratio of SBL is highest 0.809 in the fiscal year 2016/17 and the lowest in the fiscal year 2019/20 is 0.757. The average ratio is 0.779, the ratio of fiscal year 2016/17 and 2017/18 are above the average and below in the rest of the fiscal years.

From Average point of view, it can be said that LBL has high interest income to total income. This shows that in total income of LBL and SBL, interest income contributes 80.2% and 77.90% respectively. The lowest ratio of SBL indicates its low dependency in fund-based activity. The highest ratio of LBL indicates greater dependency on fund-based activities.

4.3.5 Interest Suspense to Interest from Loans & Advances Ratio

Interest suspense means the interest due but not collected. This ratio measures the composition of due but uncollected interest in the total interest income from loan & advances. The high degree of this ratio indicates the low interest turnover and low degree of this ratio indicates high interest turnover. This ratio also helps to analyze the capacity of the bank in collecting the repayments of the loans & advances.

Table 4.11: Interest suspense to interest income from loans & advances ratio

Bank/F.Y	2015/16	2016/17	2017/18	2018/19	2019/20	Mean
LBL	0.26	0.34	0.36	0.28	0.25	0.298
SBL	0.03	0.03	0.04	0.05	0.04	0.038

(*Source: Annual reports of the companies (FY2015/16 to FY 2019/20)*)

Table 4.11 shows the interest suspense to total income from loans and advances ratio of selected companies over the study period. Ratio of LBL ranges highest 0.36 in the fiscal year 2017/18 and the lowest 0.25 in the fiscal year 2019/20. Average ratio is 0.298; ratio in fiscal year 2016/17 and 2017/18 are above the average and ratio in rest of the fiscal year below the average. The ratio of SBL ranges highest of 0.05 in the fiscal year 2018/19 and lowest in the fiscal year 2015/16 and 2016/17. The average ratio is 0.038, ratio of fiscal year 2015/16 and 2016/17 are below the average and above in the rest of the fiscal year.

From Average point of view, it can be said that LBL has high interest income to total income. This shows that in total income of LBL and SBL, interest income contributes 29.80% and 3.80% respectively. The lowest ratio of SBL indicates its low dependency in fund-based activity. The highest ratio of LBL indicates greater dependency on fund-based activities.

4.4 Relationship of Loans and Net Profit

Effective loans directly affect net profit volume of the organization. It is regarded as the most important profit indicator. It helps to increase the net profit volume of the company whereas weak level of loans is the signal of lower level of profit. Thus, it is logical to review the relation of loans and net profit.

For the research proposes, net profit and loans during study period (5 yrs) are averaged to get profit and loans variable. After getting profit and loans variable, then data are analyzed using person's correlation coefficient. The following table presents the correlation coefficient of the profit and loans during study period.

Table 4.12: Relationship between loan and advance and net profit in LBL:

Correlation Matrix

		Loans	**Net profit**
Loans	Person correlation	1	0.9166
	N	5	5
Net profit	Person correlation	0.9166	1
	N	5	5

(*Source: Appendix*)

The table 4.12 presents the correlation coefficient between loans and net profit during study period. The calculated Person's Correlation Coefficient was found 0.9166, which shows high degree of correlation. It indicates that loans and net profit were found highly related with each other. That means, increasing loans helps to increase the net profit whereas decrease in loans decreases in net profit similarly. Coefficient of determination was found to be 0.8119 which indicates that 81.19% of total change in profit has been determined by the loans. Loans have high influence on net profit of the LBL. Effective loans management helps to increase and stable the net profit of the

LBL. No exception is found in case of LBL. Thus, it is logical to review the impact of various components of credit in net profit of the LBL.

Table 4.13: Relationship of loans and net profit in SBL: Correlation Matrix

		Loans	Net profit
Loans	Person correlation	1	0.953
	N	5	5
Net profit	Person correlation	0.953	1
	N	5	5

(*Source: Appendix*)

The table 4.13 presents the correlation coefficient between loans and Net profit during study period. The calculated Person's correlation coefficient was found 0.953, which shows high degree of positive correlation. It indicates that loans and net profit were found high related with each other. That means, increasing loans helps to increase the net profit whereas increase in loans decreases the net profit. Similarly, coefficient of determination was found to be 0.9111 which indicates that 91.11% of total change in profit has been determined by loans. Loans have high influence on net profit of the SBL Bank. Effective loans management directly affects to net profit of the SBL Bank. No exception is found in case of SBL Bank. Thus, it is logical to review the impact of various components of working on net profit.

