

# **CHAPTER I**

## **INTRODUCTION**

### **1.1 General Background**

Financial development is one of the key indicators of economic growth for any country. Financial institutions grant regular energy for investments, which is needed for economic development. The financial sector of any country comprising banks, finance companies, insurance companies, co-operative societies, stock markets, foreign exchange markets, mutual funds, provident funds etc. play a great role in the enhancement of the country's economic sector. The country having liberal economy from non-liberal economy after reform, positive changes are visible in the financial sector of the country.

Commercial banks play an important role in affair of the economy in various ways. The operations of commercial banks record the economic pulse of the economy. The size and composition of their transaction mirror the economic happening in the country. They are essential instruments of accelerated growth in a developing economy, by mobilizing community savings and diverting them into productive channels commercial banks expand and appreciate the value of aggregate economic activity in the economy.

At present days, the entrance of various new banks is mounting in the banking industry; on the other hand, old banks are expanding their branches in many areas of the country. There is no doubt that the increment of commercial banks obviously boosts the financial activities and hence opens the door for the economic development of the country. Under liberal and open economy it is considered natural phenomena that there is high involvement of private Sector, which mostly focus their activities toward commercialization generating high profits.

“Commercial Banks which licensed under Commercial Bank Act 1974 (2031 B.S.) are the largest group of deposit taking financial institutions in Nepal.” In general Commercial Banks can be defined as the banks undertaking business with the objective of earning profits. Commercial banks pool scattered fund and channel it to productive use. Commercial Banks can be of various forms such as Deposit Banks, Saving Bank, Industrial Bank, and Mixed Banks etc. Commercial banks render variety of services. In the absence of commercial banks, it will be impossible to meet the financial needs of the country. "A commercial bank means bank which deals in exchanging currency, accepting deposits, giving loans and doing commercial transactions." - Commercial Bank Act 1974.

For the smooth progress of the financial industry government support is vital. Taking Nepal in the context, after the liberalization policy is carried out, government of Nepal also focused for the development of the investment institution in order to fulfill the need of financial and investment deficit that had seen in financial sector. The banking sector has made hall mark progress both in terms of number and beneficiaries. By the end of fiscal year 2010/11, Nepal Rastra Bank has already licensed institutions as Banks and Non Bank financial institution. Out of them 31 are fully fledged of commercial banks, 87 Development Banks, 79 Finance Companies, 21 Micro Credit Development Banks, 16 NRB licensed Co-operatives and 38 NGOs (RRB Report 2067/68).

The financial system in Nepal has from a narrow, repressed regime till the eighties to a dynamic expanding sector in the nineties. Indicators of the last decade showed that the sector has growth both quantitatively and qualitatively. It could be observed that, at the same time, the financial market has become more competitive, dynamic and also compels. This constitutional network and the volume of operations of financial system have expanded and diversified with the number of increased in commercial banks. The adoption of the market economy has led to birth too many private commercial banks in the country as said earlier. So far, all these banks are doing very well in the slowdown in the economy, interest rates are falling down. All the banks are with funds and looking for safe and profitable avenues to invest in it.

Macroeconomics stability is prerequisite. Least developed country like ours "Nepal". where industrial development is in initial stage, these pre-mentioned prospects are essential for sustainable economic development. "It is needed that Government and all concerned must restore peace, improve investment climate by strengthening legal, institutional and regulatory framework for the private sectors, foster links with the country's rapidly growing neighbor to tap the economic benefits of the integration, and accelerate the pace of ongoing governance reforms. Nepal entry into WTO, commitments in SAFTA and BIMSTEC too makes it important to improve in investment and business climate."

Financial institutions, in order to generate capital flow, play major roles for the proper functioning of the economy. It is how these institutions act as intermediary between the individuals as well as institutions who lend and who borrow. Accepting deposits and lending money is the playing of money that the commercial banks do to reap the profit along the side. Certain rate of interest is provided to the customers for the deposit made in the company. In addition, most of the commercial banks need collateral against the loan. The quality of loan, quality of borrower and quality of securities determines the health of any financial institution. The efficiency of commercial banks lie in how it multiplies and makes productive the deposits of its depositors. Hence, Lending should be accomplished by some basic principles and practices. No commercial banks would be willing to give loan unless it has sufficient confidence in the borrower that it will not be necessary to seek the help of court for recovery. The deposits made by the banks are generally invested in productive sector. Investment by commercial banks is made by lending the same money in the higher interest rate and purchasing government securities and investing funds in the likely profitable sectors. Thus, the main operation of commercial banks can be recognized as accumulating the scattered funds from public, providing them some interest against their saving and lending the money to the public, charging some interest. Generally,

the interest charged is higher than the interest paid and this is how the company manages to make some profit to distribute dividend to the shareholders.

This research has attempted to analysis the lending practices of NABIL, EBL, BOKL and NIBL and their lending strength which will reveal the lending practices of commercial banks of Nepal. For the purpose, different tools and techniques have been applied to judge the lending practices of these organizations, drawn out the strength and weakness of the firms and try to prescribe measures to improve the lending practices of these three banks.

### **1.1.1 Commercial Banking in Nepal**

A Commercial bank is a financial organization that its major function of which is to deal in money and credit. The main business of a commercial bank is to pool the scattered idle deposits in the public and channel it for productive use. It collects deposits and invests or lends to those who stand in need of money. Bank, in other words, is a custodian of money received from the depositors. Hence, its responsibility towards the general public is pretty different than those who are involved in other types of trades and services. Modern day banks exhibit the trait more of a department store with a wide range of range of financial products of offer. Banks can be a person, a company or a firm, with a place of business, and must be involved in credit creation. The business of a modern day bank however is not only confined in borrowing deposits and lending advances only, it performs a host of other financial activities which has immensely contributed to achieve industrial and commercial progress of every country.

Though the commercial banks were established with the concept of supplying short-term credit and working capital need of the industries, they have been providing long-term loans for up to 15 years. After the enforcement to lend to priority and deprived sector, these banks initiated to provide credit to small and cottage industries,

agriculture and services. Presently, commercial banks must lend 5% of their total lending in priority and deprived sector and among these, 3 percent being compulsory to the deprived sector. NRB has a provision of refinance facility also for such loan provided to priority and deprived sector including export credit.

### **1.1.2 Brief Profile of Sample Selected Banks**

In this section the banks profile of the above subjected banks are presented to know better of the banks individually.

#### **Nabil Bank Limited (NABIL)**

Authorized Nabil Bank Limited, the first joint venture bank of Nepal, started operations in July 1984 as the name of Nepal Arab Bank Ltd under the Company Act. Dubai Bank Ltd. was the initial foreign joint venture partner of this bank with 50% equity investment. The shares owned by DBL were transferred to Emirates Bank International Ltd (EBIL), Dubai. Later EBIL sold its entire holding to National Bank Ltd, Bangladesh (NBLB). Hence, 50% of equity shares of Nabil Bank Ltd are held by NBLB and out of remaining, financial institutions have taken 20% and 30% were issued to general public of Nepal. Nabil was incorporated with the objective of extending international standard modern banking services to various sectors of the society. Pursuing its objective, Nabil provides a full range of commercial banking services through its 28 points of representation across the nation and over 170 reputed correspondent banks across the globe. Nabil bank as a pioneer it introduces many innovative products and marketing concepts in the domestic banking sector, represents a milestone in the banking history of Nepal as it started an era of modern banking with customer satisfaction measured as a focal objective while doing business. Highly qualified and experienced management team manages operations of the bank, including day-to-day operations and risk management. Bank is fully equipped with modern technology, which includes ATM's, credit cards, state of art world-renowned Software from Infosys Technologies System, Bangalore, India and Internet Banking System and Tele-Banking System.

#### **Share Capital as on 16 July 2011 (32 Ashad 2068)**

Authorized Capital	Rs. 4,000,000,000.00
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Issued Capital	Rs. 2,029,769,000.00
Paid-Up Capital	Rs. 2,029,769,000.00

**Nepal Investment Bank Limited (NIBL)**

Nepal Investment Bank Ltd. (NIBL). previously Nepal Indosuez Bank Ltd., was established in 1986 as a joint venture between Nepalese and French partners. The French partner (holding 50% of the capital of NIBL) was Credit Agricole Indosuez, a subsidiary of one the largest banking group in the world. With the decision of Credit Agricole Indosuez to divest, a group of companies comprising of bankers, professionals, industrialists and businessmen. has acquired on April 2002 the 50%

shareholding of Credit Agricole Indosuez in Nepal Indosuez Bank Ltd. The name of the bank has been changed to Nepal Investment Bank Ltd. upon approval of bank's Annual General Meeting, Nepal Rastra Bank and Company Registrar's office with the following shareholding structure.

- A group of companies holding 50% of the capital
- Rashtriya Banijya Bank holding 15% of the Capital. p
- , Rasht-iya Beema Sansthan holding the same percentage. g

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The remaining 20% being held by the General Public (which means that NIBL is a Company listed on the Nepal Stock Exchange). NIBL was the first bank to introduce an account with a minimum balance of Rs 1. It is continuously doing well in terms of deposit collection and loan disbursement. It is the only bank in Nepal to be honored by the prestigious Banker "Bank of the year 2008" award.

Share Capital as on 16 July 2011 (32 Ashad 2068)

Authorized Capital RS 4,000,000,000.00

Issued Capital Rs. 3,011,372,125.00

Paid—Up Capital Rs. 3,011,372,125.00 C

(www.nibl.com.n\_p)

Bank of Kathmandu Limited (BOKL)

Bank of Kathmandu Limited (BOKL) started its operation in March 1995 with the objective to stimulate the Nepalese economy and take it to newer heights. BOKL with aims to facilitate the nation's economy and to become more competitive globally has been focusing on its set objectives right from the beginning. It is contributing for the sustainable development of the nation by mobilizing domestic savings and channeling them to productive areas. To glorify its corporate slogan "We make your life easier" BOKL puts in conscious efforts. BOKL has already started the credit card service to its customers and is on the way to start Internet Banking and Alert Service very soon. In Internet Banking, BOKL will provide Consumer e—banking (Core, Retail and Bill Payment) as well as Corporate e—banking facilities (Trade financing and web based Cash Management). The bank has to be honored by the prestigious Banker "Bank of the year 2011" award.

Share Capital as on 16 July 2011 (32 Ashad 2068) yn

Authorized Capital Rs. 2,000,000,000.00

Issued Capital Rs. 1,604,187,300.00

. Rs.1,604,187,300.00

Paid—Up Capital

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## 1.2 Statement of Problem

The financial institutions at present days are mounting and hence there is ample market for good and viable lending. Due to this sufficient return could not be achieved. The new commercial banks just share the existing market return rather from the new markets. Due to stiff competition in the market and improper management,

the challenges are facing by some of the commercial banks to invest their entire fund in profitable sectors.

Economic development of a country succeeds only when the development of the capital formation mechanism exists. The major cause of this chronic problem is the lack of economic development or the slow rate of the national economic growth. With the increased sophistication and liberalization of financial markets, this has made the problem of debt management one of the most important issues in economic policy. Keeping pace with today's up growing economy itself is a risky task and with that commercial banks are facing tough competition too. The present situation of the country has made the investment insecure to high extend. As a result, today lending has become very challenging. Commercial Banks have to seek for secured and productive investment opportunity, which definitely is a tough job.

In addition, another problem is the gradual increase in non—performing loans. Increase in Non-performing loans can be the result of present condition of the country. Due to instable political condition, insecurity and lot many factors, industries of Nepal are T closing down and thus are the investments. This has also arson another problem. Loan mobilization in hire purchase and housing loans are increasing than that in term loan. Terms loans are more productive and contribute more to the economy than hire purchases and housing loans. These kinds of situations reduce the income generation level in the economy, which again affects the timely repayments of the due installments of Loans and Advances. Moreover, while granting the loan, banks whichi T - do not analyze the documents submitted by the borrowers, are resulting in rising non-performing loan. 4 r ` a gi T , T \_.

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to improve the profitability situation of the bank. It is necessary to establish the higher creditability position of the bank. Credit is the most effective area in commercial bank. Thus lending management is considered as the main issues in Nepalese banking sector. This study will try to seek the answers of the following statements relating to commercial banks of Nepal.

- What is the lending strength in relative terms such as Investment to Loans and Advances and Investment. Loan and advances and investment to Total Deposit ratio. loan and advances to shareholder's equity ratio etc. of the selected commercial banks'?
- What is the Lending strength in Absolute terms such as loan and advances. non—performing loans, interest income from loans and advances. loan loss provision, net profit of the selected banks?
- Does the lending efficiency of the commercial banks contribute in its total profitability?
- Does internal performance caused for increase in non—performing loan?
- How does the commercial bank manage the lending portfolio?

### 1.3. Objectives of the Study

The Primary objectives of this study are to analyze the performance of NABIL, EBL, t BOKL & NIBL regarding lending quality and quantity and to recommend suggestion for the improvement thereof. Some of other objectives are:

- To analyze and measure the ratio and volume of Loans and Advances.
- To determine the lending efficiency of the commercial banks using different ratios.
- To examine the impact of deposit. Loan and Non-performing loan on profit of selected banks.

### 1.4. Focus of the Study »

A key factor in the development of an economy is the mobilization of the domestic p

resources, Financial institutions help in the process of resource mobilization. The importance of

catalyst in the process of economic growth of a country. The importance of financial institutions in the economy has grown to an enormous extent. The

government in turn is required to regulate their activities so that the financial policies

are implemented as per the requirement of the country. Policy such as lending to

priority and deprived sectors. Lending to the educated unemployed people. Lending for

creation of entrepreneurs in the society are certain examples which the government in a developing economy try to implement with the help of financial institutions. With the growing activities of bank after the NBL and RBB, new banking policy was introduced for establishment of international investment banks and joint venture banks in foreign investment with Nepalese co-operation. Its objective was to create healthy competitive banking system and provide cheap banking facilities to people.

Commercial banks are the heart of financial system. They hold the deposits on many persons, government institutions and business units. They make funds available through their lending and investing activities to borrowing individuals, business firm and government establishments. In doing so, they assist both the flow of goods and services from the producers to consumers and the financial activities of the government. These facts show the commercial banking system of a nation is important to the functioning of the economy.

Bank creates funds from its client to saving and lends the some to needing person or

business institutions in terms of loan, advances and investment. So, proper financial decision making is more important in banking transaction for its efficiency and lending management. It plays a vital role in the business succession, so efficient lending management is needed. This study deals with the lending position, nonperforming loan, lending portfolio management and relation of lending in profitability of the selected bank.

#### 1.5. Limitation of the Study

Every work has its own restriction and limitation due to the lack of time and knowledge. Despite the thoroughness of the research, it is not perfect.

It is limited to:

1. The study is limited to the lending practices of the selected banks.

2. The study is limited to the last five years data beginning from FY 2006/07 to FY 2010/11.

3. The study is presented just for the partial fulfillment of M.B.S. (Masters of Business Studies) degree. Following are the major limitations of this thesis.

The study is based on secondary data collected from annual reports published from the relevant commercial banks. Thus the result of analysis is accordance with the information and data mentioned in the annual report.

The sample taken is four banks for the analysis of the lending practices of the

whole population of the bank.

The study is limited to last five years data beginning from FY 2006/07 to FY 2010/11.

The sources of data i.e. the published reports, articles, journals and data on the website are assumed to be exact and truthful.

Standard normal performance level is not available especially in Nepalese

context. So, interpretations of data are depended upon common sense. In this context, concerned advice from experts is taken.

· The limitation and drawbacks of the tools used itself are also the limitations.

#### 1.6. Significance of the Study

There is very little research made by previous researchers on lending practices of commercial banks. The Nepalese financial market is growing day by day; New financial institutions especially finance companies and development banks; entering into the market and the existed finance companies and development banks; expanding their capital and switching into the commercial banks as the essential part of our economy and lending IS (me of fbi y \_\_g. A .;\_\_ 5 ff yvy, E l t . . » \_ ` ~ ? .

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hardly Therefore. this research will be very significant for the upcoming researchers and also to the people who are interested in this field. Moreover, as I am a management graduate willing to peruse my career in banking sector. this study will prove to be significant in my individual level to enhance my career in banking sector.

1.7. Organization of the Study

The study on the lending practices of NABIL, EBL. BOKL and NIBL has been divided into five chapters viz. Introduction. Review of Literature, Research Methodology, Presentation and Analysis of Data and Summary, Conclusion & Recommendation.

Chapter I: Introduction

It includes general background of the study, historical perspective of banking industry, overview of sample banks, statements of the problem, objectives of the study, significance of the study and limitation of the study.



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## Chapter V: Summary, Conclusion and Recommendation

The fifth & final chapter deals with summary of the previous chapters. It also includes conclusions drawn up and recommendations made for the further improvement of the area of the study.

Besides these chapters, Bibliography and Appendices are presented at the end of the study.

## **CHAPTER II**

### **REVIEW OF LITERATURE**

The review of literature is a crucial aspect because it denotes planning of the study. The main purpose of review of literature is to find out what works have been done in the area of the research problem under study and what has not done in the field of the research study being undertaken. For review study, the researcher uses different books, reports, journals and research studies published by various institutions, unpublished dissertations submitted by master level students have been reviewed.

It is divided in to two headings:

- ) Conceptual Review
- ) Review of Relevant NRB Directives
- ) Review of Related Articles, Journals and Thesis

#### **2.1 Conceptual Review**

The modern financial evaluation has greatly affected the role and importance of financial performance. Nowadays, finance is best characterized as ever changing with new ideas and techniques. Only efficient manager of the company can achieve the set up goals. If a commercial bank does not maintain proper lending policy, it makes the commercial bank more risky. If a commercial bank has inadequate lending policy, it must use proper lending policy in accordance to NRB directives.

Nepal Rastra Bank has been acting as the father figure of the commercial banks. NRB is the central supervisory authority that has every control over the running commercial bank. All the transactions commercial banks make are directed by the NRB. All the activities that commercial banks are authorized to do or restricted to do are listed out by the NRB. It is like the boundary of activities of commercial bank set by the NRB. There are NRB directives related with following areas, for commercial banks to confine them through their activities.

- ) Capital Structure

- ) Classification of Loans and provision for loan loss
- ) Per customer loan limits
- ) Collection of deposits
- ) About lending
- ) Consortium Financing
- ) Minimum liquidity requirement
- ) Interest rates
- ) Financial resource in the form of deposits, loans etc.
- ) Credit information and Blacklisting
- ) Statistical Documentation
- ) Formation of Branches and offices
- ) About Shares
- ) Guidelines to be followed

### **2.1.1 Principles of Good Lending**

Needless to say, lending is the major income generating activity of any commercial banks and it is also one of their main functions. Even though, commercial banks cannot just go on giving loan to just anyone and any institution. It is one of major income generating technique of banks. However, if loans are not distributed properly and cautiously then it may be the main cause of the failure of the company as well. In case loans were advanced carelessly and the borrower fails to pay out their debts, company can be history. Flow of money is lifeblood of banks and the bad loans arise there can interrupt the flow. Thus, it should be well analyzed beforehand to give out any loans. Below given are the factors whereupon any prospect loan should be analyzed.

- (i) **Safety:-** the bank should ensure that the money lent by them goes to the ideal type of borrower and is utilized in a proper way in pre-mentioned purpose so that it will not only be safe at the time of lending but will remain so throughout the transactions. Moreover, after serving a useful purpose in the

trade of industry where sum of lent money is utilized is finally repaid back with interest.