4.5 Relationship of Loans and Non-Performing Loans

Effective non-performing loans directly affect the volume of the loans of the LBL. It is regarded as the most important indicator. It helps to increase the risky in loans management of the LBL whereas weak level of non-performing loans is signal of the better performance of the loans management. Thus, it is logical to review the valuation of non-performing loans & loans management.

For the research purpose, the non-performing loan and loan management during study period (5 years) are averaged to get non-performing loans and loans variables. After getting non-performing loans and loans, then data are analyzed using Person's correlation coefficient. The following table presents the correlation coefficient of the non-performing loan and loans management during study period.

Table 4.14: Relationship between loan and non-performing loans in LBL

Correlation Matrix

		LOANS	**Non-performing loan**
LOANS	Person correlation	1	–0.656
	N	5	5
Non-performing loan	Person correlation	–0.656	1
	N	5	5

(*Source: Appendix*)

The table 4.14 presents the correlation coefficient between non-performing loan and loans during study period. The calculated Person's correlation coefficient was found –0.656, which shows moderate, negative correlation. It indicates that non-performing loans and loans were moderately, negatively related with each other. That means, decreasing on performance in loans management. Coefficient of determination was found 0.4536 which indicates that 45.36% of total change in loans management has been negatively determined by non-performing loans.

Loan management has been negatively influenced by non-performing loans. Effectively loans management helps to decrease the non-performing loans. No exception is found in case of LBL Banks. Thus it is logical to review the impact of various components of working in loans management.

Table 4.15: Relationship between loan and non-performing loans in SBL:

Correlation Matrix

		Loans	**Net profit**
Loans	Person correlation	1	–0.265
	N	5	5
Net profit	Person correlation	–0.265	1
	N	5	5

(*Source: Appendix*)

The table 4.15 presents the correlation coefficient between non-performing loan and loans during study period. The calculated Person's correlation coefficient was found –

0.265, shows low negative correlation. It indicates that non-performing loans and loans were negatively related with each other. It means, decreasing performance in loan management. Coefficient of determination was found 0.0656 which indicates that 6.56% of total change in loans management has been negatively determined by non-performing loans. Loan management has been negatively influenced by non-performing loans. Effectively loans management helps to decrease the non-performing loans. No exception is found in case of SBL. Thus it is logical to review the impact of various components of working in loans management.

4.6 Impact of Loan and Advances on Net Profit

Loans have high implication for determining net profit. Effective loans directly affect the net profit of the banks. It means that the net profit of the banks is largely depended by the loans management. Thus, it is more significance to know the impact of loans in net profit. To find out the result the five yes data (study period) of net profit, loans are averaged to get a variable of net profit & loans. Thereafter, simple regression analysis is used for computation. The following table presents the regression analysis of the independent variable loans on dependent variables net profit of the SBL Bank.

Table 4.16: Regression Analysis on loan and advance and net profit in SBL

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.955 (a)	.911	.890	36.85203

(a) Predictors: (Constant), Loan

Regression equation of Net Profit (Y) on Loan and advances (X) is given by

Regression equation	Constant (a)	Coefficient (b)
$\hat{Y} = a + bx$	**–2.489**	**0.24**

(*Source: Appendix*)

Table 4.16 shows the dependency of Net profit on loans. The calculated R was found 0.911 indicates that there is high relationship dependent variable profit on independent variable loans. After considering the error term, the adjusted R square value was found.890 which indicates that 8.9% of the total variation in the dependent variable net profit has been explained by the independent variable loans. Thus, it can be concluded that loans is a strong determinant of net profit. Therefore management loans should seriously be taken to achieve the goal of the SBL Bank.

The value of b is found to be 0.24, which means that, on average, 1 rupee change in total loan would result in 1.24 paisa change in the Net profit of SBL. Given the Net profit of the SBL for coming years, we can use the above Equation to estimate what the consumer loan of the SBL would likely to be in the coming years.

Table 4.17: Regression Analysis on loan and advance and net profit in LBL

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.917(a)	.825	0.765	48.49817

(a) Predictors: (Constant), Loan

Regression equation of Net Profit (Y) on Loan and advances (X) is given by

Regression equation	Constant (a)	Coefficient (b)
$\hat{Y} = a + bx$	**–166.875**	**0.045**

(*Source: Appendix*)

Table 4.17 shows the dependency of net profit on loans. The calculated R was found 0.917 indicates that there is high relationship dependent variable profit on independent variable loans. After considering the error term, the adjusted R square value was found 0.765 which indicates that 7.65% of the total variation in the dependent variable net profit has been explained by the independent variable loans. Thus, it can be concluded that loans is a strong determinant of net profit. Therefore management loans should seriously be taken to achieve the goal of the LBL Bank.
The value of b is found to be 0.045, which means that, on average, 1 rupee change in total loan would result in 1.45 paisa change in the Net profit of LBL. Given the Net profit of the SBL for coming years, we can use the above Equation to estimate what the consumer loan of the SBL would likely to be in the coming years.

4.7 Trend Analysis Least Square Method

Trend analysis is a statistical tool, which will highlight the previous trend of the financial performance and helps in forecasting the future financial results of these banks. Trend analysis shows the trend of loan and advances of seven banks for eight years. Loan and advances shows a bank's efficiency in performance of efficient utilization of the same indicates its success and profitability.
The trend analysis on loan and advances for coming year is following.

The value of Y (loan and advance) when financial is 6th year (2020/21), 7th year (2021/22) and 8th year (2022/23).

Now,

Regression equation Y = a + bX

Loan and advances on the 6th year

$$Y = 483.54 + 2396.75 \times 6 = 14864.04$$

Loan and advances for 7 the year

$$Y = 483.54 + 2396.75 \times 7 = 17260.79$$

Loan and advances for 8 the year

$$Y = 483.54 + 2396.75 \times 8 = 19657.54$$

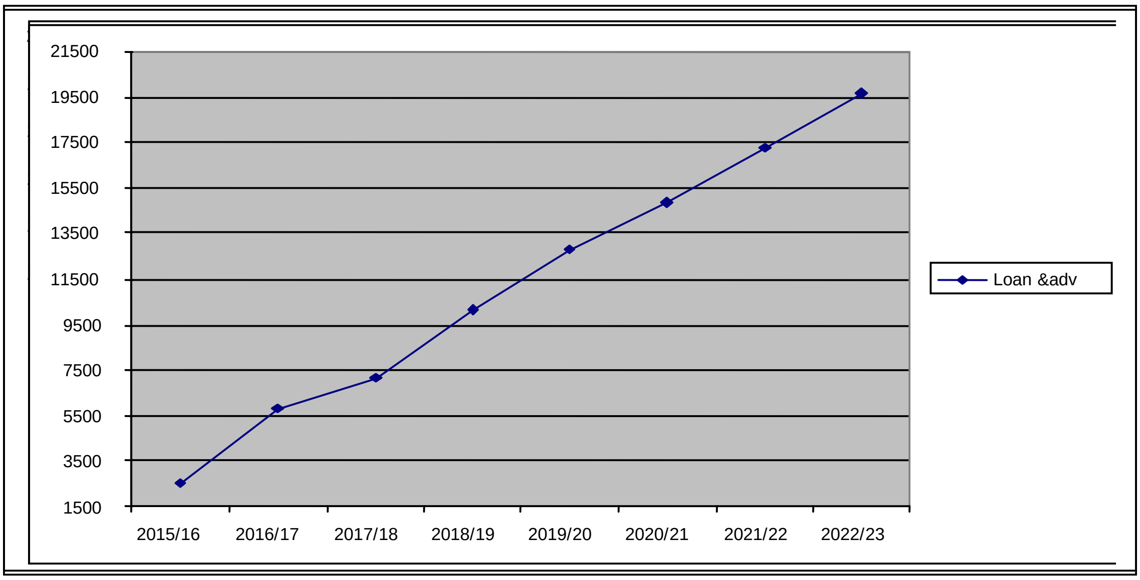
Table 4.18: Trend Forecast of Loan and Advance of Siddhartha Bank Limited

(Rs. In '000')

	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Loan & Advance	2564.43	5772.14	7130.13	10126.06	12776.2	14864.04	17260.79	19657.54

(*Source: Annual reports of bank*)

Figure 4.1: Loan and advances Trend line of Siddhartha Bank Limited



(*Source: Annual reports of bank*)

Based on analysis presented table that concludes loan and advances has been increasing trend. The expected loan and advances is 14864.04 million, 17260.79

million and 19657.54 million in the fiscal years 2020/21, 2021/22 and 2022/23.