- (ii) **Liquidity:** - Besides 'safety' factor, it is also necessary that the money lent out must be repaid in accordance with agreed terms of repayment. In order to achieve this, the borrower must have reliable sources of sufficient income.
  
- (iii) **Purpose:** - The purpose of lending should be productive so that money not only remains safe but also provides a definite source of repayment.
  
- (iv) **Profitability:** - Financial institution should generate sufficient income to cover the expenses. Such expenses are interest expenses on deposits, staff expenses, office operating expenses, provision for depreciation on their fixed assets, provision of bad or doubtful debts; to pay bonus for staffs, income tax to government and of course dividend to its shareholders and plough back returns to expand its business volume. Considering these costs, financial institute should decide upon lending rate.
  
- (v) **Security:** - The primary objective of commercial banks is not to lend against security. It should lend on the basis of character, capacity of the borrower. However, security is considered as assurance of cushion to fall back upon in case of failure to repay the loan and interest dues by the borrower due to various reasons.
  
- (vi) **Spread:** - There is a popular saying that "Do not keep all the eggs in the same basket." If invested in a certain project and the projects fails whole business is ruined. "Diversification of lending is another important principle of good lending. An element of risk is always present in every loan advanced however secure it might appear to be. In fact, the entire lending business is

one of the taking calculated risks and a successful financier is in expert in assessing such risk. Thus commercial bank should diversify its lending program in various sectors of economy, business and industry and geographical areas.

**(vii)National Interest, suitability:** - Even if loan advanced satisfies all the aforementioned principles, still it might not be appropriate. The lending program may run contradict with national interests. Central bank has issued directives prohibiting commercial banks to allow particular types of loan and advances.

### **2.1.2 Loan Proposal Processing**

While granting and providing approval to the loan proposal any financial institution should undergo different process. The analysis and procedure of loan granting may be more detailed based on the volume or amount of loan. If the amount of loan is high then detailed analysis is mandatory. Generally, following study and analysis is performed while granting the loan.

#### **Proposal Submit**

Firstly, the proposal consisting of detailed information regarding the loan is sub mitted for demanding the loan to the financial institution. And the bank should start to study and analyze the proposal.

#### **Sector Analysis**

Before granting loan the bank needs to analyze about the type of loan. The loan demanded by the client is related to which sector should be analyzed. For example, whether the loan is consumer loan or financial loan etc. Similarly, the subsector e about the c also studied. Furthermore, the restriction (for example government restriction on the sector), local convenience or support, competition of the sector on

which loan is proposed is analyzed. If it seems to be viable from above studies the study is done about the client.

### **Client & Credit Information Analysis**

The market status or goodwill of the client is studied. Nature of client, capacity of client is analyzed. Whether the client is the regular consumer or the first to the bank, whether he is taking loan from other intuitions too or not, whether client is demanding loan as per the volume of business or not etc. are analyzed.

Credit analysis is primarily historical based on available credit information; it is compiled to make a prediction of future behaviour. In fact, credit analyst believes that history or past information is a clue to the future.

### **Credit information for consumer lending**

- (i) **Payment record:** - Past payment behaviour of the client (loan taker) is regarded as the most important factor judging credit quality. Regular payments of instalments of previously taken loan can be the example of regular payment records. Furthermore, whether the client is taking loan from other institutions or not is also studied. If, he is taking loan, then to what volume, should also be studied. If the clients taking loan above 10 lakhs from other institution then the bank need to demand credit information of client form that institution.
  
- (ii) **Income:** - Income consists of wages/salary, rental and business income if self-employed. These incomes are verified with employer/industry average – comparing with wage and salary of other employers of similar nature. In the case of business income, nature of business, sales turnover, profit margin cash flow analysis etc. are verified. Matching between the cash flow of client and the instalment of loan is conducted. If possible, a total asset (moveable plus immovable) of the client is also assessed.

- (iii) Residence:** - An address checking is a routine part of the verification. The size and types of residence are also indications of the applicant's housing expenses, social responsibilities and wealth. Plus point is if the customer is a permanent local resident. It is likely that he/she would pay his/her dues in time and there is less probabilities of him/her having any intentions of fraud.
- (iv) Marital Status:** - Information about single, married, widowed, divorced or separated marital status of the applicants is sometimes sought and considered important while accessing consumer credit. Marital relationship may affect income and obligations as well as person's happiness. Loan default and collection problems repeatedly arise from marital adjustments. Besides it is important that while granting loans, the spouse is taken as a personal guarantee.
- (v) Age:** - Age of the applicant may be another factor in accessing credit risk. Too young and old applicants may be regarded as high credit risk. Too young applicant are usually not financially established and often considered transient and uncommitted. Older persons are recipients of limited income and prone to illness. Thus, people who are aged within the working period of life should be more preferred to others.
- (vi) References:** - References from previous creditors, friends and business associates, persons who have treated others fairly and loyally are likely to give the same consideration to a new credit relationship.

### **Collateral/Security Analysis**

It is most important and critical factor while granting loan to the client. Assets and income that may be liquidated provide a backup means of payment when the income stream cease. Securities and estate without heavy debt payment are good reserve assets. Types of collateral, marketability of collateral deposited are studied. These

days, most of the client deposit their land and houses as collateral while taking loan. If the collateral is land, then the location, certificate of four boundaries are to be studied. If the land is located near the highway or in the city then it is good. For the large volume of loan, field study and valuation report of the land deposited as collateral is to be compulsorily conducted.

After above studies and analysis is done then as per the loan limit proposal is submitted to the concern authority for final approval. If the loan amount is large, the Board of Directors may sit the meeting and give final decision for the approval loan. After the loan is approved, collateral deposited are made banned to sale and use for other activities.

### **2.1.3 Commercial Credit Information**

In addition to similar kinds of information as consumer application, commercial credit information contains the following: -

#### **a) Financial Statement**

- (i) Usually balance sheet, income statement and cash flow statement certified by management and auditors.
- (ii) Shows the position, trend and flow of applicant's business.

#### **b) Customers and creditors listing**

- (i) Provide means and authorization to make inquiries with those doing business with the applicants.

#### **c) Credit Bureaus**

#### **d) Credit applications/interview etc.**

## 2.1.4 Analysis of Credit Risk

### Five 'C's of Credit

- (i) **Character:** - The quality of willingness to repay debts duly is ranked above all other considerations. The good character and intentions of the borrower is very important and thus should be seriously considered. Information about the character of the client can be gathered from his working place, references, neighbours and other places he is associated with. This job is tedious but should be carried out for safe investment.
  
- (ii) **Capacity:** - Repaying back as per the schedule made. The gross income, expenses and net income of the client/borrower should be analyzed whether the borrower lives on salary/wages or any other forms of income source. Whether the borrower has some extra income sources other than salary/wages that can be used to repay the scheduled instalments should be considered. It should be analyzed beforehand whether the borrower has enough income to pay the scheduled instalments.
  
- (iii) **Capital:** - Capital provides a cushion to absorb operating and asset losses that might otherwise harm debt repayment. This is in fact, is the assurance against the loans granted to the borrowers.
  
- (iv) **Collateral:** - Adequacy of collateral is a must to ensure the recovery of loan. In case of default, by any cause, the collateral kept should have value enough to recover the loan granted and interest borne by it. It is recommended that only 50% of the value of collateral to be granted as loan. But considering other factors like character of borrower and his credit worthiness, this percentage can be made flexible.
  
- (v) **Conditions:** - Borrowers may be under unfavourable economic conditions beyond their control. Repayment depends not only upon character, capacity and

collateral but also on those factors over which the borrower exercises little of has not control as for example natural calamities or drastic economic crises.

### **2.1.5 Basic requirements in a borrower**

There are some basic requirements that should be fulfilled by the client to justify him/herself as a probable borrower. Commercial Bank cannot lend money to justify anyone blindly. It should be confident regarding the trustworthiness and intentions of the probable borrower beforehand. The borrower, on the other hand, should provide the Bank with all pertaining documents that the company seeks to build confidence on borrower. The basic requirements borrowers are as follows:

#### **If the applicant is an individual**

- a) Applicant should be a Nepali citizen.
- b) Should have good knowledge about the work they intend to commerce.
- c) Normally the applicant should not have taken loan from any other similar kind of institutions.
- d) Applicant should present the job-planning scheme.
- e) Personal information.
- f) Business registration and income tax.
- g) Quotation and personal guarantee.
- h) Driving License.
- i) Others.

#### **If the application is partnership firm**

- a) The firm should be registered in related department.
- b) The person dealing with the borrowing of the firm should be specified in the partnership contract.
- c) Income tax registration certificate.
- d) And other required and possible items from point 1.

**If the applicant is private limited company or public limited company**

- a) Company should be registered.
- b) Working place, project place should be specified and all the assets should be in the name of the company.
- c) Audited Balance Sheet, Profit and loss Accounts and other required financial documents, at least of one year, should be presented.
- d) If the work place and/or project place is leased, the lease contract should be presented.
- e) The authorized person should apply for the loan.
- f) Loan amount applied must be within the limit of memorandum of the company or must be decided by the board.
- g) Decisions of the promoters.
- h) Personal information of the main person.
- i) Written personal guarantee of proprietors.
- j) Citizenship of promoters and proprietors.
- k) And other required and possible items from points 1 and 2

**2.2 Review of Relevant NRB Directives**

Funds used by commercial banks for the purpose of advancing of loans are that of public. Commercial banks collect deposits from public and it is very same fund they use to make profit. Thus, to prevent this public fund being miss-utilized and to protect the savings of public, NRB has given directives to the commercial banks regarding investment of public fund along with the directives to perform all other jobs of commercial bank. Since loan and advances and leased assets is the first and the main sector of investment, to minimize the risk here, NRB has specifically given guidelines relevant to loan and advances and leased assets in NRB directives for commercial banks 2066 No. 2, 3, 12 & 15.

### **NRB Directives No. 2/068**

Under this directive, using the authority of Nepal Rastra Bank Act 2058 section 79, NRB has given criteria for classification of loan and advances with accordance to calculation of loan loss provision. The main objective of doing this, as specified by NRB, is to minimize the risk of bankruptcy leading to endowment of public fund due to incautious investment in bad loan and advances.

As guidelines provided by the directives of NRB, licensed institution shall, as of end of Asoj, Poush, Chaitra and Ashad, preparation of statement of outstanding loan and advances classified on the basis of aging and submit the particulars as per the enclosed forms to Supervision Department of NRB within one month from the end of each quarter.

In the directives given by NRB, loan and advances are initially categorized as performing loan and non-performing loan. Pass loan and advances are defined as performing loan whereas Sub-standard, doubtful and loss loan fall under the categorization of non-performing loan. All loan and advances extended against gold and silver, fixed deposit receipts, credit card and against security of HMG securities and NRB bonds shall be included in “pass” category.

Loan cases like loan granted to the project which is not presently working or mis-utilization of loan (not been used for the purpose originally intended) or blacklisted or whose borrower has run away or absconding and declared bankrupt or whose securities are inadequate are also treated as bad loan and classified as non-performing loan even if they are within the due dates. Purchased and discounted bills, credit and guarantee not realized within 90 days from the due date are also categorized as loss loan. Bills have only two classifications either Pass or Loss.

Licensed institutions may reschedule or restructure loans only upon submission of a written 'Plan of Action' by the borrower which is resurrecting on the following grounds,

- Evidence of existence of adequate loan documentation and securities.
- Licensed institutions are assured on possibility of recovery of restructured or rescheduled loan. Restructuring means process of changing the nature of conditions of loan/facility, adding or deleting of conditions and change in time limit. Rescheduling loan means extending repayment period/time of credit taken by the borrower.
- In addition of the written 'Plan of Action' for rescheduling or restructuring of loan as per clause (1), at least 25% of accrued interest outstanding on date of rescheduling or restructuring should have been collected. Renewal of loan by collecting all interest can be classified as Pass loan. Loan loss provisioning is 12.5% for restructured or rescheduled loans.

### **Loan Loss Provision**

The loan loss provisioning on the outstanding loan and advances and bills purchases shall be provided on the basis of classification made as per this directive as follows.

<b>Classification of Loan</b>	<b>Loan Loss Provision</b>
Pass	1 Percent
Substandard	25 Percent
Doubtful	50 Percent
Bad loans	100 Percent

*Adjustment of loan loss provision is prohibited except under the following cases.*

- The loan has been completely written off.
- In the event of repayment of instalment or partial payments of loan, the loan loss provision has to be provided as per loan classification and write back the provisions related to amount of repaid loans.

- Where the instalment of principal and interest of restructured or rescheduled loan is serviced regularly for two consecutive years, the loan loss provisioning may be adjusted. However the amount, adjusted by writing back loan loss provision cannot be used for distribution of dividend or issue bonus shares by showing in the profit.

NBA taken over by the banks should be provisioned for loss as 25%, 50%, 75% & 100% in years 1<sup>st</sup>, 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> respectively till it is sold off.

Actions will be taken in cases on non-compliances of the directives given by NRB under section 100 of NRB Act, 2058.

### **NRB Directives 3/068**

#### **Single Borrower Obligator Limit**

This directive was imposed by NRB to minimize the risk that can arise due to concentration of loans and advances to one customer.

##### **a) Fixation of limit on credit and facilities**

- (i) For “A”, “B” and “C” class licensed institutions may extend to a single borrower or group related borrowers the amount of Fund based loan and advances up to 25% of the Core Capital Fund and Non-fund based off balance sheet facilities like L/C, Guarantees, acceptances, commitments up to 50% of its core capital fund. However, from the start of fiscal year 2067/68 the single obligor limit for both fund and non-fund based items is only 25%.

##### **b) Exemption in limit of credit and facilities**

The exposure limits per clause 1 above shall not be applicable in respect of the following: -

- (i) Credits and facilities extended against own fixed deposit receipts, HMG securities. NRB Bonds as well as against unconditional guarantees issued by

World Bank, Asian Development Bank and other International Finance Corporation including multilateral institutions and international rated banks.

- (ii) Loan and advances and facilities provided by “A” class licensed institutions to Nepal Oil Corporation and Nepal Food Corporation for the purpose of import of specified merchandise as LP gas, Petrol, Diesel, Kerosene and food items respectively.

**c) Related parties are to be considered as a group.**

**d) Submission of return on related customers.**

**e) Treatment as separate group.**

For the purpose of drawing limits in granting loans and advances, lease financing and giving other services, customers with personal relations are categorized in to a single group under the following conditions: -

- (i) In case one company has acquired 25% or more shares of another company then those both companies are considered as a single group.
- (ii) In case a director of a company is a shareholder of another company or his/her relative; spouse, son, daughter in law, unmarried daughter, adopted son, adopted unmarried daughter, parents, step mother and younger dependent siblings residing under the same roof or the companies who's 25% or more share are owned by above mentioned relatives individually or jointly.
- (iii) In case the firms; companies are legally connected in a group or members of such groups.
- (iv) If relatives mentioned in point (b) do not, individually or jointly own 25% or more shares of a company but had the following positions: -
  - a) Chairperson BOD
  - b) Managing Director of the company

(v) In case one customer or company has given cross guarantee to another customer or company.

**f) Provision of cent percent to minimize concentrated risk.**

In case the company has mobilized funds in loans and advances more than authorized, company has to make provisions of exceeding amount by 100%.

**g) Provision relating to sector credit**

Under the directive no. 3, using the authority of Nepal Rastra Bank Act NRB has given criteria for classifying loan and advances under different sectors and sub-sectors and also determined the amount of loan commercial banks are authorized to disburse under the given sectors and sub-sectors. The main objective of doing this, as specified by NRB, is to minimize the risk and to make sure the distribution of loan and advances into various sectors of economy.

Commercial Banks can sanction loan under following sectors as described in NRB Directive No. 3:

1. Hire purchase loan
2. Housing Loan
3. Lease Financing
4. Term Loan – Medium and Long Term only
  - 4.1 Agriculture and agro-based business
  - 4.2 Industry
  - 4.3 Business
  - 4.4 Education
  - 4.5 Health
  - 4.6 Tourism

- 4.7 Hydro-power
- 4.8 Others
- 5. Fund Based Merchant Banking Activities
  - 5.1 Venture Capital
  - 5.2 Bridge Financing
  - 5.3 Other Merchant Banking Transaction
- 6. Non-Fund Merchant Banking Activities
  - 6.1 Corporate Counselling
  - 6.2 Project Counselling
  - 6.3 Issue Management
  - 6.4 Share Underwriting
  - 6.5 Portfolio Management

An additional provision has to be made at the end of Poush and Ashad every fiscal year if the limit on sector or sub-sector wise loan amount is violated. Provision should be made of 25% of the exceeded loan amount.

### **NRB Directives 12/068**

The major clauses defined in this directive, forwarded as per the NRB Act 2058, section 88 and NRB Credit Information Regulation 2059 regarding the credit information and blacklisting, are as under;

#### **a) Details regarding Customer/Loaner to be sent to centre**

Licensed institutions should send the details of loan sanctioned amounting to Rs. 25 lacs or above within 15 days of month past as per Form No. 1 to the centre and should send the details as per Form No. 2 on quarterly basis till the loan is not paid.

#### **b) Ask for Credit Information Compulsorily**

Licensed institutions should compulsorily ask for credit information before providing new loan/renew of loan/restructuring or rescheduling the loan amounting to Rs. 10 lac or above.

**c) Process of Blacklisting**

Licensed Institutions should compulsorily recommend for black listing of related parties to the centre if the conditions provisioned in the directives is satisfied. The centre might blacklist the party within 15 days after proper verification if licensed institutions recommend for blacklisting.

**d) Licensed Institutions are banned to provide loan to Blacklisted client**

Licensed Institutions are banned to provide any new loan/facility, additional loan/facility, renew of loan/facility, remaining instalments of loan sanctioned on instalment basis and even accepting the guarantee to the blacklisted person, firm, companies or organized institutions.

**e) Conditions for Blacklisting**

Borrower having loan of Rs. 25 lac or above from licensed institutions or any individual should be blacklisted if any or all of the following conditions;

- ) If the repayment date of instalment of principle or interest of loan crosses one year. But, the BOD of the concerned institution may add the tenure of maximum 3 months considering the situation.
- ) If the miss utilization of loan and facility is proved.
- ) If it is proved that the material proved as security is miss utilized.
- ) If the Borrower is out of contact.
- ) If the file is cased against Borrower in the court.
- ) If deceive of amount by using fraud cheque, draft, foreign currency, credit/debit cards, bills etc. or if the court proves guilty for subject of attempting to deceive.
- ) If any individual, firm, company or organized institutions are proved to be involved in crime of financial transactions.

) The condition of not paying off the loan within the time frame mentioned in loan agreement by any individual, firm, company or organized institutions and in condition of punishment for recovery as per section 57 of Financial Institution Act 2063.

) In the condition of writing off the loan by the licensed institutions.

) Issue of non-cashable cheque or lack of sufficient balance in account.

**f) Provision of Withdrawing Name from Blacklist**

) Payment of Principle and Interest of matured loan.

) If the Board of Director of concerned licensed institution prolong the maturity period of loan deeming suitable and rescheduling or restructuring the loan within the realm of directive of this bank.