Trend of Loan and advances of Laxmi Bank Limited

Computation of straight line trend analysis of loan and advance of Laxmi Bank Limited

Now,

Regression equation $Y = a + bX$

Loan and advances on the 6th year

$Y = 7422.81 + 1388.03 \times 6 = 15750.99$

Loan and advances for 7 the year

$Y = 7422.81 + 1388.03 \times 7 = 17139.02$

Loan and advances for 8 the year

$Y = 7422.81 + 1388.03 \times 8 = 18527.05$

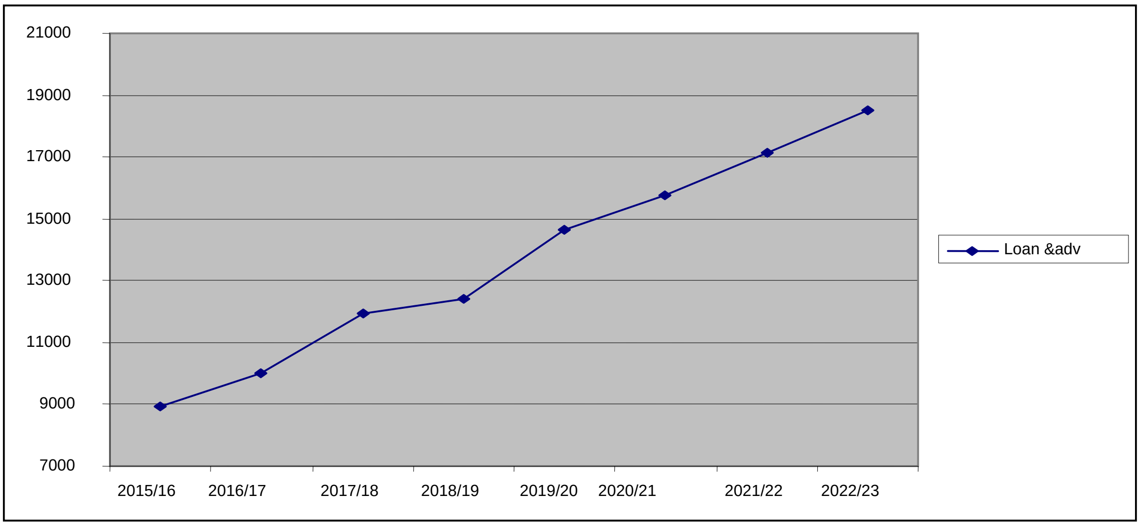
Table 4.19: Trend Forecast of Loan and Advance of Laxmi Bank Limited

(Rs. In '000')

FY	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23
Loan & Advance	8913.72	10001.85	11951.9	12424.52	14642.56	15750.99	17139.02	18527.05

(*Source: Annual reports of bank*)

Figure 4.2: Loan and advance Trend Line of Laxmi Bank Limited



(*Source: Annual reports of bank*)

Based on analysis presented table that concludes loan and advances has been increasing trend. The expected loan and advances is 15750.99 million, 17139.02 million and 18527.05 million in the fiscal year 2020/21, 2021/22 and 2022/23.

Non-interest bearing deposits to total deposit ratio

Table 4.20: Correlation Non-interest bearing deposits to total deposit ratio

Banks	R	r^2	t-value (calculated)	t-value (tabulated)	Sig./Insig.
Sidhartha Bank Limited	0.17	0.03	0.30	2.353	Insig.
Laxmi bank Limtied	0.75	0.56	1.96	2.353	Insig

(Source: Appendix- I)

The above table shows that there is insignificant correlation between Noninterest bearing to total deposit ratio of both SDBL and LBL at 5% level of significance and degree of freedom at 3 since the calculated t-value is less than tabulated t-value.