) In condition of approval from BOD of concerned licensed institutions regarding acceptance of credit liability by other person, firm, company or organized institutions and in such condition the accepting person, firm company or organized institutions is given the tenure of maximum 1 year and is blacklisted if the loan is not repaid or is not made regular within that period, the new person, firm, company or organized institutions should also be blacklisted.

**NRB Directive 15/068**

NRB has stated this directive no 15 regarding the interest rates, with the objective of creating a healthy competition between interests paid on deposits and interest gained from loans.

- a) Fixation of Interest Rates: - “A”, “B” and “C” class institutions are free to fix interest rates for both deposits and lending including the fixation of types of interest and procedures.
- b) Prohibition for fixing flat rate in interest: - Licensed institutions other than “D” class cannot fix interest rates on loans and advances.

- c) Interest rates to be approved: - Licensed institutions shall implement the interest rates for deposits and lending, procedure for calculation of interest, penal interest, commission and service charges only after approval. The institutions cannot vary (upward or downward) interest rates for deposits in excess of 0.5 percent over the published.
- d) Submission of return on interest rates: - The licensed institutions shall compulsorily submit particulars of interest rates of deposits and lending to Banks and Financial Institutions Regulation Department Nepal Rastra Bank within 7 days of each quarter ending. Further, the licensed institutions shall submit the whole arrangements and procedures relating to interest rates as per the clause 3 above at the time of initial implementation and changes made there within 7 days.
- e) Interest rates to be published: - The national level “A”, “B”, and “C” class financial institutions shall publish the particulars as per clause 4 above at times of each amendment made in the interest rates on deposits and lending on National Daily Newspapers. However, it should be published on quarterly basis whether it is changed or not. Regional/District Level institutions shall publish the particulars in the Regional/District level Newspapers. “D” class institutions may publish the interest rates putting the information on its notice board.
- f) Recognition of Interest Income: - The interest accruals on loan and advances shall be recognized as income on cash basis. Interest accrued shall be recognized in the year of cash realization.
- g) Action for non-compliance: - If the licensed institutions found not complying with the directives relating to branches/offices action may be initiated under the Nepal Rastra Bank Act, 2058.

### 2.3 Review of Articles, Journals and Thesis

Under this, various articles and dissertations have been reviewed for the purpose of clarification of lending practices and policies of the company under consideration.

#### 2.3.1 Review of Related Articles and Journals

Bhatta, (2004), in this article “Financial Policies to Prevent Financial Crisis”, Nepal Rastra Bank, the author has suggested that the financial markets have become an

exciting, challenging and ever changing sector in the recent years. The emergence of global financial institutions as a result of increased economic liberalization has raised a host of questions for financial planners and policy makers. The growth of financial markets has caused complexities in the management and if they are not managed and addressed properly with appropriate policies, then the result is the financial crisis. The financial crisis, which took place in Chile in 1992, Mexico in 1994, South Asian countries 1997, Russian Federation in 1998, Ecuador and Brazil in 1999 and Argentina in the late 2001 were the result of an abrupt growth in the size of financial markets posing serious challenges to their management.

According to the author of the article, the financial crisis in most of the markets, particularly in emerging market, undergo several stages. The initial stage is deterioration in financial and non-balance sheets and which promotes the second stage that is currency crisis. Due to the currency crises the financial institutions lack capacity of investment which will in third stage makes further determination of financial and non-financial balance sheets. This stage is the one that caused the economy to full – fledged financial crisis with its devastating consequences.

Pradhan (2004) in his articles, “The importance of loan information centre and its activities” published in NRB annual publication says that the loan information centre was established to fulfil the necessity of company working in relation to information related to loan. He further adds that the negative, trends like delaying the payments of principal and interest, deficient loan approval procedures, lack of constant inspection of project, lack of coordination between bank and finance companies have aided in the increase of non-performing loans ultimately affecting the national economy negatively. The author recommends the banks and finance companies to help the loan information centre by following the directives of Nepal Rastra Bank and utilizing the information obtained from the centre so that positive changes can be witnessed.

Shrestha S. (1999) in her articles, “Leading operation of commercial banks of Nepal and its impact on GDP” has presented with the objectives to make an analysis of contribution of commercial banks’ lending to the GDP of Nepal. She has set hypothesis that there has been positive impact of lending commercial banks to the GDP. In research methodology, she has considered GDP as the dependent variable and

various sectors of lending Viz. Agriculture, industrial, commercial service and general multiple regression technique has been applied to analyse the contribution.

NRB Economic Report (2010/11) is also reviewed about Money and Banking (4.1 to 4.5)

The liquidity pressure in the banking sector continued into the current fiscal year. The liquidity crunch happened to affect a number of banks and financial institutions despite overall management of liquidity through the monetary instruments. A cautious monetary management approach was used to cope with the potential high risk to the banking sector emanating from the BOP deficit of the previous year, higher price rise, and credit flows to the unproductive sector. Reason for the liquidity crunch in the banking sector is attributable mainly to the failure in boosting the public expenditure accompanied by decline in deposit collection rate. It is getting more of a challenge to managing liquidity amidst lower economic growth, higher rate of price rise, and the adverse BOP situation.

The financial system of the country is getting intensive, accompanied by the expansion of access to financial services with establishment of banks and financial institutions, and expansion of their branch offices. Banking business operates in an environment of risk due to its nature of work. As such, it is necessary to keep the financial sector as a whole strong and capable by protecting its financial stability from negative effects due to unhealthy competition with growing numbers of such institutions. For this, challenge is broadening the regulatory and supervision works, and enhancing the effectiveness and capacity of Nepal Rastra Bank. Besides, it is necessary for making the institutional governance and self – regulatory system effective.

Although financial condition of the two banks, one fully government and another partially owned, have improved as a result of their restructuring, the capital fund of both these banks is still negative. Making necessary arrangement for capital adequacy of these banks is challenge. As measures for reducing the level of non-performing loans of the banking sector as a whole, strengthening of the Revenue Tribunal, and make necessary preparation for the establishment of Asset Management Company are other challenges.

It is necessary to adopt the deposit guarantee scheme in all banks and financial institutions through its expansion for: (a) encouraging mobilization of savings for national economic development; (b) encouraging the bank and financial institutions for mobilization of such savings to the productive sector; and (c) enhancing the confidence of the people towards these institutions while protecting the interest of the people and depositors.

There has been a notable growth in the number of development banks, saving and credit cooperatives, and NGOs engaged in micro-finance transaction. As cooperative institutions occupy a major share in saving mobilization and credit flows, establishment of a second-tier supervisory institution with an arrangement for regulation, inspection and supervision of such institutions has become necessary. Besides, it has also become necessary to develop a structure suitable to geographical, economic and social condition of the country for increasing access to banking and financial services to the ultra poor, remote and rural areas for effectively addressing the issue of financial inclusiveness.

Shrestha M.K. (2007) "Fundamentals of Banking", the author has highlighted the concept and principles of good lending. In this book the author has said that lending is the fundamental function of commercial banks. The commercial banks fulfil the credit needs of various sectors of the economy as well as the investment on securities, whether it is government or non-government. The lending policies of commercial banks are based on the profit maximizing of the institution as well as the economic enhancement of the country. Out of their total income on an average 60 to 70% of income consists from lending activities which is called as exposure based income because banks are exposed to default risk. Moreover, the writer has mentioned that safety, liquidity, purpose, profitability, spread, security, national income and suitability etc. should be wisely considered by commercial banks for doing lending practices.

According to Greenworld & Joseph, the performer of no such sector is as contingent upon the future performance of other enterprises as is that of the financial sector. This contingency is high that it has always been difficult to the banking industry to pursue the objective of profit maximization as zealously as another industry could afford to. It

is this difference, which explains precisely why lenders cannot simply lend to those who are willing to offer the highest price (interest).

Radhaswami & Vasudevan (1979), “The mechanism of credit creation is used to expand the business. Fluctuation in the credit facilities granted by banks has an important bearing on the level of economic activity. Expansion of banks credit is followed by increase in production, employment, sales and prices. In a developing economy the banks offer more and more credit and increase the resources of the industries, thereby causing faster economic development. Banks play a decisive role in the industrial development of the country. The credit facilities extended by banks must be uniform and rational; otherwise there will be haphazard development of country. The flow of credit is very much like smooth and uniform throughout the organs of human body, so also credit should flow steadily and evenly through various sectors of the economy. If credit flow is artificially plugged or arrested, it would be irreparable harm to economy just as clotting of our blood vessels would lead to fatal results.”

“Lending is the essence of commercial banking; consequently the formulation and implementation of sound lending policies are among the most important responsibilities of bank directors and management. Well-conceived lending policies and careful lending practices are essential if a bank is to perform its credit creating function effectively and minimizing the risk inherent in any extension of credit.” (Cross; 1963:56).

“Lending is a form of trade. It means giving up purchasing power now in exchange for power in the future”. (Kohn; 1996:32).

“Commercial Banks perform a very important service to all sectors of the economy by providing facilities by lending and investing activities to the people. The primary function of commercial banks is the extension of credit to worthy borrowers. In making credit available, commercial banks are rendering a great social service, through their actions production is increased, capital investment are expanded, and a higher standard of living is realized. Although the investment activities of commercial banks are usually considered separately from lending, the economic effects and social results are the same” (Reed, Cotter, Gill and Smith, 1980:1-5).

### 2.3.2 Review of Related Thesis

Shahi (2001), on “Investment policy of Commercial Banks of Nepal”, recommended that commercial banks must mobilize its funds in different sectors such as purchasing of shares and debentures of other financial and non-financial companies. The banks should make continuous efforts to explore new competitive and high yielding investment opportunities to optimize its investment portfolio. Loan default in commercial banks is a result of various factors i.e. political influence, lack of necessary skills of project appraisal, improper collateral valuation, irregular supervision and lack of entrepreneurship attitude. He suggested enacting loan recovery act to enhance the function of recovery of loan.

The main objective of his study is to compare the investment policy of Nepal Bank Limited with other joint venture banks like NABIL, NGBL and NIBL. The conclusion drawn regarding the investment policy by comparing it with other three joint venture banks is inappropriate as NBL is a semi government which will be different in terms like interference level of government. NBL is unexposed to the global market unlike other joint venture commercial banks.

Tuladhar (2002), in his thesis “ A study on investment policy of Nepal Grindlays Banks Ltd in comparison to other joint venture banks of Nepal” has said that the basic objective of his study is to highlight the various aspects of the investment policy which are – to study the fund mobilization and investment policy with respect to fee based off-balance sheet transaction and fund based on-balance sheet, to evaluate the growth ratio of loan and advances and total investment with respective growth rate of total deposit and net profit, to evaluate the trends of deposit utilization towards total investment and loan & advances and its projection for next five years. He found the profitability position off NGBL is higher than NABIL and HBL. NGBL maintained successful liquidity position than others because of uncertain efficient return depositor may withdraws at high portion and invest in newly opened organization. The NGBL is providing less loan and advances in comparison to its deposits than other two banks and still it has largest profit. Its earning consistency is sound than the other two banks. The volume of growth of loan and advances is highest of HBL. He has concluded that joint venture banks are discouraged at lower level depositor and interested in higher

level of clients as paramount customers. He recommended following a liberal lending policy so that more percentage of deposits can be invested in to different profitable sectors as well as loan and advances. Investment and loan & advances are significant factor that affects the bank profitability.

Further to his study, he has focused to invest more percentage of deposit for NGBL, it might not be appropriate because liquidity is given high preference and importance in banking operation. When depositors demand money back, bank must return them to maintain its creditability. Bank needs to maximize its wealth, goodwill, no. Of branches so as to collect more scattered deposit of people and invest in the sectors which will give high return and is more potential for investment.

In the study he has done empirical study of customers view regarding adopted investment policy of concerned joint venture banks and distributed to one hundred customers at the bank to collect primary data for the analysis. He has used secondary data, reports, financial and statistical tools for the data analysis.

Chaudhari (2003), in his thesis “A study on Investment policy of Nepal Indosuez Bank Ltd (NIBL) in comparison to Nepal SBI Bank Limited” has compared the investment policy of Nepal Indosuez Bank Ltd. with Nepal SBI Bank Ltd. the main objective of his study is to examine the liquidity, asset management and profitability position, investment policy, the growth ratio of loans and advances and investment to total deposit and net profit of NIBL in comparison to SBI and to find out the trend of deposit utilization and its projection for next five years. He has found out that SBI’s return on loan and advances does not seem satisfactory since the average return is 2.6% whereas NIBL has a better performance of return of 8% from consistency point of view, NIBL’s ratio is completely consistent whereas SBI’s ratio is highly deviated since CVs are 0 and 53.85% respectively.

In the recommendation part, he has stated that loan and advances to total deposit of NIBL is also lower than that of SBI. And it is in decreasing trend. Therefore, to improve the situation in future NIBL is recommended to be more liberal in providing the loan and advance and get the better result. It has to pay proper insight towards cash reserve ratio to make it stronger and to mobilize the excessive fund in a profitable sector. It should invest more on profitable sectors rather than focusing its investment

on government securities as it yields lesser return. It should synchronize between deposit collection and investment even though they are different activities. NIBL is to be more liberal in providing the loan and advances and gets the better result. As the larger the covered area, the stronger will be the portfolio and bigger the amount of advance will become.

He further recommends NIBL to expand its services in rural areas and provide banking service to the rural dwellers also, as it has limited itself only in the urban areas. It has also to thoroughly implement the NRB directives by providing banking facilities to accelerate the rural areas economic development of the country. In his study he found out that “NIBL had earned high profit because its services are only for well off. It enjoys in paying penalty interest instead of not granting loan in priority sector. So NIBL is recommended to invest in priority and deprived sectors rather than paying penalty.

He has taken secondary data only for the study and has used various financial and statistical tools for the data presentation and analysis. Data which are related to fund mobilization as loan and advance and investment on government securities and other financial institutions are considered. In the study he has studied only a part of the loan under the investment policy finding the relationship between loans and advances with various variables. As his thesis is mainly related to investment policy he has focused mainly on the investment part explaining some of the relations of loans and advances.

Khadka (2004), in her thesis on “ A comparative study on Investment Policy of Commercial Banks” in which she has taken NABIL, SCBNL and NIBL banks as commercial banks and taken as average industry to compare with NBL. The specific objective of her study are to evaluate the liquidity, asset management efficiency and profitability position of NBL in comparison to other commercial banks and to find out the relationship between deposits and total investment, deposit and loan & advances and net profit and outside assets. She has found out that there is not much difference between the mean ratio of loan and advances to current assets of NBL and other commercial banks. The mean ratio of NBL is slightly higher than that of other commercial banks. However, NBL’s ratios are found to be less uniform in comparison to other banks. It shows that the liquidity position of NBL is comparatively better than

that of other banks. In contrast, the ratios of NBL are found to be less consistent than that of other commercial banks.

Shrestha (2005), "A comparative study on Investment Practices of Joint Venture Commercial Banks with Special reference to Nabil Bank Ltd, Standard Chartered Bank Nepal Limited and Nepal SBI Bank Limited", has compared the investment policy adopted by Nabil, SBI and SCBNL with each other. The specific objective of his study are to evaluate the liquidity management, asset management efficiency, profitability, risk position and investment practices of Nabil, SBI and SCBNL, to project the deposit and investment trends of the sample organization.

He had figured out the problem, conclusion and recommendation as follows:

" Commercial Banks are more emphasized to be making loan on short term basis against movable merchandise. Commercial Banks have a lot of deposits but very little investment opportunity. They are even discouraging people by very low interest rate and minimum threshold balance.

Commercial banks invest their funds in limited areas to achieve higher amount of profit. This is regarded as a very risky step. Which may lead to lose in profit as well as principle. The credit extended by commercial banks to agriculture and industrial sector is not satisfactory to meet the growing need of the principle.

He has concluded that since the liquidity position on Nabil and SCBNL have not found satisfactory, it is, therefore, suggested them to improve cash and bank balance to meet current obligation. SCBNL's loans and advances to total deposit ratio is low at all, it is recommended to follow liberal lending policy for enhancement of fund mobilization. It is recommended to NSBI Bank that it has to enhance off balance sheet transactions, diversifying their investments, open new branches, play merchant banking role and invest their risky assets and shareholder's fund to gain higher profit margin.

Nabil and SCBNL are recommended to increase cash and balance to meet current obligations and loan demand.

Joshi (2006), on "A study on financial analysis of NIBL". The main objectives of her study are to examine the overall financial position of NIBL, to examine liquidity ratio,

profitability ratio and ownership ratios of the bank and to analyze the bankruptcy score of the bank for the period of five fiscal years from 1997/98 to 2001/02. She has found that the analysis of the banks shows that the deposit have been increasing gradually during the study period i.e. (2053/054 to 2057/058). However, the rate of increase was comparatively low in the year 1997/98 than in the year 2001/02. Total loans and advances have been also increasing. The total investment of the bank has been increasing over the years, which is mainly due to banks strategy of safe lending and also as a result of increase in customer deposits and limited opportunities for prudent lending. As the loan and advances from the bank is increasing provision for loan loss has also been increasing. The banki has been holding adequate provision for losses over the years and the general loan loss provision was 4% in average of the total risk assets.

In her study she has recommended that the bank should focus more on non-risky lending opportunities such as mortgages, housing loans and personal loans. It should carefully examine safety of principle as well as sources of repayment, capital structure, requirement and credit worthiness of borrower for providing credits. In other words, credit manager should evaluate credit risk by considering well-known five C's of credit viz character, capacity, capital, collateral and conditions.

Further, she recommends that the bank should invest more in loan and advances and less in government securities. However, she has not explained the relation of investment in government securities in absolute terms.

The financial analysis of NIBL has been analyzed and interpreted in this thesis. Analysis on terms of loan and advances in simply presented with comparison with the precious year data only. On the loans and advances part also, only simple comparison has been done. Whether the loan classification and provisioning of loan, investment in priority and deprived sector loan, investment regulation of NRB's directive has been followed or not has not been explained.

Shrestha (2007), " Impact and Implementation of NRB Guidelines (Directives on Commercial Banks" – A Study on Nabil Bank Limited and Nepal SBI Bank Limited" found out that both the Nabil Bank and Nepal SBI Bank have been fully implementing the NRB's directives. The main objectives of her study are to review directives of

NRB related to commercial banks. Her study concluded with the broad objective of examining the state of NRB functions in the commercial banks in Nepal. Capital Adequacy Ratio of Nabil and Nepal SBI are 13.40% and 12.86% respectively which are more than 9%. Banks are following the directives but in some cases such like supplementary capital and balance at NRB there is shortfalls. The excess amount of core capital in supplementary capital and 1% excess amount of total deposits in balance at NRB can compensate this shortfall. The banks have categorized the loan amount into four different categories as per NRBs directives. The increasing loan loss-provisioning amount decreases the profit of the banks. The change in the single borrower limit has brought down the limits of the fund based and non-fund based loans which have resulted to reduce loan exposure to banks.