Correlation between interest and total income Ratio

Generally, the higher Interest creates positive attitude among the shareholders towards bank, which accordingly helps to increase the total income Ratio.

Table 4.21: Correlation between interest and total income Ratio

Banks	r	r^2	t-value (calculated)	t-value (tabulated)	Sig./Insig.
Siddhartha Bank Limited	0.33	0.11	0.60	2.353	Insig.
Laxmi bank Limited	0.91	0.83	3.84	2.353	Sig

(Source: Appendix- II)

The above table shows that there is insignificant correlation between interest and Total income Ratio of SDBL Bank at 5% level of significance and degree of freedom at 3 since the calculated t-value (0.60) is less than tabulated t-value (2.132).Similarly there is significant correlation between Interest and Total income Ratio of Sidharth Bank and Laxmi Bank Limited since the calculated t-value (3.84) is greater than tabulated t-value (2.353).

4.8 Major Findings

From the above analyses of credit management, following major findings have been obtained:

- Average loan and advances to total deposit to total deposit ratio of LBL and SBL is 0.520 and 0.852 respectively. SBL has maintained higher loan & advances to total deposit. In this way, it shows that SBL seems to be strong to mobilize its total deposit as loan & advances. However higher ratio does not mean it is always better from the point of liquidity. Both banks are capable to use more than 50% of deposit on loan and advances. If maintained this, it help make consistency on the profitability of the banks.
- SBL has lowest non performing loan to total loan and advances, this SBL is best performer than the LBL. Banking sector is seriously affected by the non-performing loan. Both banks are not far from this above fact. If non-performing loan increases, the overall banking business will be affected. So provision amount will increase and profit will decrease. So, it is suggested that both banks (SBL & LBL) to be sincere while granting loan and to do effective follow up for recovery of non-performing loan.
- Average loan and advances to total assets of LBL and SBL 0.452 and 0.608 it can be concluded that the higher mean ratio indicates the good lending performance. Here LBL should focus to increase loan and advances to total asset ratio to increase lending performance.
- Loan and advances to current assets ratio of LBL is in an increasing trend. Average ratio of LBL and SBL is 4.43 and 6.42. From the mean point of view, it can be said that mean ratio of SBL has highest than LBL. It can be concluded that the higher mean ratio indicates the good short term lending performance. Here LBL should focus to increase loan and advances to current assets ratio to increase short term lending performance.
- Increase ratio indicates the increased volume of non-performing loans and vice versa. Loan loss provision of LBL is decreasing trend in the fiscal year 2016/17, so the decreasing loan loss ratio indicates efficient credit policy and gradual increment on the performance of the company. Here loan loss provision to total loan and advances of SBL is in increasing trend, which indicates increased volume of non-performing loans of SBL; we can say this is due to the ineffective

credit policy and poor performance of the company.

- Average interest expenses to total expenses ratio of LBL is higher. SBL has low interest expenses to total expenses ratio, it shows that decrease in cost of deposit as decrease in the interest expenses to total expenses ratio decrease.
- Total income of LBL and SBL, interest income contributes 81.70% and 79.10% respectively. The lowest ratio of SBL indicates its low dependency in fund-based activity. The highest ratio of LBL indicates greater dependency on fund-based activities.
- Correlation Coefficient between the loans and advances to net profit of LBL is 0.9066; it indicates high degree of positive relationship between loans and net profit. This means. Increasing loans helps to increase the net profit. Loans have high influence on net profit of the LBL. Effective loans management helps to increase and stable the net profit of the LBL Correlation Coefficient between the loan and advances to net profit of SBL is 0.954; it indicates high degree of positive relation between loan and net profit. Loans have high influence on net profit of the SBL Bank. Effective loans management directly affects to net profit of the SBL Bank.
- Correlation coefficient between non-performing loan and loans during of LBL is -0.666, which shows moderate, negative correlation. It indicates that non-performing loans and loans were moderately, negatively related with each other. That means, decreasing on performance in loans management. Effectively loans management helps to decrease the non-performing loans.
- Correlation coefficient between non-performing loan and loans of SBL is –0.275; it indicates that non-performing loans and loans were negatively related with each other. Coefficient of determination was found 0.0756 which indicates that 7.56% of total change in loans management has been negatively determined by non-performing loans. Loan management has been negatively influenced by non-performing loans. Effectively loans management helps to decrease the non-performing loans.
- Coefficient of determination of N value was found.880 which indicates that 8.8% of the total variation in the dependent variable net profit has been explained by the independent variable loans. Thus, it can be concluded that loans is a strong determinant of net profit. Therefore management loans should seriously be taken

to achieve the goal of the SBL Bank. The value of b is found to be 0.25, which means that, on average, 1 rupee change in total loan would result in 1.25 paisa change in the Net profit of SBL.