In her thesis study she has recommended that both Nabil and SBI banks to increase its supplementary capital as it has shortfall in comparison with NRB guidelines and to meet the supplementary capital adequacy ratio even though it can be compensated by the excess amount of core capital. The supplementary capital needs to be increased by Rs. 122.74 million in Nabil Bank and Rs. 125.57 million in Nepal SBI Bank. She says liquidity and profitability are like two wheels of one cart so banks cannot run in the absence of any one of them. One can be achieved only at the cost of the others. Only liquid banks can attract lower core deposits, which helps in reducing interest expenses and give loan to good customer at lower rate, which results in requirement of less provision and high net profit. So banks should increase their primary reserve now to maintain the liquidity risk due to scrap out the secondary reserves. On the basis of finding, Nabil Bank has shortfall of Rs. 140.74 million thus it has to increase its balance at NRB by such amount for better performance even after adding 1% excess amount of cash of total deposit.

Primary data has been used in order to get the view of bankers on the directives issued by NRB. Questionnaire related to NRB Directives (1-5) are used to collect data for the study and implementation of directives by commercial bank. Secondary data are also used for the analysis. On this study the general directives are taken as guidelines. So all directives are not considered for study. Only the directives issued in 2001 and 2002 are considered for the study.

Bista (2008), "NRB directives implementation and impact on selected commercial bank in Nepal" analysed whether the sample banks have been following the NRB directives related to commercial banks and its impact on their operation. The major objectives of the study were:

- )] To examine whether the banks have been following the directives provided by NRB
- )] To analyse the impact to the changes in the NRB Directives on the performance of the commercial banks
- )] To inspect whether NRB has been regularly monitoring the activities of commercial banks.

The study concluded that some directives of NRB should be revised which should help to bring prosperity not only to the shareholders but also to the depositors, the employees and the economy of the country as a whole. It also suggested that commercial banks have to come up with a stronger internal audit department to make sure that the directives are properly implemented. Banks need to give priority in Human Resource Development to monitor and collect already disbursed loans. Also, NRB should be more practical while issuing the directives which should not issued to meet the international standard only but they need to be applicable in context of Nepal as well.

Maharjan (2009), “Loan Management of Nepalese Commercial Banks” in which he examined the loan management of the commercial banks in Nepal.

The main objectives of the study were:

- )] To determine how for the banks are investing in the priority sector and the deprived sector.
- )] To determine the trend of the deposit and the loan
- )] To determine the loan loss provision made by banks

The researcher concluded that loan and advances are the profitable assets for the banks and it very risky too. Due to this reason, the loans and advances should be effectively managed and controlled. The study suggested that the banks should follow the NRB directives strictly for effectiveness and better financial status of the banks.

Shahi (2010), “ Lending Operation and Practice of Joint Venture Banks in Nepal”, has examined the lending operation and practice of joint venture banks.

The main objectives of the research were:

- )] To determine the liquidity position
- )] To measure the banks’ lending strength

- ) To analyse the portfolio behaviour of lending and measuring the ratio and volume of loans and advances made in agriculture, priority and productive sector.

This research has concluded that the high volume of liquidity shows the high degree of lending strength. The situation has been prevailing in all of the banks taken into consideration for the study. The lack of reliable lending opportunities and fear of losing the principle in rural sector has been keeping the same banks to less orient towards the lending functions. Hence, the government should take appropriate actions to initiate these banks to attract to flow credit in rural economy.

Karki, (2011), in his thesis entitled “A comparative analyses of financial performance of NABIL an SCBNL”, has pointed out following objectives:

- ) To evaluate liquidity position of both banks.
- ) To analyze comparative financial performance of both banks.
- ) To study the comparative position of both banks.
- ) To offer a package of suggestion to improve the financial performance.
- ) To identify the relationship between interests earned and operating profit.

The research has been major findings of this study as SCBNL has efficiently operated its long-term fund, deposit and assets to generate more profits. Liquidity position of NABIL bank is favourable in many cases it seems excessive. The proposed recommendation for these banks are to reduce its excessive non-performing assets (cash and bank balance) and invest on the income generating current assets (treasury bills), while SCBNL must strength the liquidity position. Comparatively SCBNL's profit ability position is better than that of NABIL.

#### 2.4 Research Gap

There is a certain gap between the present research and past research. Previous research conducted generally on investment policy of commercial banks of two banks. In some cases, there was also found the investment policy of maximum of four banks without any ranking criteria. Those analyses expressed all items in the statement in the form of amount. The previous researchers did not disclose the practical lending policies, which is practiced by the commercial banks. Thus to fulfil this gap the present research is conducted. It covers top four commercial banks, which is selected top ten yearly trade of NEPSE in the F Y 2010/11. The analysis based on expressing

all items in the statement as percentage. It is modern approach to evaluate the lending practices.

NABIL, EBL, BOKL and NIBL are the leading commercial banks of the country having the huge market share and its investment activities. Most important point to remember about lending policy is that every financial measure should be compared across time and across over same line of companies to be meaningful. Prior research has been conducted on the basis of traditional lending practices. The value of the approach was quantitative relations. The world is becoming more dynamic and subject to rapid changes. This research will be based upon the modern approaches to lending practices; which included comparable group approach and consideration of economic and strategic factors where feasible. Thus, the research will be an interest to wide range of its stakeholders other government regulatory interests. This may be the first effort to performance evaluation of top four commercial banks with sufficient time frame in a systematic manner.

## **CHAPTER – III**

### **RESEARDCH METHODOLOG**

The prime objective of this study is to assess the lending practices and policies of selected joint venture banks. This chapter is related to the Research employed in the entire aspect of the study. “ Research may be defined as the systematic and objective analysis and recording of controlled observations that may lead to the developments of generalizations principles or theories, resulting in prediction and possibly ultimate controls of events”. Thus, the chapter is to stress on the different method and conditions, which are used while conducting this study. This chapter includes the research design, Data collection techniques, data collection procedure, population and samples and method of data analysis.

#### 3.1 Research Design

Research Design is a plan for the collection and analysis of data. According to Paul and Tull, a research design is the specification of methods and procedures for acquiring the information needed. It is the overall operational pattern of framework, of the project that stipulates what information is to be collected from which sources by what procedures. If it has a good design, it will ensure that the information obtaines is relevant to the research questions and that it was collected by objective and economical procedures.

Research design is the plan, structure and strategy of investigation conceived so as to obtain answers to research objectives through analysis of data. The first step of the study is to collect necessary information and data concerning the study. Therefoe, research design means the definite procedure and techniques, which guides the study and the ways to do the study. This, in fact, is the specific presentation of the various steps in research process. These steps include the selection of a research problem, presentation of the problem, formulation of hypothesis, methodology, survey of literature and documentation, data collection, interpretation, presentation, report writing and bibliography.

The basic objective of this study is to evaluate the lending structure of four commercial banks under study. The research design of this study is analytical as well as descriptive approaches to evaluate the financial performance of these banks. Basically this study is based on secondary data and the past five years data from 2006/07 to 2010/11 will be used for the finding of objective.

### 3.2 Populations and Sample

At the end of fiscal year 2010/11, there are 31 commercial banks licensed by NRB are operating in Nepal. This whole number of bank is the population. However, while conducting the research four banks out of 31 has been taken as the samples for the study. It means, more than 12 percent of the population has been taken as the sample for the preparation of this research. The sample was collected by random selection of the commercial banks. Due to the easy availability of data and the popularity among the banks, the sample banks are selected.

### 3.3 Sources of Data

All the data necessary for the accomplishment of the research are collected from secondary sources. Besides, necessary suggestion and ideas are taken from the experts either related to the selected bank or outside the banks as per the requirement. Other sources of data are summarized below:

- ) Annual report of NABIL, EBL, BOKL and NIBL.
- ) Bulletin and reports of concerned bank.
- ) Related URL.
- ) Materials published in newspapers and magazines.
- ) Other related journals, periodicals, books and booklets.

### 3.4 Data Collecting Procedure

The annual reports of respective commercial banks are collected by going to the share department of respective banks. NRB economic report 2009/10 was brought from my friend Surendra Prasad Gupta who had taken it from Research Department of Nepal Rastra Bank. The internet also proved to be a very good source of data. Various

websites were used for the collection of data which are listed in the bibliography. After the collection of data they have been grouped according to their nature in their tabular and chart to pick up relevant data. These data are then presented and refined for the purpose of the study and analysis.

### 3.5 Methods of Data Analysis

The data presented in the study will be analyzed by using following tools and techniques for the accomplishment of the research.

#### 3.5.1 Financial Tools

In this research study, there are various financial tools but only selected ratios are used on the study.

##### 3.5.1.1 Ratio Analysis

The relationship between two accounting figure, expressed mathematically, is known as financial ratio (or simply as ratio). A ratio is simply one number expressed in terms of another and as such it expresses the quantitative relationship between any two numbers. Ratio can be expressed in terms of percentage, proportion and as a coefficient. “The technique of ratio analysis is a part of the whole process of analysis of financial statement of any business of industrial concern especially to take output and credit decisions – through this technique, a comparative study can be made between different statics concerning varied facets of a business unit. Just as blood pressure, pulse and temperatures are the measures of the health of an individual, so does ratio analysis measure the economics of financial health of business concern. Thus, the technique of ratio analysis is of a considerable significance in studying the financial stability, liquidity, profitability and the quality of the management of the business and industrial concerns.” (Kothari; 1994:1-264)

As far as we are concerned about the financial ratio, a ratio between two relevant figures, which provide a certain relation, and have negative or positive correlation between them will only be studied. Since comparing two incomparable figures and their ratios give no idea and judgement on analysis and its remains as an absurd figure only. This section has been divided into following sub-sections.

##### 3.6.1.2 Assets/Liability management ratios

Asset/Liability Management Ratio measures the proportion of various assets and liabilities in Balance Sheet. The proper management of assets and liabilities ensures its effective utilization. The banking business converts the liability into assets by way of its lending and investment functions. Assets and liabilities management ratio measures its efficiency in multiplying various liabilities in performing assets. The following are the various ratios relating to assets liability management, used to determine the lending strength of the subjected finance companies.

- (i) Investment to Loans and Advances and Investment Ratio
- (ii) Loans and Advances and Investment to Total Deposit Ratio
- (iii) Loans and Advances to Shareholder's Equity Ratio

#### 3.5.1.3 Activity Ratio

Activity ratio measures the performance efficiency of an organization from various angles of its operations. These ratios indicate the efficiency of activity an enterprise to utilize available funds, particularly short-term funds. The following ratios are used in this study to determine the efficiency, quality and the contribution of loans and advances in the total profitability.

- (i) Loan Loss Provision to Total Loan and Advances Ratio.
- (ii) Non-performing Loans to Total Loan and Advances Ratio.
- (iii) Interest Income from Loans and Advances to Total Income Ratio.
- (iv) Interest Suspense to Total Interest Income from Loans and Advances Ratio.
- (v) Loans and Advances to Total Deposit Ratio.
- (vi) Interest Income to Interest Expense Ratio.

#### 3.5.1.4 Profitability Ratio

Profit is the difference between the revenues and the expenditures over a period. Profit is the main element that makes an organization to survive. The profit, in other hand, measures the management ability regarding how well they have utilized their funds to generate surplus. The given ratios are used to determine the efficiency of the lending, its quality and contribution on total profitability.

(i) Net Profit to Shareholder's Equity Ratio.

(ii) Earnings per Share (EPS).

### 3.6.2 Statistical Tools

Statistical Methods are the mathematical technique used to facilitate the analysis and interpretation of numerical data secured from groups of individuals or groups of observations from a single individual. The figures provide detailed description and tabulate as well as analyze data without subjectivity, but only objectivity. The results can be presented in brief and precise language and complex and complicated problems can be studied in very simple way. It becomes possible to convert abstract problems into, figures and complex data in the form of tables. The various statistical tools used in this study to analyze the collected data are as follow: -

#### 3.5.2.1 Standard Deviation (S.D.)

The measurement of the scatterness of the mass of figure in a series about an average is known as dispersion. The standard deviation measures the absolute dispersion. The greater the amount of dispersion, greater will be the standard deviation. A small standard deviation means a high degree of uniformity of the observation as well as homogeneity off a series. In this study, standard deviation fo different ratio is calculated. It is denoted by “

Standard Deviation () =

#### 3.5.2.2 Coefficient of Variation (C.V.)

The coefficient of variance measures the ratio of the standard deviation to the mean expressed in percent. It is calculated as under: -

C.V. =

Where,

= standard deviation

= mean value of variances

Coefficient of variance is also useful in comparing the amount of variation in data groups with different mean. It is the relative measure of dispersion. A distribution with

smaller coefficient is said to be more homogeneous than the other. On other hand, a series with greater coefficient of variance is said to be more variable of heterogeneous than the other (Gupta, S. C.; 2000:416).

### 3.5.2.3 Correlation of Coefficient

The coefficient of correlation measure the degree of relationship between two sets of sigma. There is various method of finding out coefficient of correlation but Karl Pearson's method is applied in the study. The result of correlation coefficient is always between -1 and +1. It is indicated by r. When r is +1, it means there is perfect relationship between two variables and vice-versa. When r = 0, it means there is no relationship between two variables. The compute formula is mentioned below:

r =

### 3.5.2.4 Coefficient of Determination:

It is simply the zooming of correlation coefficient. It also measures the degree of relationship between the two variables. When the correlation coefficient comes in very small denomination then coefficient of determination helps to understand it more precisely by zooming it. It is denoted by r<sup>2</sup>.

### 3.5.2.5 Probable Error

Probable error of the correlation coefficient is denoted by P. E. It is used for the testing the reliability of the calculated value of r. P. E. is defined by: -

P.E.(r) =

Where,

P.E. (r) = Probable error of correlation coefficient

r = correlation coefficient

n = number of observation

### 3.5.2.6 Trend line/Regression

The literal meaning of the word "regression" is stepping or returning back to the average value. The term was first developed by Francis Galton in 1877. Regression is

the statistical tool with the help of which we can estimate or predict the unknown value of one variable from the known value of any other variable. Assuming that the two variables are closely related, we can estimate the value of one variable from the value of another. The variable whose value is given is called “independent variable” and the variable whose value is to be predicted is called “dependent variable”.

The regression equation of y on x is expressed as;

$$Y_c = a + bx$$

Where,

$Y_c$  = value of y computed from the relationship for a given x.

“a” and “b” are constants and also known as the parameters of the line. The parameter “a” determines the distance of the line directly above or below the origin, while parameter “b” determines the slope of the line i.e. the change in y with per unit change in x. X is an independent variable and y is dependent variable.

### 3.6 Method of Analysis and Presentation

Various applied methods of analysis are as simple as possible proper financial and statistical tools are used and result are presented in tables and also shown in diagram too. Detailed calculations, which cannot be shown in the main body part of the research report, are presented in Appendix tables at the end of the research report. Chart, diagram, and graphs have been used for making report simpler and easier to understand.

## Chapter IV

### DATA PRESENTATION AND ANALYSIS

The basic objective of analyzing the financial performance and interpretation is to highlight the lending strength of the commercial banks. Lending strength is that important aspect of any banks, which, if not kept in track while performing the functions, can lead to very critical situation. This, in fact, shows the situation of commercial banks in terms of investments in loans and advances. Whether the company is lending in accordance with the deposits it is collecting and the investments made by the shareholders or not should be analyzed regularly. Any idle deposit is loss to the company. Here, under this topic, an attempt is made to analyze the lending strength of the commercial banks under study in relative terms as well as absolute terms.

#### 4.1 Measuring the Lending Strength in Relative Terms

The lending strength of commercial banks under study is measured in relative terms in this section. The relationship between various assets and liabilities of the balance sheet has been established to show the relative strength of lending strength of each commercial bank comparatively.

##### 4.1.1 Investment to Loans and Advances Ratio

This ratio measures the contribution made by investment in total amount of loans and advances and investments. The proportion between investment and loans and advances depicts the management attitude towards risky assets and safety assets. This also measures the risk that the company is taking in its investment. The high ratio indicates the mobilization of funds in safe area and vice versa. However, safety does not provide with satisfactory return, as is said, "No" risk no gain". Thus, a compromising ratio between risk and profit should be maintained.

Table 4.1

Investment to Loans & Advances

Fiscal year	Ratios			

	NABIL	EBL	BOKL	NIBL
2006/07	0.5625	0.3539	0.3184	0.3763
2007/08	0.4568	0.2686	0.2571	

(source: Annexure II)

Table 4.1 shows the ratios of investment to Loans and Advances. NABIL bank is the highest ratios and BOKL is the lowest ratios on the study period of sample bank. The ratios ranged from 0.5625 of NABIL and 0.1806 of NIBL in different fiscal years. NIBL has the least ratio throughout the study period keeping aside the least ratio 0.1806 in the fiscal year 2010/11. Analyzing the 5-year data of all the four commercial banks, it is noted that no single bank has a steady increase in the ratio throughout the period. In the initial period BOKL is the lowest ratios and at the end of the period NIBL is the lowest ratios. The trends of the all sample bank are decreasing from study period. The ratio of EBL and BOKL in fiscal year 2010/11 is nearly equal at 0.245.

The mean of the sample banks are 0.4339, 0.2595, 0.2414 and 0.246 of NABIL, EBL, BOKL and NIBL respectively and NABIL is the highest mean and standard deviation (risk) and BOKL is the lowest mean and risk of the selected banks on the study period.

The C.V. of NIBL is highest of all sample banks figuring at 28022% which reveal that there is high variability in the ratios of NIBL. Similarly, NABIL has the lowest C.V. of 17.22% whereas the C.V. of EBL and BOKL are 21.41% and 19.31% respectively. Furthermore NABIL is sound variability in the ratios of loan and advance better than

other three banks and NIBL is high variability in the ratios of investment to loan and advances.

The figure of the investment to loan and advance presented below.

Figure 4.1

Investment to Loans & Advances

#### 4.1.2 Loans and Advances and Investment to Total Deposit Ratio

Loans and Advances and Investments are the major area of fund mobilization. This is the major area where the funds collected as deposits are channelized. The first part, loans and advances is more crucial and also bears more risk than investments but also gives the higher return. Whereas, the second half, investments has lesser risk and gives lower return in compare to loans and advances. Loans and Advances and Investment to Total Deposits ratio indicate the firm's fund mobilizing power in gross. Total deposits collected, against giving interest to the customers, is the total amount available for investments. Loans and advances and investment are the major areas where the companies can mobilize the funds with some returns. Any idle deposits mean loss to the company. Thus, this ratio measures how well the deposits have been mobilized. In other words, we can say that this ratio measures what part of deposits are generating income for the company to give out interest to the deposits and also make profit.

Table-4.2

Investment and Loans & Advance to Total Deposit

From the table 4.2, shows the ratio of Investment and Loans and Advances to Total Deposits. This means the portion of deposit being mobilized to generate income. The ratios range from 0.9128 of EBL in year 2008/09 to 1.06 of NABIL in year 2006/07. NABIL has the highest ratios throughout the period followed by BOKL, NIBL and EBL.

NABIL and EBL has highest ratio of 1.0645 and 1.0484 in 2006/07, whereas BOKL and NIBL has highest ratio of 1.035 and 0.9831 in the year 2010/11 and 2007/08. EBL has the lowest ratio throughout the study period. The ratios of the entire sample bank are decreasing in year 2009/10 and increasing in year 2010/11. None of the companies showed a steady increasing trend of the ratios. All the banks have a slight ups and down in the ratios in across the period of five years.

The mean of the entire sample banks are 1.0229, 0.9566, 0.9940 and 0.9668 of NABIL, EBL, BOKL and NIBL respectively. NABIL has the mean highest; EBL is highest standard deviation (risk) and lowest mean. The C.V. of EBL is highest with 6.22% which reveal that there is high variability in the ratios of EBL. Similarly, the lowest value of C.V. is of NIBL at 1.76% which indicates that NIBL has more consistent performance in fund mobilization.

Figure – 4.2

Investment and Loans & Advance to Total Deposit

#### 4.1.3 Loans and Advances to Shareholder's Equity Ratio

Shareholders equity consist of share capital, share premium, reserves fund, retained earnings etc. The ratio between Loans and Advances to shareholders equity shows how far the shareholder's equity has been able to generate assets to multiply its wealth. Shareholder's equity is the investment made by shareholders in the company and loans and advances mean mobilization of that invested funds in profit generating sector. Thus, this ratio measures size of the business and their success in converting liability into assets.

Table – 4.3

Loans and Advance to Shareholder's Equity

Table 4.3 shows the ratios of loans and advances to shareholder's equity. The ratios range from 7.1733 of BOKL in 2010/11 to 12.9422 of EBL in 2006/07. The ratio of merely the NABIL is in increasing trend whereas the ratios of rest three banks are fluctuating. This fluctuation is probably due to increase in the shareholder's equity of the companies in different years.

The mean ratios of all the commercial bank are 8.4695, 10.7626, 8.4957 and 9.0557 of NABIL, EBL, BOKL and NIBL respectively. EBL has the highest mean ratio whereas NABIL has the lowest and EBL has the highest S.D. ratio whereas NABIL has the lowest. It can be concluded that they have not succeeded in increasing loans and advances in proportion to the size of their capital. The C.V. of EBL is highest of 11% which real that there is high variability in the ratios of EBL. Similarly, the lowest value of C.V. is of NABIL whose value is 5.29%. Therefore, EBL is high variability in the ratios of loan and advances to shareholder's equity.

Figure – 4.3

Loans and Advance to Shareholder's Equity

#### 4.2 Measuring the Lending Strength in Absolute Terms

In this topic, the various variables in their absolute values are measured individually. The value of individual variables enables to measure the gross contribution of respective commercial bank in those aspects. The ratio analysis merely describes the ratio between the two variables but does not tell about the absolute value of those variables. Thus, in this section, some of the important individual variables in their absolute value of Mean and Standard Deviation are examined. Simultaneously, to measure the relative measure of variability of data, the Coefficient of Variation is also measured.

#### 4.2.1 Loans and Advances

One of the dominant functions of commercial bank is to create credit from its borrowed fund. By doing so it is converting its liability into assets. The high volume of loans and advances is indicator of good performance in credit sector. In other words, the volume of loans and advances is taken as one crucial element for measuring the performance of any commercial banks.

In this chapter, we analyze the impact assessment of NRB regulatory system on commercial bank. The main important or crucial tool to evaluate the true and actual position of any organization is its past information and data. The strength and weakness of the organization can be appraised from the proper analysis of data. This part of the report focuses on presentation and analysis of data related to the NRB norms to obtain the objectives of the study.

#### 4.1 Capital Fund Analysis

**Table 4.1**  
**Capital Fund of Nepal Investment Bank Ltd.**

*(Amount in Rs.)*

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
Core capital	506830000	621430000	710610000	1161477520	1393273570
Supplementary	53020000	7382000	388770000	417290910	700926080
Total capital fund	559850000	695250000	1099380000	1578768420	2094199650
TRWA	3519800000	7896160000	9836700000	13632906760	17491787670
<b>NRB Requirement (%)</b>					
Core Capital to RWA	4.5	5	5.5	5.5	5.5
CAR	9	10	11	11	11
<b>Actual Maintained (%)</b>					
Core capital to RWA	14.4	7.87	7.22	8.52	7.97
CAR	15.91	8.8	11.18	11.58	11.97
<b>Excess or short fall in (%) of Core Capital to RWA</b>					

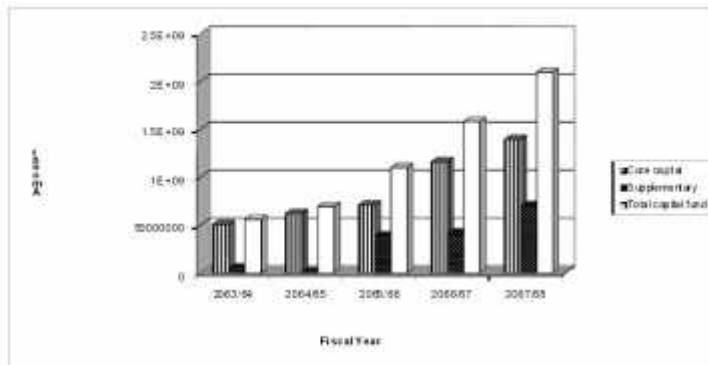
Percentage	9.9	2.87	1.72	3.02	2.47
RWA (Rs)	348439000	226622000	169591500	411667648	431225248

**Excess or Short fall in (%) Capital Adequacy Raito**

Percentage	6.91	-1.2	0.18	0.58	0.97
Amount	243068000	-94366000	17343000	79148676	170103006

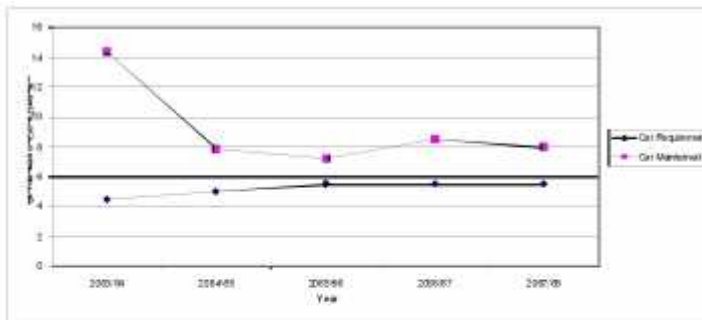
*Source: Annual Report of NIBL, 2060/61 to 2066/67.*

**Figure 4.1**  
**Capital Fund of NIBL**

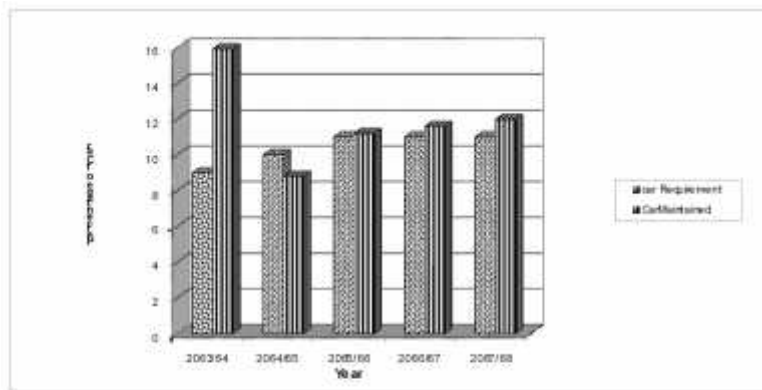


The given data shows that the capital fund, core capital and supplementary capital are in increasing trend. If we see the figures then investment bank ltd has subsequently increased its total capital fund by increasing its core capital more than that of supplementary capital but in the fiscal year. Nepal investment bank issue 7.5% redeemable debt called "Nepal Investment Bank bond 2063" of worth Rs. 30,00,00,000/-, which is the main cause for increase in supplementary capital by 426.65%. The portion of core capital in total capital fund is around 77% in five year average while that of supplementary capital is around 23% in five year average. It means contribution of core capital is in more growth of total capital fund. Core capital play important role in safeguarding both survive of the bank and stability of the financial system so commercial banks give more priority to core capital than that of supplementary capital.

**Figure 4.2  
Core Capital to RWA of NIBL**



**Figure 4.3  
CAR to RWA of NIBL**



The core capital to risk weighted assets and CAR of the Nepal Investment bank during the fiscal year 2063/64, 2064/65, 2065/66, 2066/67 and 2067/68 is within the excess by 9.9%, and 6.91, 1.72 and 0.18%, 3.02% and 0.58%, 2.47% and 0.97% respectively than NRB requirement. But in the fiscal year 2063/64, capital adequacy ratio is only 8.80% while NRB requirement is 10% that is the shortfall of 1.2%. So during the year capital adequacy amount is short by Rs.

94366000. Another side, we see the core capital is by 2.87%. In this fiscal year shortfall amount is due to the shortfall in supplementary capital, comparing to previous year 2063/64. Another main cause is heavy increase in risk-weighted assets than comparison of core capital, supplementary capital and total capital fund. Capital increased by 39.23% and total capital increased by 22.61%, another side risk weighted assets increased by 124.34%. Increase in risk weighted assets is due to heavy increase in on balance sheet items like loan fixes assets and similarly heavy increase in off balance sheet items like letter of credit, bid bond, performance bond, advance payment guarantee and other guarantee.

In the fiscal year 2063/64, Nepal Investment bank ltd. Issued bonus share worth Rs. 6.799 crore and also right share issue worth Rs. 5.666 corer so as to increase its total capital fund to meet the NRB norms and also to expand its banking activities.

Similarly, in the fiscal year 2064/65, Nepal Investment bank is able to maintain its capital adequacy requirement as well as core capital to risk weighted assets. If we see the data, there is a huge increment in supplementary capital by 426.65% than previous year. In the fiscal year 2063/64, Nepal Investment bank issue 7.5% redeemable debenture called "Nepal Investment Bank Bond 2067" of worth Rs.300000000/- which is the main cause for increase in supplementary capital by 426.65%. Similarly, it has also maintained capital adjustment reserve in order to issue right share in the ratio of 1:1 and maintaining of debenture redemption fund which also increase the core capital. By right issuing, it is increasing its paid up capital to Rs.59058000 and its authorized capital will be Rs.1000000000/- (Rs. One billion). All these activities are gear up only due to meet the NRB norms of capital adequacy requirement and increase the capital to two billion by 2069/70.

So as to fulfill the requirements of NRB norms, Nepal Investment Bank Ltd. is forced to increase its capital base for implementation of NRB norms. NIBL has

taken various steps like it issue right share and bonus share in the fiscal year 2063/64 and purposed to right issue in the fiscal year 2063/64 at the ratio 1:1 to increase its paid up capital.

To maintain the required capital adequacy norms, NIBL had allocated huge portion of profit into different reserve fund, which is ultimately, reduce the shareholders dividend.

**Table 4.2**

**Portion of Dividend on Net Profit**

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
Net profit	57105284	116817659	152670976	232147098	350536413
Dividend+ Bonus share	67993800	59058600	44293950	73467313	327531200
Percentage	119.07%	50.56%	29.01%	31.65%	93.44%

*Source: Annual Report of NIBL, 2063/64 to 2067/68.*

$$\text{Percentage} = \frac{\text{Dividend} \Gamma \text{ BonusShare}}{\text{Net Profit}} | 100$$

If we see the dividend provided to shareholders form net profit than what we see is during the fiscal year 2063/64. In this year, bank had provide the bonus share instead of dividend, bonus share were issued from net profit of that year plus from retained earning. Similarly, the bank had issued bonus share in the fiscal year 2066/67. As well as in the fiscal year 2063/64, 2064/65, 2065/66, 2066/67 and 2067/68 shareholders receive dividend in percentages 50.56%, 29.01%, 31.65%, 33.70% and 93.44% of net profit. It means remaining portion of net profit was allocated for different reserves. So we can say that because of maintaining of different reserves for sufficient capital fund shareholders get less paid. This will make shareholders unhappy and may have negative impact on investment of banks shares. Public may not be willing to invest in banks share as they were not well paid. This may bring problems in the banking industry. So NRB while issuing directives must be very careful and take into consideration

the interest of investors and negatives as well as positive impact of such directives.

**Table 4.3**  
**Capital Fund of NABIL Bank Ltd.**

*(Amount in Rs.)*

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
Core Capital	1062670887	1276849132	1439454303	1610510308	1830794417
Supplementary Capital	352616710	178246483	169961989	155562222	258529605
Total Capital Fund	1415287597	1455095615	1609416292	1766072530	2089324022
TRWA	10563619794	11145732462	11872009411	14193071630	16976368425

**NRB Requirement %**

Core Capital to RWA	4.5	5	5.5	5.5	5.5
CAR	9	10	11	11	11

**Actual Maintained %**

Core Capital to RWA	10.6	11.46	12.12	11.35	10.78
CAR	13.4	13.06	13.56	12.44	12.31

**Excess/shortfall in (%) Core Capital to RWA**

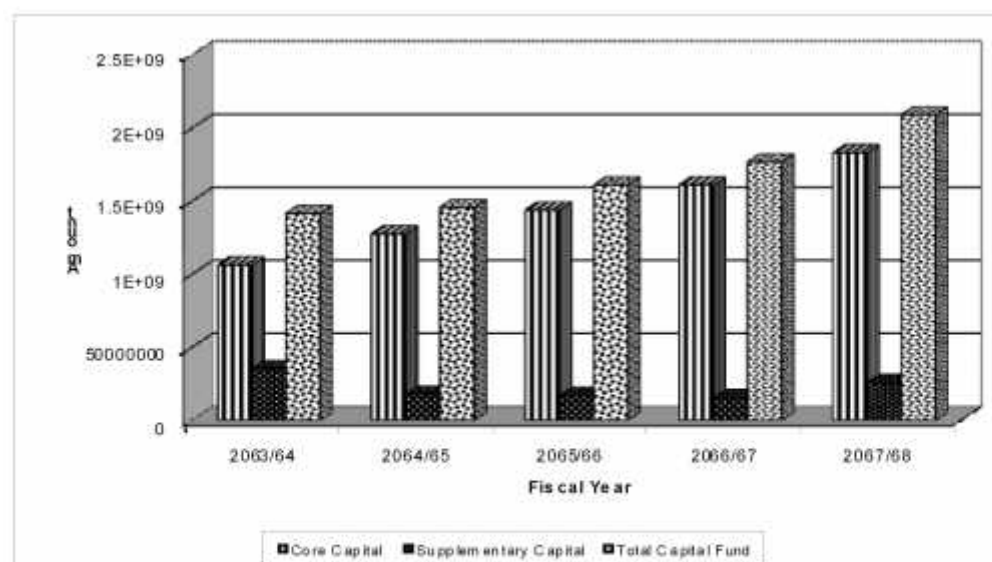
Percentage	5.56	6.46	6.62	5.85	5.28
RWA (Rs)	587307996	719562509	786493785	829891368	897094154

**Excess or Short fall in (%) Capital Adequacy Ratio**

Percentage	4.4	3.06	2.56	1.44	1.31
Amount	464561816	340522369	303495256	204834651	221923496

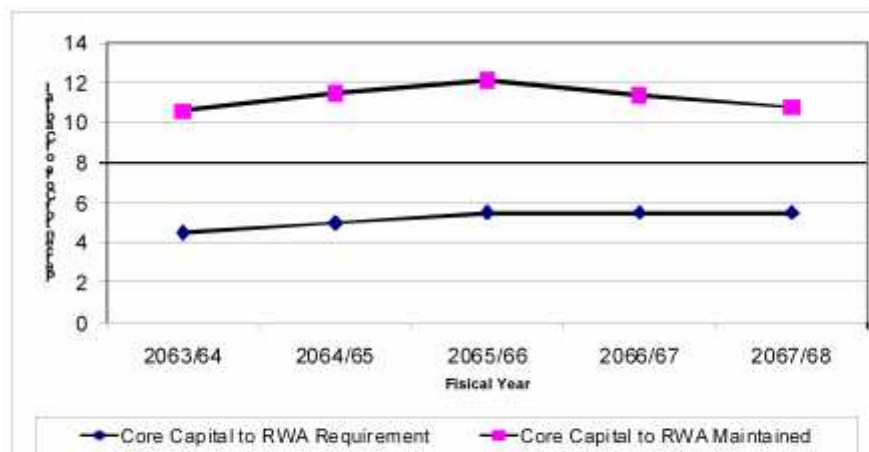
*Source: Annual Report of NABIL, 2063/64 to 2067/68.*

**Figure 4.4**  
**Capital Fund of NABIL Bank Limited**

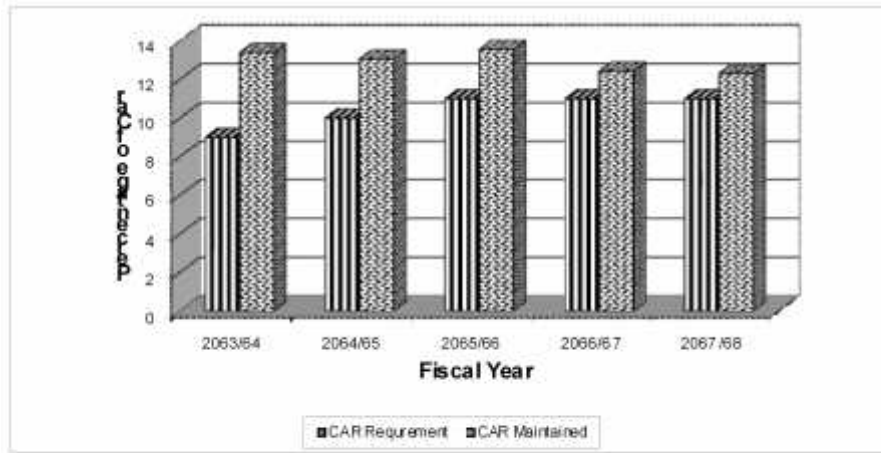


The above data shows that the total capital fund and core capital is increasing in fiscal year 2063/64 to till date. But supplementary capital is in decreasing trend in fiscal year 2064/65, 2065/66 and 2066/67 while increases in 2067/68. If we see the figures than NABIL bank has subsequently increased its capital fund by increasing its core capital more than that of supplementary capital. The portion of core capital in total capital fund is around 86% in five-year average while that of supplementary capital is around 14% in five-year average. It means contribution of core capital is more in growth of total capital fund. Core capital is play vital role in safeguarding both the survival of the bank and stability than that of supplementary capital.

**Figure 4.5**  
**Core Capital to RWA of NABIL Bank Limited**



**Figure 4.6**  
**CAR to RWA of NABIL Bank Limited**



We see that from the following data that NABIL bank has maintained its capital adequacy norms. To comply with NRB norms, this bank has subsequently increased its capital fund by increasing more in its core capital. But supplementary capital is in decreasing trend till FY 2066/67 and after in fiscal year 2067/68 it gradually increased. At the same time its risk-weighted assets is also increasing each year. If we see the contribution to total capital fund then the portion of core capital is very high and is sufficient enough to meet the CAR also not taking into consideration of supplementary capital.

The capital adequacy ratio and core capital to RWA of NABIL Bank Ltd., during the fiscal year 2063/64, 2064/65, 2065/66, 2066/67 and 2067/68 is within the limit and even excess by 5.56% and 4.4%, 6.46% and 3.06%, 6.62% and 2.56%, 5.85% and 1.44%, 5.28% and 1.31% respectively than NRB requirement. So as to fulfill the requirement of NABIL bank to increase its capital base. In the fiscal year 2063/064 the bank has paid cash dividend of Rs.417906240. Lastly, the CAR and core capital to risk weighted assets ratio indicate the positive or better condition of the bank.

To maintain the required capital adequacy norms, NABIL bank has allocated huge portion of profit into different reserve fund, which ultimately reduce the shareholders dividend.

**Table 4.4**

**Portion of Dividend on Net Profit**

(Amount in Rs.)