- Coefficient of determination of LBL is 0.763 which indicates that 7.63% of the total variation in the dependent variable net profit has been explained by the independent variable loans. Thus, it can be concluded that loans is a strong determinant of net profit. Therefore management loans should seriously be taken to achieve the goal of the LBL Bank. The value of b is found to be 0.040, which means that, on average, 1 rupee change in total loan would result in 1.4 paisa change in the Net profit of LBL.
- Least square trend line shows the loan and advances of SBL have been increasing with a constant growth rate of 2396.75. The expected loan and advances is 14864.04 million, 17260.79 million and 19657.54 million in the fiscal year 2020/21, 2021/22 and 2022/23.
- Least square trend line shows the loan and advances of LBL have been increasing with a constant growth rate of 1388.23. The expected loan and advances is 15750.99 million, 17139.02 million and 18527.05 million in the fiscal year 2020/21, 2021/22 and 2022/23.

CHAPTER V
SUMMARY, CONCLUSION AND RECOMMENDATIONS

As the final chapter of the study, this chapter briefly explains the summary of the study, tries to fetch out findings and conclusions and attempts to offer suggestions and recommendations for strengthen the financial position of the sample banks.

5.1 Summary

Development of any nation depends on capital vested and mobilized in productive sectors like industries trade and business of every nook and corners of the country. In fact, the development of economy of the world is this result of substantial investment in such productive sectors In order to boost up the economy and the social life of any country, it is extremely essential to have a mechanism through which small amount of saving can be collected and transferred into efficient uses. Hence, finance plays a vital role and thus contributes in the economic development of nation and the banks provide such financial services.

The basis of business is borrowing from individuals, firms and occasionally government i.e. receiving deposit from them. With these resources and bank's own capital, banks disburse loan or extend credit and also invest in securities. Bank is an institution, which deals with the transaction of money. They perform several financial monetary and economic activities that are essential to accelerate the rate of economic growth of the country.

At present, 27 commercial banks have been operating in Nepal. After the adaptation of liberal policy by the government in 1990 number of banks and financial institutions are increasing day by day. They have been rendering high quality banking services to the people. There is cut throat competition between banks and financial intuitions.

This research has been undertaken to evaluate the credit management of commercial banks. Two banks Laxmi Bank Limited and Investment Bank Limited banks are under study and five year financial statements of respective banks have been used for the study. The study has been divided into five chapters which include introduction, review of literature, research methodology, data presentation and analysis and summary, conclusion and recommendation. This study mainly based in secondary data, with include published annual report and other publication of banks. Other related information was gathered from the concerned banks, Nepal Rasta Bank, Nepal Stock Exchange, Securities Board of Nepal, different websites. The data have been analyzed by using financial and statistical tools like ratio analysis, correlation coefficient, regression analysis trend analysis etc.