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
Net Profit	271638612	416235811	455311222	520114085	635262349
Dividend + Bonus Share	147496320	245817200	319575360	344158080	417906240
Percentage	54.30%	95.06%	70.19%	66.17%	65.78%

Source: Annual Report of NABIL, 2060/61 to 2066/67.

$$\text{Percentage} = \frac{\text{Dividend} \Gamma \text{ BonusShare}}{\text{Net Profit}} | 100$$

If we see the dividend provided to shareholder from net profit then we see during the fiscal year 2063/64 shareholders get only 54.3% of total net profit and remaining amount was set aside as retained earning and also for general reserve fund. Similarly, the NABIL bank had paid the cash decided in the fiscal year 2063/64, 2064/65, 2065/66, 2066/67 and 2067/68 shareholder receive only 95.06%, 70.19%, 66.17% and 65.78% respectively of total net profit. NABIL bank focused the shareholder desire and fulfills it to pay the annual cash dividend and bonus share. Time to time the bank pays the dividend, which would create better operational condition for banks and a good image of bank in the eyes of shareholders. During the last two year NABIL bank have reduced the dividend percentage. NABIL bank paid the cash dividend regularly although net profits were lower. So NABIL bank should be very careful and must consider the desire of shareholders and concentrate towards giving good return to its shareholders since shareholders are the real owner of the bank.

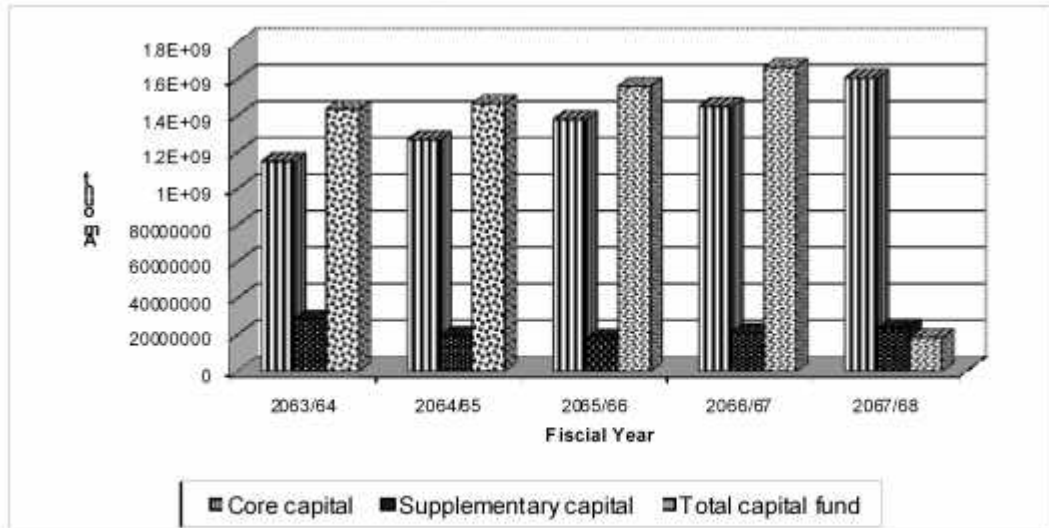
**Table 4.5**  
**Capital Fund of Standard Chartered Bank Nepal Ltd.**

(Amount in Rs.)

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
Core capital	1149512332	1268588863	1378971720	1450185184	1606898000
Supplementary capital	285828205	196260737	181183932	214175837	237344000
Total capital fund	1435340637	1464849599	1560155652	1664361021	184424000
RWA	8256121462	10307526845	10023087569	10497531776	12369488438
<b>NRB Requirement (%)</b>					
Core capital to RWA	4.5	5	5.5	5.5	5.5
CAR	9	10	11	11	11
<b>Actual Maintained (%)</b>					
Core capital to RWA	13.92	12.31	13.76	13.81	12.99
CAR	17.39	14.21	15.57	15.85	14.91
<b>Excess or Short Fall in (%) Core Capital to RWA</b>					
Interest percentage	9.42	7.31	8.26	8.31	7.49
RWA (Rs)	18.70	18.11	19.90	20.99	22.28
<b>Excess or Short Fall in (%) Capital Adequacy Ratio</b>					
Percentage	8.39	4.21	4.57	4.85	3.91
Amount	692289606	434096915	457616019	509632525	483598000

*Source: Annual Report of SCBNL, 2063/64 to 2067/68.*

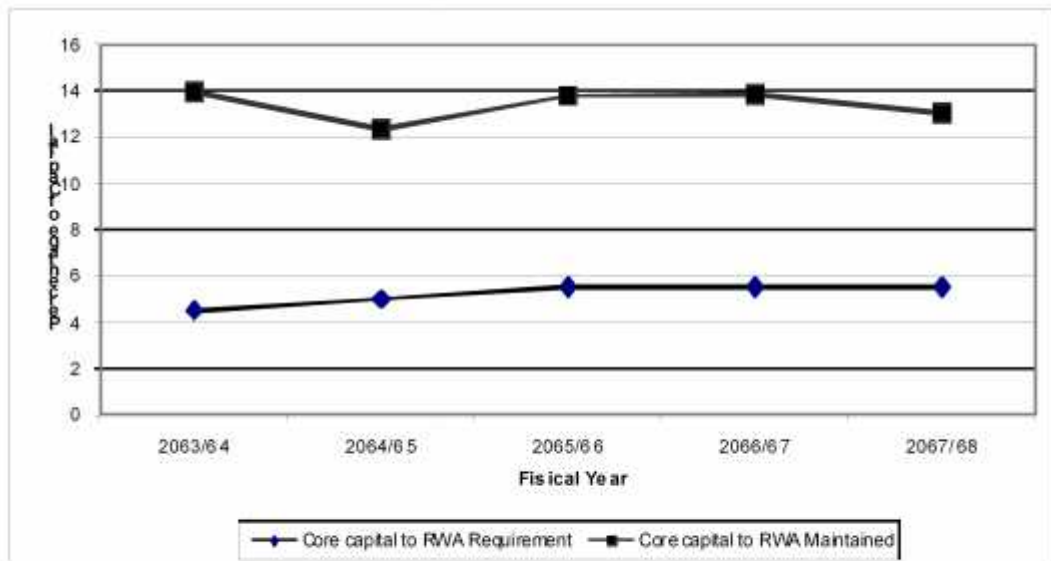
**Figure 4.7**  
**Capital Fund of Standard Chartered Bank Limited**



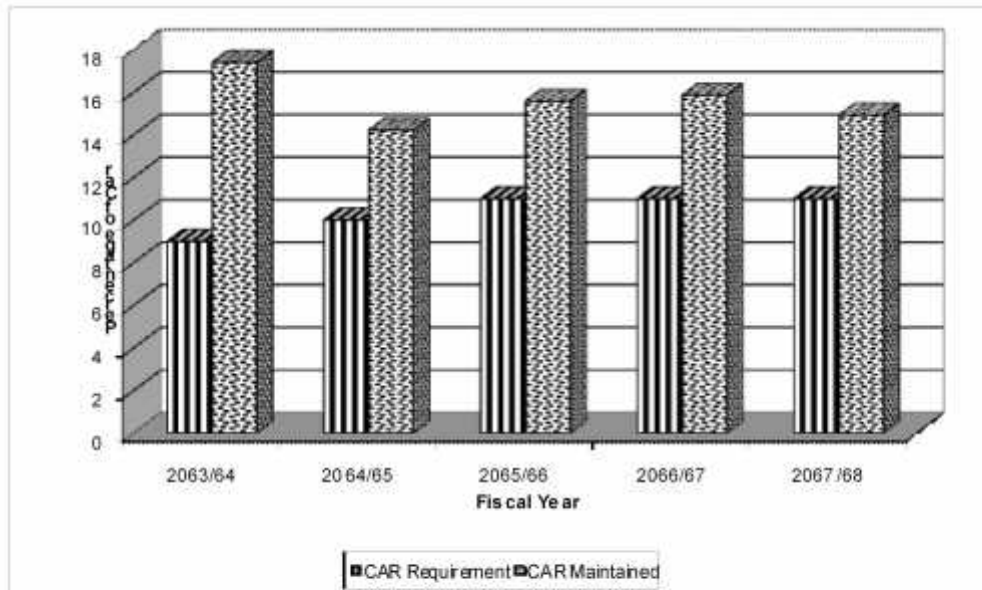
The above data shows the total capital fund and capital is in increasing trend but supplementary capital fund decreases in 2060/61 then after it was gradually increase. If we see the given data of standard chartered bank limited has subsequently increased its capital fund by increasing its core capital more then supplementary capital. The portion of core capital in total capital fund is around 86% in five-year average while that of supplementary capital is around 14% in five-year average. It means that the contribution of core capital is more in growth of total capital fund. Core capital plays an important role in safeguarding both the survival of the bank and stability of the financial system so commercial bank gives more priority to core capital than that of supplementary capital.

**Figure 4.8**

**Core Capital RWA of Standard Chartered Bank Limited**



**Figure 4.9:  
CAR to RWA of Standard Chartered Bank**



The core capital to risk weighted assets of standard chartered bank during the fiscal year 2060/61, 2063/64, 2064/65, 2065/66 and 2066/67 is within the limit and over by 9.42%, 7.31%, 8.26%, 8.31% and 7.49% as well as capital adequacy ratio is within the limit and shows that standard chartered bank has maintained its capital adequacy norms, which is the guidelines of NRB. Thus bank has subsequently increased its capital fund by increasing more in its core capital and as well as supplementary capital has also increased in small amount. At the same time its risk weighted assets is also increasing each year if we see the contribution of total capital fund than the portion of core capital is very high and is sufficient enough to meet the CAR also not talking into consideration of supplementary capital. If we see the growth figure of core capital, supplementary capital and total capital fund is increasing every year but is decreasing ratio. Risk weighted assets of standard chartered bank is increasing every year so as to fulfill the NRB directives.

Standard chartered bank has reduced the loan loss provision in every fiscal year from 2060/61 to till date. It reduced the loan loss provision than after reduced the supplementary capital. Therefore, the supplementary capital of the bank is decreasing in fiscal year 2060/61. Than after in the next fiscal year the bank has increased the exchange equalization reserve, it would be increased by the supplementary capital.

To maintain the required capital adequacy norms, SC bank had allocated huge portion of its profit to different reserve fund, which ultimately reduce the shareholders dividend.

**Table 4.6**  
**Portion of Dividend on Net Profit**

*(Amount in Rs.)*

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
Net Profit	479206569	506930870	537800124	536244885	658755881
Dividend + Bonus Share	339548800	373503680	412104440	449568480	524496560
Percentage	70.85%	73.68%	76.63%	83.84%	79.62%

*Source: Annual Report of SCBNL, 2063/64 to 2067/68.*

$$\text{Percentage} = \frac{\text{Dividend} \Gamma \text{ Bonus Share}}{\text{Net Profit}} | 100$$

The above data, shows the dividend provided to shareholder from net profit during the fiscal year 2063/64 shareholder get only 70.86% of total net profit in the form of cash dividend. Similarly in the fiscal year 2064/65, 2065/66 & 2066/67 shareholders received only 73.68%, 76.63%, and 83.84% of total net profit but in the fiscal year 2062/66 SCBNL has declared the cash dividend as well as bonus share. In this year shareholders receive only 79.62% of total net profit in the form of cash dividend and bonus share. It means remaining portion of net profit was allocated for different reserves. So we can say that because of maintaining of different reserves for sufficient capital fund shareholders get less paid. This will make shareholders unhappy and may have negative impact on

investment but SCBNL management has find out this type of shareholder desire and fulfill their requirement.

## 4.2 Loan and Loan Loss Provision Analysis

**Table 4.7**  
**Loan and Loan Loss Provision of NIBL**

(Amount in Rs.)

Fiscal Year	2063/64	2064/65	2065/66	2066/67	2067/68
<b>Performing Loan</b>	<b>2583230154</b>	<b>5804696154</b>	<b>6942667856</b>	<b>10172289866</b>	<b>12905658783</b>
Non-performing Loan (NPL)	130294717	117091823	181435009	280874131	272493041
Sub standard	17231526	22030528	10839263	821624	44238859
Doubtful	3481767	3594004	63878948	74941884	497100
Bad	109581434	91467291	106716798	255110623	227757082
<b>Total Loan and Advance</b>	<b>2713524871</b>	<b>5921788103</b>	<b>7124102865</b>	<b>10453163997</b>	<b>13178151824</b>
<b>Loan Loss Provision (LLP)</b>	<b>149101389</b>	<b>149647852</b>	<b>206296249</b>	<b>327108374</b>	<b>401943787</b>
Performing loan	36381448	57207172	68685896	101059649	165141439
Sub Standard loan	20896168	2491094	2727587	211972	11059715
Doubtful	1648839	457354	29896016	37557734	248550
Bad	108981434	89492232	104986750	188279019	225494083

### Provision Maintain in %

Pass loan	1.41	0.99	0.99	0.99	1.28
Substandard	12.13	11.31	25.16	25.8	25
Doubtful	47.36	12.73	46.8	50.12	50
Bad	99.45	97.84	98.38	91.8	99.01

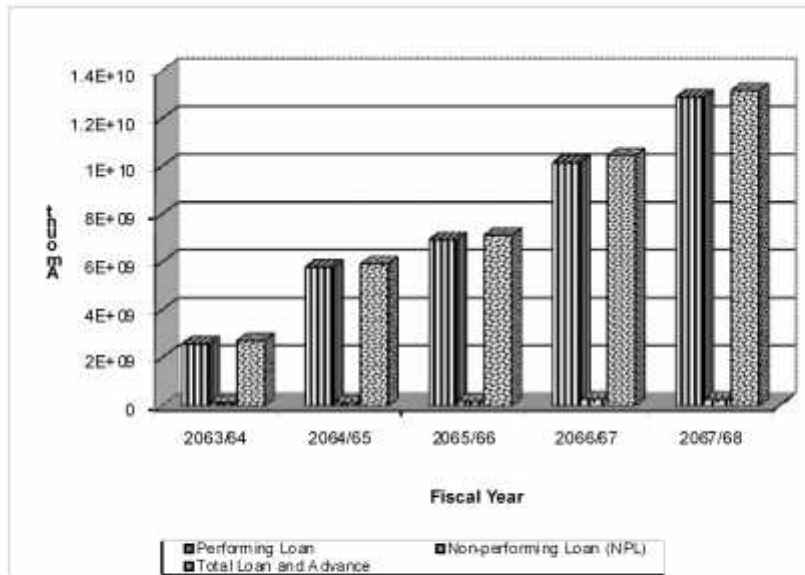
### NRB Requirement (%)

Pass loan	1	1	1	1	1
Substandard	25	25	25	25	25
Doubtful	50	50	50	50	50
Bad	100	100	100	100	100

LLP to total loan & Advance	5.49	2.53	2.9	3.13	3.05
NPL to total loan & Advance	4.8	1.98	2.55	2.69	2.07
LLP to NPL	114.43	127.8	113.7	116.46	147.51

Source: Annual Report of NIBL, 2063/64 to 2067/68.

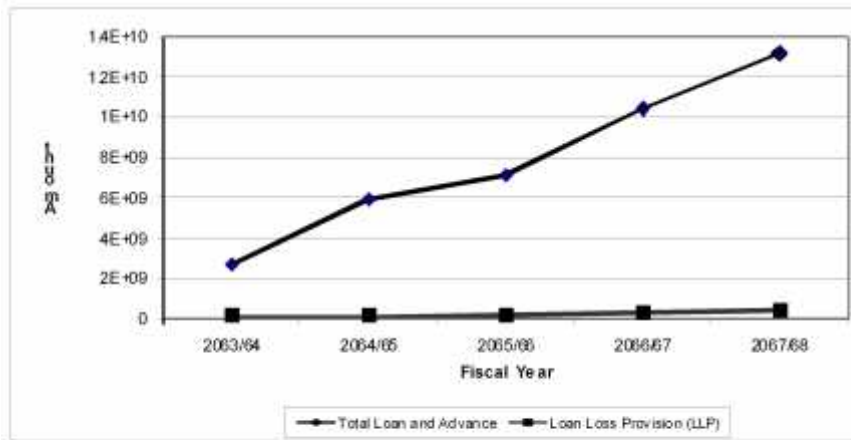
**Figure 4.10**  
**Portfolio of Loan and Advance of NIBL**



If we see the loan and loan loss provision table, then what we see is in the total loan and advances, the portion of performing loan is increasing every year while portion of non performing loan is decreasing but in the year 2065/66 to 2066/67 it has increased and then after it has decreased. To overcome the problem of non-performing asset NIB is reducing its NPL account as well as also reduces the burden of maintaining high provision for NPL account. Total loan and advances increases more than 100% in the year 2063/64 with the increase in performing loan, which is good, sign for NIB as interest earned in loan amount in the main source of income for commercial banks. Due to the norms of NRB directives NIB is reducing non-performing loans.

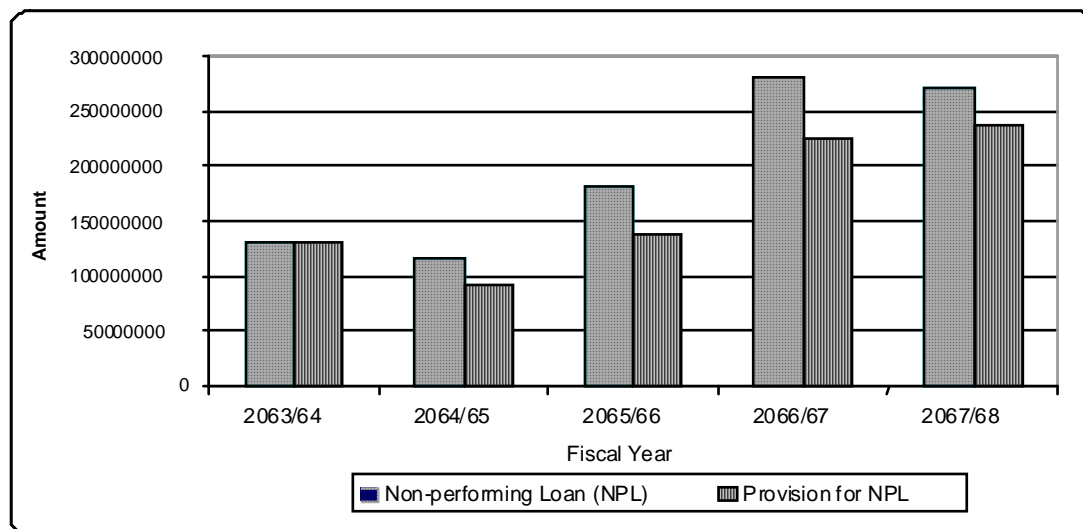
**Figure 4.11**

**Loan Loss Provision and Total Loan and Advance**



The ratio of loan loss provision to total loan & advances of Nepal Investment Bank ranges from 2.5% to 5.4% in different years. Since, high provision is to be maintained for non-performing loan, higher ratio indicates high portion of non-performing loan in the total loan and advances but here data shows low ratio, which is also in decreasing trend that means non performing loan of Nepal Investment Bank is decreasing every year in the total volume of loan and advances. So we can take it as Nepal Investment Bank's efficient, effective and strong managing its loan and advances and coping with probable loan loss and also complying with the NRB norms. If there had not been NRB guidelines to maintain high provision on NPL then there might be high portion of non-performing loan in the total loan portfolio.

**Figure 4.12**  
**NPL and Provision for NPL**



Nepal Investment Bank is not complying with the NRB norms for loan loss provision. It is maintain by Nepal Investment Bank falls short by few percentage in each year and also NPL is increased in the year 2064/65 and 2065/66 by more that 50% compared to previous year. In the portfolio of NPL portion of bad was very high, which is not good sign for Nepal Investment Bank so, by not maintaining the required provision and high portion of bad can expose Nepal Investment Bank to risk and also can't cope with the future contingencies that may cause due to NPL. High provision is better but since amount maintained for provision remains idle and does not yield any return. It may have negative impact in return or profit, which will be affected so to remain unaffected from profit viewpoint, the NRB norms for loan loss provision should be appropriate or NPL has reduced as per the guidelines.

**Table 4.8**  
**Loan and Loan Loss Provision of NABIL Bank Ltd.**

(Amount in Rs.)

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
<b>Performing Loan</b>	<b>7244970881</b>	<b>7664053458</b>	<b>8261978118</b>	<b>10802229684</b>	<b>13096157779</b>
Non-performing loan (NPL)	556877682	449630763	286678920	144506893	182624480
Sub standard	260277239	76311974	22139920	22072562	62665914
Doubtful	230936540	279117410	65552224	1934092	29565952
Bad	65663903	94201379	198983773	120500239	90392614
<b>Total loan and &amp; Advance</b>	<b>7801848563</b>	<b>8113684221</b>	<b>8548657038</b>	<b>10946736577</b>	<b>13278782259</b>
<b>Loan Loss Provision (LLP)</b>	<b>363953887</b>	<b>357732236</b>	<b>358664187</b>	<b>360566575</b>	<b>356239106</b>
Performing loan	140918813	122587932	127733990	235345571	214301301
Sub Standard loan	62681307	18320228	5140970	6865463	42573904
Doubtful	114424624	136619817	32384357	1415926	13896064
Bad	45929143	80204259	193404870	116939615	85467837

**Provision Maintain in %**

Pass loan	1.94	1.6	1.55	2.18	1.64
Substandard	24.08	24	23.22	31.1	67.93
Doubtful	49.55	48.95	49.4	73.21	47
Bad	69.95	85.14	97.2	97.05	94.55

**NRB Requirement (%)**

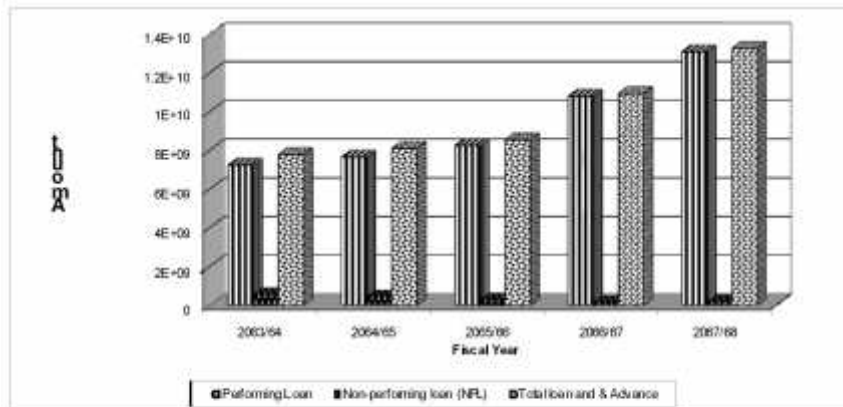
Pass loan	1	1	1	1	1
Substandard	25	25	25	25	25
Doubtful	50	50	50	50	50
Bad	100	100	100	100	100

LLP to total loan & Adv.	4.67	4.41	4.2	3.29	2.68
NPL to total loan & Adv	7.23	5.54	3.35	1.32	1.38
LLP to NPL	65.36	79.56	125.11	249.51	195.07

*Source: Annual Report of NIBL, 2063/64 to 2067/68.*

**Figure 4.13**

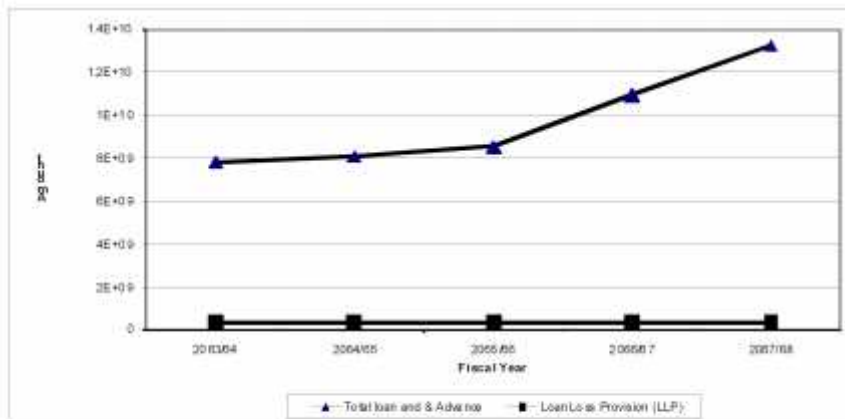
**Portfolio of Loan and Advance of NABIL Bank Limited**



As per the above table of loan and loan loss provision shows the total loan and advances are increasing every year compare to previous year; similarly performing loan has also increased every year than previous year as well as NPL has decreased every year compared to previous year. In the year 2065/66 and 2066/67, NPL has huge amount which should be reduced this year NPL decreased the percentage around 45-50%. In the portfolio of total loan and advances portion of performing loan is around 96.25% while remaining is NPL. This shows that NABIL bank is distributing its loan very carefully and by increasing the portion of performing loan in the portfolio, NABIL bank is trying to make its assets good and earn interest without bearing any risk. Due to the norms of NRB directives NABIL bank is increasing its portion of performing loan in the portfolio of total loan and advances. There by reducing the burden of maintaining high provision for NPL.

**Figure 4.14**

**Loan Loss Provision to Total Loan and Advance**



The ratio of loan loss provision to total loan and advances of NABIL bank is around 2.6% to 4.6% in different years. Since, high provision is being maintained for Non-performing loan, higher ratio means high portion of non performing loan in the total loan and advances and lower ratio indicates low portion of non performing loan is the total loan and advances but here data shows the ratio has decreased in a slow rate every year in the total volume of loan & advances. It also signifies the good quality of assets in the total volume of loan and advances as well as NABIL bank's efficiently and effectively toward its strong management of its loan and advances and coping with probable loan loss and also complying with the NRB norms. If there had not been NRB guidelines to maintain high provision on non-performing loan then, there might be high portion of non-performing loan in the total loan portfolio. NABIL bank is complying with the NRB norms for loan loss provision. Although, the loan loss provision of NABIL bank is gradually decreasing each year but during the year 2065/66 and 2066/67 NPL have declined dramatically to a huge amount to the tune of 45 percent to 50 percent. So, if the NPL is

decreasing, it is a good sign for banking sector. And in that category NABIL Bank is performing very efficiently and effectively, as maintaining high provision provides security form loan loss but maintaining in excess may be disadvantageous to the bank. As amount maintained for provision remains idle and does not yield any return, it may have negative impact in return or profit will be affected.

**Table 4.9**

**Loan and Loan Loss Provisioning of SCBNL Ltd.**

*(Amount in Rs.)*

<b>Fiscal Year</b>	<b>2063/64</b>	<b>2064/65</b>	<b>2065/66</b>	<b>2066/67</b>	<b>2067/68</b>
<b>Performing Loan</b>	<b>5420247725</b>	<b>5752213972</b>	<b>6441664201</b>	<b>8194560390</b>	<b>9010347896</b>
Non-performing loan	275933961	247948667	252198110	226308403	195932315
Sub standard	3325800	7052540		10443017	16492340
Doubtful	140293920	130000000	130989043	104521470	65608277
Bad	132314241	110896127	121209069	11343916	113831698
<b>Total Loan and Adv.</b>	<b>5696181686</b>	<b>6000162639</b>	<b>6693862311</b>	<b>8420868793</b>	<b>9206280211</b>
<b>Loan Loss Provision</b>	<b>33217578</b>	<b>304339118</b>	<b>283620230</b>	<b>277661010</b>	<b>270862401</b>
Performing loan	93883927	94179857	64416641	81945605	90103479
Standard loan	831450	1763135		2610754	4123085
Doubtful	105146960	97500000	90994522	81760735	62804139
Bad	132314241	110896126	121209067	111343916	113831698

**Provision Maintain in (%)**

Performing loan	1.73	1.64	1	1	1
Substandard	25	25		25	25
Doubtful	74.95	75	64.47	78.22	95.75
Bad	100	100	100	100	100

**NRB Requirement (%)**

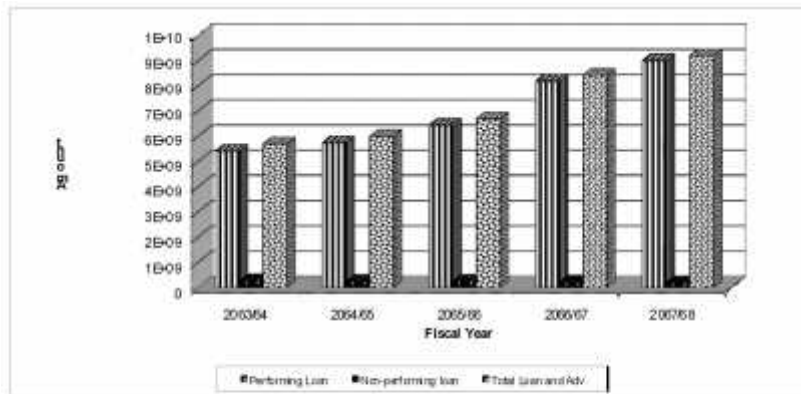
Performing loan	1	1	1	1	1
Substandard	25	25	25	25	25
Doubtful	50	50	50	50	50
Bad	100	100	100	100	100

LP to total loan & Adv.	5.83	5.07	4.22	3.3	2.94
NPL to total loan & Adv.	4.84	4.13	3.77	2.69	2.13

LLP to NPL (%)	120.38	122.74	112.46	122.69	138.24
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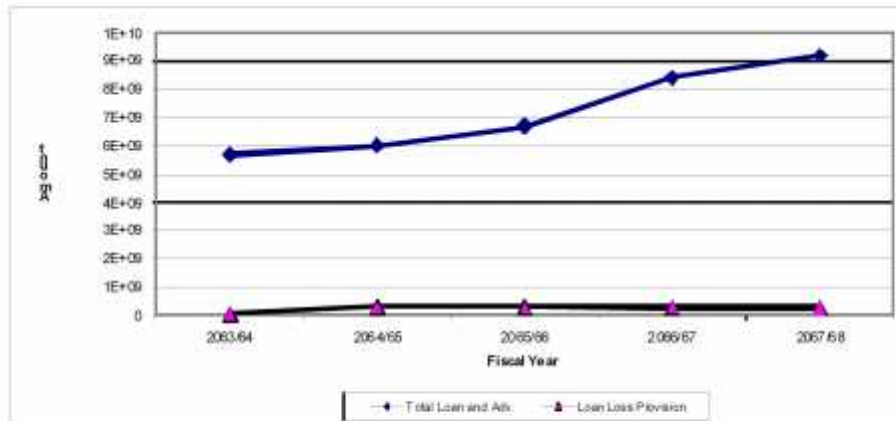
*Source: Annual Report of SCBNL, 2063/64 to 2067/68.*

**Figure 4.15**  
**Portfolio of Loan and Advances of SCBL**



As per above table of loan and loan loss provision shows the total loan and advances are increasing every year compare to previous year. Similarly, pass loan (performing loan) is also increasing but if we see the NPL then there is little bit decreases in the fiscal year 2004/05 but next year it has increased for a little amount and the fiscal year 2006/07 onwards the NPL has reduced consistently for next year. In the portfolio of total loan and advances portion of pass loan (performing loan) is around 96% while remaining is NPL. This shows that standard chartered bank should distribute the loan very carefully and by increasing the portion of performing loan in the portfolio. Standard Chartered Bank is trying to make its assets good and earn interest without bearing any risk. Due to the norms of NRB directives Standard Chartered Bank is increasing its portion of performing loan in the portfolio of total loan and advances.

**Figure 4.16**



### **Loan Loss Provision of SC Bank Limited**

The ratio of loan loss provision (LLP) to total loan and advances of SC banks is around 2.9% to 5.8% in different years. Since, high provision is to be maintained for the non-performing loan (NPL), higher ratio indicates high portion of non-performing loan in the total loan and advances. The Standard Chartered Bank loan loss provision is decreasing of every year i.e. fiscal year 2063/64 to 2067/68. It indicates that reducing loan loss provision is the sign of the good quality of assets in the volume of loan and advances. So we can take it, as Standard Chartered Bank is efficiency and effectively managing of its loan and advances and coping with probable loan loss and also complying with the NRB norms. If there had not been NRB guidelines to maintain high provision on non-performing loan, then there might be high portion of non-performing loan in the total loan portfolio.

Loan loss provision of Standard Chartered Bank shows that its provision is within the requirement of NRB during the fiscal year 2063/64 to 2067/68. In this year, it has not maintained the requirement of provision of NPL in the

Standard Chartered Bank. Thus it is exposed to risk. Which might be dangerous if such loan are not be recovered. But by maintaining the requirement in the following year Standard Chartered Bank has corrected its mistake and complies with the NRB norms.

Standard Chartered Bank has maintained the provision in excess for pass loan (performing loan) in the fiscal year 2063/64 and 2064/65. In reaming fiscal years it has maintained its provision as per NRB requirement. Maintaining high provision is to provide security from loan loss but maintaining in excess may be disadvantageous to the bank. As amount maintained for provision remains idle and does not yield any return, it may have negative impact in return or profit will be affected so, to remain unaffected from profit viewpoint bank must maintain provision as required.

### **4.3 Single Borrower Limits**

Single borrower limits is the limit which should not be more than the one set by regulatory authorities to extend maximum amount of loan to a single borrower or a group of borrowers. The bank gives loans to various sectors for the long-term survival of the banks by receiving deposits from general public so that depositors' deposits are the major portions of the bank's lending liability and the loan and advances of the banks to the borrowers is the major portion of its total assets. Therefore the banks should be more careful while making loans otherwise banks may fail to make repayment of the deposits to the depositors, which results in the liquidation of the banks.

With a view to safeguard the depositors money and protect the banks form bankruptcy. NRB has issuing directives from time to time under the prudential norms. The directives related to single borrower limits has the main objectives is to set up limits on the maximum amount of loans that can be lend to a single borrower or group of borrowers. The single borrower limit is based only on the core capital in the new directives whereas these limits were based on the total capital fund as per old provision. The total core capital of SC bank, NABIL

bank and NIBL bank are given below. So, single borrower limit is computed as percentage given by the NRB directives. The percentage of single borrower limit to be applied for SCBNL, NABIL and NIB are as follows:

**Table 4.10**  
**Comparative Chart of the Single Borrower Limit of NIBL**

New Provision Limits			Old Provision Limits	
Year	Fund based	Non fund based	Fund based	Non fund based
	25% of core capital	50 % of core capital	35% of total capital fund	50% of total capital fund
2063/64	126707500	253415000	195947500	279925000
2064/65	155357500	310715000	243337500	347625000
2065/66	177652500	355305000	384783000	549690000
2066/67	290369380	580738760	552568947	789384210
2067/68	348318392	696636785	732969877	1047099825

*Source: Annual Report of NIBL, 2063/64 to 2067/68.*

**Table 4.11**  
**Comparative Chart of the Single Borrower Limit of NABIL Bank Ltd.**

New provision limits			Old provision limits	
Year	Fund based	Non fund based	Fund based	Non fund based
	25% of core capital	50 % of core capital	35% of total capital fund	50% of total capital fund
2063/64	265667722	531335443	495350659	707643798
2064/65	319212283	638424566	509283465	727547807
2065/66	359863576	719727152	563295702	804708146
2066/67	402627577	805255154	618125385	883036265
2067/68	457698604	915397208	731263408	1044662011

*Source: Annual Report of NABIL, 2063/64 to 2067/68.*

**Table 4.12**

**Comparative Chart of the Single Borrower Limit of SCBNL**

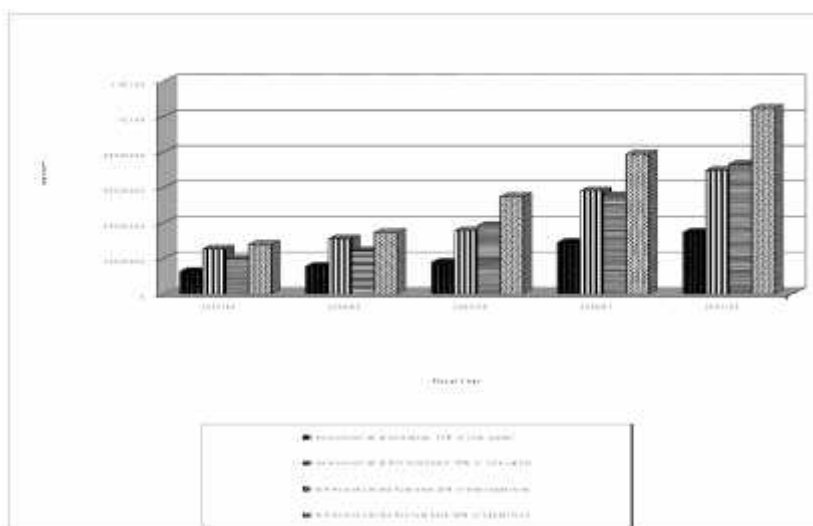
Year	New provision limits		Old provision limits	
	Fund based	Non fund based	Fund based	Non fund based
	25% of core capital	50 % of core capital	35% of total capital fund	50% of total capital fund
2063/64	287378083	574756166	502369188	717670269
2064/65	317147216	634294431	512697360	732424800
2065/66	344742930	689485860	546054478	780077826
2066/67	362546296	725092592	582526357	832180510
2067/68	401724500	803449000	645484700	922121000

Source: Annual Report of SCBNL, 2063/64 to 2067/68.

The following comparison data of old and new provision on fund based and non fund based shows the impact of changes is presented more clearly through the use of multiple bar diagram. It shows below separately.