5.2 Conclusion

The study shows that over the period, Average loan and advances ratio of LBL and SBL is 0.510 and 0.534. Both banks are capable to use more than 50% of deposit on loan and advances. If maintained this, it help make consistency on the profitability of the banks.. Banking sector is seriously affected by the non-performing loan. Both banks are not far from this above fact. If non-performing loan increases, the overall banking business will be affected. So provision amount will increase and profit will decrease. So, it is suggested that both banks (SBL & LBL) to be sincere while granting loan and to do effective follow up for recovery of non-performing loan. Average loan and advances to total assets of LBL and SBL 0.453 and 0.580 it can be concluded that the higher mean ratio indicates the good lending performance. Here LBL should focus to increase loan and advances to total asset ratio to increase lending performance. Loan and advances to current assets ratio of LBL is in increasing trend. Here LBL should focus to increase loan and advances to current assets ratio to increase short term lending performance. Loan loss provision of LBL is decreasing trend in the fiscal year 2019/20, so the decreasing loan loss ratio indicates efficient credit policy and gradual increment on the performance of the company. Here loan loss provision to total loan and advances of SBL is in increasing trend, which indicates increased volume of non-performing loans of SBL; we can say this is due to the ineffective credit policy and poor performance of the company. Total income of LBL and SBL, interest income contributes 81.70% and 79.10% respectively. The lowest ratio of SBL indicates its low dependency in fund-based activity. Correlation Coefficient between the loans and advances to net profit of LBL is 0.9166 and Correlation Coefficient between the loan and advances to net profit of SBL is 0.954. Correlation coefficient between non-performing loan and loans during of LBL is –0.676, Correlation coefficient between non-performing loan and loans of SBL are –0.275. Effectively loans management helps to decrease the non-performing loans. The value of b is found to be 0.24, which means that, on average, 1 rupee change in total loan would result in 1.24 paisa change in the Net profit of SBL. Least square trend line shows the loan and advances of SBL have been increasing with a constant growth rate of 2396.75. Least square trend line shows the loan and advances of LBL have been increasing with a constant growth rate of 1388.23.

5.3 Recommendations

The findings of the study reflect both positive and negative results with respect to the financial performance of the sampled banks. But the recommendations have been presented for the improvement of the negative of the banks. As per the above conclusion the following suggestions can be concluded for the banks:

- Both banks should try to increase the loan and advances to deposit; here they have maintained more than 50%. High ratio shows the capability of bank on mobilizing its total deposit as loan and advances.Banking sector is seriously affected by the non-performing loans. Both banks are not far from this above fact. If non-performing loan increases, the overall banking business will be affected Banks should sincere while granting loan and to do effective follow up for recovery of non-performing loan.
- Average loan and advances to total assets of LBL is below 50%. So, LBL should focus to increase loan and advances to total asset ratio to increase lending performance.
- Banks should do lot exercise in more credit creation and reducing the interest rate for loan and advances. This will help them to maintain more competitive.
- Banks could do better by offering modern banking facilities and new product for the development of banking industry. Provision for doubtful loan should to be maintaining as per the directives of Nepal Rastra bank.
- Other recommendations for the achievement of target goals and objective of commercial banks. From above study, analysis and observation with facts we must conclude with a reasonable realistic solution. Some of important and valuable suggestion for strength of commercial bank establishment, sustainable growth. Commercial banks have to channel zed fund by gradually shifting priorities from consumer loan to the productive sector to help for capital formation in the country. Commercials banks have to improve their quality of services.

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CHAPTER I INTRODUCTION 1.1 Background of the Study Since 2012, Nepal has opened itself to international investment as a liberalized economy. Nearly half of the population, particularly those living in rural regions, fall below the absolute poverty line and lack access to even the most basic necessities, such as clean, safe drinking water, adequate food, power, roads, and so forth.

Basic human indicators such as **life expectancy, literacy, nutrition level, etc., also** demonstrate **Nepal**

's position as one of the nations that aims to eradicate the extreme poverty that still exists there by gradually developing the entire country and by giving impoverished people access to the necessities of life. The landlocked situation of Nepal, inadequate resource mobilization and use, inadequate infrastructure development, and an unstable eco-political climate are the main causes of the country's delayed growth. (Bhandari, 2005). Nepal's commercial banks are expanding incredibly quickly. Nepal has a total of 27 commercial banks. A nation's economic progress is significantly influenced by its banking industry. A bank is a tool for economic growth that helps individuals get credit and preserves the confidence of different societal groups. Therefore, commercial banks are those financial organizations that primarily deal with trade, commerce, industry, and agricultural operations and who regularly seek them assistance for financial and other needs.

Commercial banks ' goals **are to mobilize idle resources, which** are important **for** internal capital generation **and mobilization**

as well as development efforts (Bhandari, 2005). The practice of storing people's gold and valuables was developed by ancient goldsmiths, who laid the groundwork for the concept of banking. Under this arrangement,

depositors would leave their gold for safekeeping and **would** receive **their gold and** valuables back **after paying a small fee for safekeeping and**