**Figure 4.17**

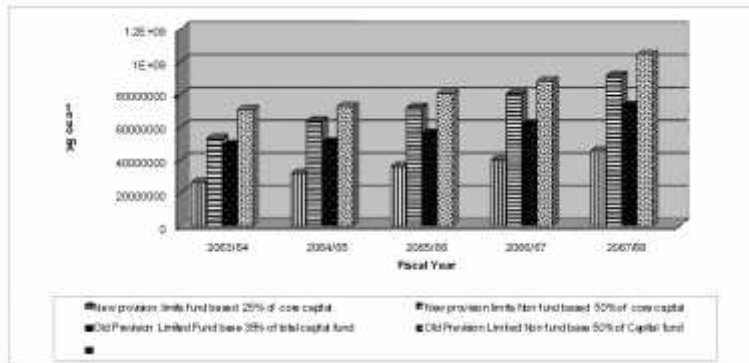
**Comparative Figure of Single Borrower Limit of NIBL**





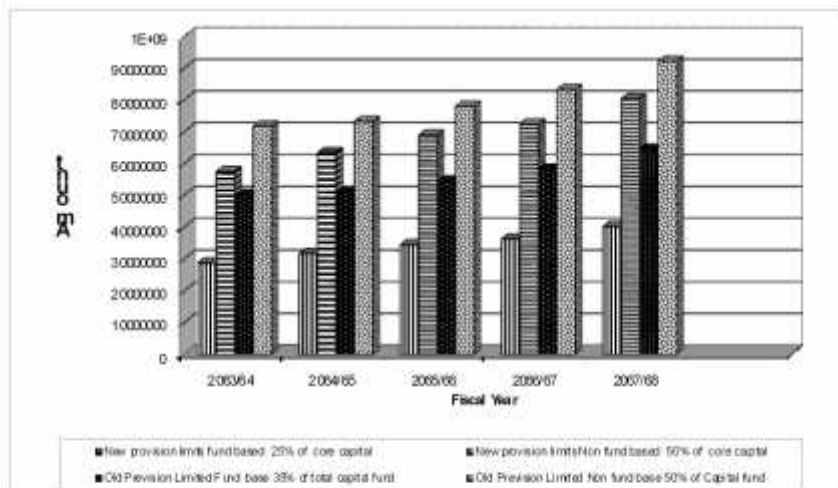
**Figure 4.18**

**Comparative Figure of Single Borrower Limit of NABIL Bank Ltd.**



**Figure 4.19**

**Comparative Figure of Single Borrower Limit of SCBNL**



From above figure it clearly shows that the limits of loan has come down by both fund based and non fund based due to the changes brought by the directives for the reduction of the limits by such huge amounts will surely make an impact on the banks. The above data shows that the SCBNL and NABIL as well as NIBL bank has increasing trend of fund based and non-fund base. All the data are increasing for the previous years. It shows that single borrower limit. The single borrower limits were previously based on the total capital fund, which is made by both core capital and supplementary capital. But the new provision is based only on core capital, which is lower than the total capital fund.

Incase of the loans already disbursed before 16th July 2002, single borrower limit has to be maintained 40% of fund based and 75% of non-fund based of core capital up to the end of fiscal year 2001/02. But 25% of fund based and 50% of non-fund based of core capital is applicable for the start of the 2002/03 to onward.

The single borrower limit of SCBNL, NABIL and NIBL is above the table. If the banks has distributed excess amount of loan limit then it has to increases the core capital in order to fill the gap, if any exceeded amount of loans within the limit, where the core capital of the bank includes the paid-up capital share premium. Non-redeemable preference shares, general reserves and accumulated profit/ loss account and profit of this year. If there is no possibility of increasing core capital, banks must reduce the loan exposure of the customers. It will substantially reduce bank's capacity to finance this will make an adverse impact on the profitability of the banks.

## 4.4 Correlation Analysis

**Table 4.13**  
**Correlation Analysis between Loan and Advance with Net Profit**

	Coefficient of Correlation	Relationship	Co-efficient of Determination	Probable Error	6*PE	Significant or Insignificant
NIBL	0.9837	High degree of positive correlation	0.9677	0.0975	0.585	Significant
NABIL	0.9088	High degree of positive correlation	0.8259	0.0525	0.315	Significant
SCBNL	0.8664	High degree of positive correlation	0.7506	0.0752	0.451	Significant

As we know net profit is the important amount of bank, total loan and advances disbursed by the bank plays important role in the income of the bank. The correlation coefficient between the loan and advances with net profit describes the degree of relationship between these two variables in which, we see that, among the two variables then loan and advances is independent variable where as net profit is dependent variable. Hence through this comparison we can find out the changes taken place in Net profit with every change in loan and advances and other invested found sources, to what extend is the impact of loan and advances on net profit of bank can be calculated or is exhibited by the correlation coefficient.

The above table shows that coefficient of correlation ( $r$ ) of NIBL, SCBNL & NABIL is 0.9837, 0.8664 and 0.9088 respectively, that is there is high degree of positive correlation between loan and advances and Net profit of all these selected banks. It means with every increase in the volume of loan and advances there will also be increment in the Net profit with the some volume so there is a close relationship between loan & advance and Net profit.

The coefficient of determination ( $r^2$ ) for NIBL is 0.9677; it means 96.77% of the total variation in Net profit (dependent variable) has been explained by the loan and advances (independent variable). Similarly for SCBNL is 0.7506, it

means 75.06% of the total variation in Net profit (dependent variable) has been explained by the loan and advances (independent variable). And finally NABIL is 0.8259; it means 82.59% of the total variation in Net profit (dependent variable) has been explained by the loan and advances (independent variable).

The correlation of coefficient of NIBL, SCBNL and NABIL is 0.9837, 0.8664 and 0.9088 respectively which are greater than 6 times the values of their respective probable error. Hence, we can interpret that the correlation between two variables loan and advances and Net profit of all the three banks are certain and significant and as well as there is closeness between these two variables.

#### 4.5 Primary Data Analysis

Primary data are collected form listed commercial bank and investors or depositors as well as individual academicians. More than one respondent have been included form the same organization as far as possible. The respondent of the data cover personalities involving in policy formulation with the position of NRB directives.

**Table 4.14**  
**No of Respondents**

S. No.	Designation	Number
1	NRB Officials	10
2	Staffs of the commercial banks	12
3	Individual investors	6
4	Academicians	4
Total		32

*Source: Field Survey, 2009*

All together 32 respondents are analyzed in this section. In the first query that, How effective is the role of NRB in regulating and supervising of the

commercial bank; 22 respondents were with the opinion that, they are highly effective while 10 respondents were with the opinion that, NRB plays good supervisory role for the commercial banks. The second query was that, Which supervisory system is the best; 20 of the respondents shows their both (onsite and offsite inspection) are good for controlling and monitoring; while 7 of the respondents were with the favor of onsite inspection and only 5 respondents were in favor of offsite inspection. Third query was; to what extend are the effect of the NRB Directives on commercial bank; 18 of the respondents agreed that it helps in promoting safe and sound banking system, 10 of the respondent agreement to facilitate bank customers and 4 of the respondent agreed with the constraint bank activities. The fourth query was what is the reason behind the changes made in the directives?, 16 of the respondents were in opinion with to develop the better financial institutions. 12 people opines that to meet the international standard and 4 people said that the constraint bank activities and fifth questionnaire was to survey the opinion of the respondents why NRB directives are necessary to the commercial bank; 14 person said to protect interest of depositors, 12 person said to enhance the creditability of the financial system and 4 person said to protect the financial institution.

**Table 4.15**  
**Primary Data Analysis I**

S.N.	Statement	Weight			Mean	Ranking
		1	2	3		
1.	How effective is the role of NRB in regulating and supervising of the commercial bank?	-	10	22	2.69	I
2.	Which supervisory system is the best?	5	7	20	2.47	II
3.	What are the effects of the NRB Directives on commercial bank?	2	10	18	2.38	III
4.	What is the reason behind the change made in the directives	4	12	16	2.37	IV
5.	Why NRB directives are	4	12	14	2.19	V

	necessary to the commercial bank?					
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Source: Field Survey, 2009

The respondent of the sample have been presented as it is, sum of the respondents didn't assign the rank for the given alternatives has been shown in the no response column. The first query indicates that the most of the respondent agree with the highly effective supervising and regulating role of NRB on commercial bank. The mean of the first query is near about the rank 5. It means the NRB regulating or supervising role is better for the commercial bank. The second questionnaire indicates that the more than 50% of respondents agree that the both onsite and offsite inspection system is the best. So the NRB has always used to the onsite and offsite supervisory system. The third query finds out that the NRB directives support the commercial bank to promoting safe and sound banking system as well as facilitates the customers and the depositors. The fourth query indicates that the half of the respondent agree with the better financial institution and most of the remaining respondents agree with to meet the international standard. Finally, the fifth query indicate that all commercial banks has to necessarily implement the NRB directive which to protect the interest of depositors and to enhance the creditability of the financial system and to protect the financial institution.

**Table 4.16**

**Primary Data Analysis II**

S.N.	Statement	Weight			Mean	Ranking
		1	2	3		
1.	Are the commercial banks implementing the directives issued by NRB?	5	2	25	2.63	I
2.	Do you think it is necessary to implement the directives issued by NRB?	4	9	15	2.09	V
3.	Is there any access or shortfall in NRB directives?	9	5	17	2.19	IV
4.	What is the reason for setting capital adequacy norms?	6	7	18	2.31	III

5.	How your banks wish to meet the increase requirement capital as prescribed by NRB?	10	10	12	2.06	VI
6.	Who will be benefited most by maintaining capital adequacy requirement?	2	10	18	2.3	II

*Source: Field Survey, 2009*

Among the six alternatives provided, the respondents ranked that, the first query: Are the commercial banks implementing the directives issued by NRB; 25 respondents had the opinion in “yes” 2 respondents were with the negative opinion and 5 respondents were without any opinion. Most of the respondents agreed with the commercial banks were implementing the NRB directives regularly and minority of the respondent doesn't know about the NRB directives. The second query was that Do you think it is necessary to implement the directives issued by NRB; 15 respondent showed that they were agreed with the necessary implementation of the directives and remaining respondent don't know about the NRB directives as well as they said that it is not necessary to implement the NRB directives on commercial banks. The forth questionnaire was that, what is the reasons for setting capital adequacy norms; 19 respondent agreed with to protect the interest of depositors, 7 respondents said that to protect the interest of the borrowers and 6 respondents were in opinion that, to protect the financial institution. It means that more than 50% respondent agreed with to protect the interest of the depositors for setting capital adequacy norms. The fifth query was how your bank wish to meet the increase requirement of capital as prescribed by NRB; 12 respondents were in the favor of increasing the core capital, 10 respondents were with their opinion by increasing the supplementary capital and only 10 respondents were in the favor of adopting mergers and acquisitions of the same category commercial banks. It indicates that, all respondents equally emphasized to increase the core capital, supplementary capital and merger and acquisitions of the same types of firms. Finally sixth query that, who will be benefited most by maintaining capital adequacy requirement; 18 respondents agreed that, the depositors would be

benefited by maintaining capital adequacy requirement. 10 respondents agreed with the shareholder also be benefited and 2 respondent agreed that the others would be benefited, who are relating to the commercial banks.

**Table 4.17**  
**Primary Data Analysis III**

S.N.	Statement	Weight			Mean	Ranking
		1	2	3		
1.	Are the commercial banks allowed free to set capital adequacy ratio by them?	2	4	25	2.66	I
2.	Whether loan and advance are reviewed on periodic basis?	3	8	20	2.47	IV
3.	Is capital adequacy requirement set by NRB fit for regulation and supervision of commercial bank?	0	2	25	2.46	V
4.	Does the increase in requirement of Rs. 2 billion capital shall create a barrier for new entrants?	6	4	22	2.5	III
5.	Are the provisions in NRB directives about the black listing of the loan defaulter adequate?	6	10	16	2.31	VII
6.	Are you satisfied with the existing requirement of the percentage of the loan and loan loss provision of NRB?	6	2	24	2.56	II
7.	Do you think that commercial bank will be affected by new directives relating to borrower limit?	5	3	24	2.41	VI

*Source: Field Survey, 2009*

The first query was that: Should the commercial bank allow free to set capital adequacy ratio by them; 25 respondents were not in the favor of setting capital adequacy ratio by commercial banks. 4 respondents agreed to set Capital Adequacy Ratio by the commercial bank and 2 respondents don't know about the question. The 2<sup>nd</sup> query that whether loan and advance are reviewed on periodic basis; 20 respondents were in the opinion to review the loan & advances on periodic basis regularly, 8 respondents were not in the opinion of reviewing the loan & advance on periodic basis. The third query was that capital adequacy requirement set by NRB is fit for regulation and supervision of commercial bank; 25 respondent agreed with the right to setting capital adequacy requirement by NRB for its effective regulation and supervision on commercial bank and only 2 respondent did not agree to set the capital adequacy requirement by NRB. The fourth query was that Does the increase in

requirement of Rs. 2 billion capital shall create a barrier for new entrants; 22 respondents were with the opinion that, although the new capital requirement Act will create a barrier for new entrants but in long-term it will benefit the bank and financial institutions. 4 respondents were having neutral opinion regarding the new capital requirement Act. 6 respondents were not in the favor of new CRA. They were with the opinion that, it will stop the new players to make their entries in the banking industry. The fifth query was that, Are the provisions in NRB directives about the black listing of the loan defaulter adequate; 16 respondents were confirming that NRB have issued enough provisions to protect the banks from the defaulters. 10 respondents still have their opinion that, the existing provision of NRB are not sufficient enough to protect the bank from defaulters. 6 respondents were with the view that the NRB provisions can help to protect the bank only to some extent by the loan defaulters. The sixth query that, Are you satisfied with existing requirement for the loan and loan loss provision of NRB; 24 respondents showed their opinion that the loan and loan loss provision of present ratio is adequate to commercial banks. More than 50% respondent satisfied with the NRB loan loss provision directives, only 2 respondents would not satisfied with the present provision in NRB and 6 respondents did not know about the question. Finally, seventh query was that, Do you think that commercial banks will be affected by new directives related to single to borrower limit; 24 respondents expressed their opinion that it has not affected commercial banks activities and 5 respondents did not know about the question; 3 respondents were of the opinion that, it is effecting the bank adversely.

#### **4.6 Major Findings of the Study**

The major findings of the study are as follows:

##### **a. Nepal Investment Bank Limited**

Capital adequacy ratio and core capital of NIBL bank during the study period were within limit and even excess. Core capital to RWA is highest in the year

2060/61 while capital adequacy ratio is also highest in the same year 2060/61. The CAR is highly decreased during the fiscal year 2060/61 and then it slightly increases and core capital to RWA is fluctuating in every year. But if we see the figure of core capital, Supplementary capital and total capital fund then all are towards increasing trend. If we see the structure of total capital fund then contribution of core capital in total capital fund is around 71% while that of supplementary capital is only 23%. Core capital plays the dominant role in total capital fund. NIBL also gave more priority to core capital rather than supplementary capital. RWA is also increasing every year.

To meet the NRB requirement NIBL issues NIBL bond 2067 worth Rs.30 crore shareholders were provided with bonus share worth Rs.6.7999 crore and right share worth Rs.5.666 crore were issued in the fiscal year 2060/61 proposes to right issue in the fiscal year 2065/66 large portion of net profit were allocated in different reserve fund which has ultimately reduce the shareholders earning. Shareholders were provided dividend and bonus share in different year except in the year 2060/61 but in small volume as big portion of Net profit was blocked in reserves. In the portfolio of total loan and advances pass loan is around 95% while that of NPL is around 5% in average of five year. The trend of pass loan is increasing trend and NPL is decreasing during the fiscal year 2060/61 and thereafter it increase. Bad loan of NIBL is fluctuating but the last two year 2065/66 & 2061/65 it has highly increased, provision for all loans is not sufficient during the year 2060/61 to 2066/67.

#### **b. NABIL Bank Limited**

Capital adequacy ratio and core capital of NABIL bank during the study period were in excess position. Core capital to RWA and CAR is the highest in the year 2064/65 and slightly decreased in the fiscal year 2065/66 and 2066/67 compared to the fiscal year 2064/65 but if we see the figure of the core capital, supplementary capital and total capital fund all is in increasing trend as well as RWA is also increasing every year. In the portfolio of total capital fund contribution of core capital is around 86% while that of supplementary capital is

only 14% so that core capital plays dominate role in total capital fund. NABIL Bank gave more priority to core capital rather than supplementary capital. To meet the NRB requirement, NABIL bank announced the bonus share and right shares timely. NABIL Bank has provided regular dividend every year but the current year the bank has paid dividend in 100% of par value.

In the portfolio of total loan and advances, pass loan occupied around 96.25% while that of NPL is around 3.75% in average 5 year. The trend of pass loan is increasing every year while the trend of NPL decreased during the fiscal year 2060/61 to 2065/66 but in fiscal year the 2066/67 NPL has increased. Bad loan of NABIL is fluctuating every year. If the bad loan increases, loan loss provision also increase in the same ratio. Provision for all loans is not sufficient during the fiscal year 2060/61 to 2066/67. Provisioning value is increasing every year.

### **c. Standard Chartered Bank Limited**

Capital adequacy ratio and core capital of SC bank during the study period were within the limit and even excess. Core capital to RWA is highest in the year 2060/61 while capital adequacy ratio is also highest in the year 2060/61. The CAR and core capital to RWA has slightly fluctuated during the fiscal year 2060/61 to 2066/67 but if we see the figure of core capital, supplementary capital and total capital fund then core capital is in increasing trend while there is fluctuation in the supplementary capital but the total capital fund is in increasing trend. If we see the structure of total capital fund then contribution of core capital in total capital fund is around 86% while that of supplementary capital is only 14% SC Bank gave more priority to core capital rather than supplementary capital. RWA is in fluctuating position.

In the portfolio of total loan advances pass loan is around 96% while that of NPL is around 4% in average of five year. The trend of pass loan is in increasing trend every year and NPL is increasing trend during the FY 2060/61 to 2064/65 thereafter it decreases in 2066/67. Bad loan of SCBNL is fluctuating

every year. Provision for doubtful loan is not sufficient in the fiscal year 2064/65 in the NRB requirement.

The coefficient correlation and probable error of all the banks shows that net profit is closely related with loan and advance with every increase in the value of loan and advances. There is increase in net profit too so that net profit is dependent upon the total loan and advances as well as other investment of banking activities.

### **Findings of Primary Data:**

#### **From Analysis I:**

- a. The NRB regulating and supervising role is better for commercial bank operations.
- b. The onsite and offsite supervisory system of NRB is more relevant and appropriate for the banking operations.
- c. The NRB directives support the commercial bank to promoting safe and sound banking system as well as facilitate the customers and the depositors.
- d. The half of the respondent agreed with the idea of developing better financial institution and most of the remaining respondents agree on meeting the international standard as regard to the reasons behind the frequent changes in directives.
- e. Based on the respondents' opinion, majority of the respondents have opined that NRB directives are necessary to protect the interest of depositors as well as to enhance the creditability of the financial system.

#### **From Analysis II:**

- a. The commercial banks were implementing the NRB directives regularly and minority respondent don't know about the NRB directives.

- b. More than 50% respondents agreed with to protect the interest of the depositors for setting capital adequacy norms. The respondent agrees with the interest of the depositors.
- c. All respondent have equally emphasized in the increasing core capital, supplementary capital and merger and acquisitions of the same types of firms.

**From Analysis III:**

- a. Majority of the respondents were in the opinion that, commercial banks should not be allowed freely to set their norm of capital adequacy ratio, rather it should be under the strict directives of NRB.
- b. Loan and advance should be reviewed on periodic basis.
- c. Capital adequacy requirement set by NRB are fit for regulation and supervision of commercial bank.
- d. The increase in requirement of Rs. 2 billion Capital Requirement Act shall create a barrier for new entrants.
- e. The provisions in NRB directives about the black listing the loan defaulter are enough/adequate.
- f. The loan and loan loss provision of present ratio is adequate to commercial banks.
- g. Commercial bank shall not be much affected with the new directives of single borrower limit.

## CHAPTER V

### **SUMMARY CONCLUSION AND RECOMMENDATIONS**

#### 5.1 Summary

The economic development of a country cannot be imagined without the development of commerce and industry. The role of commercial banks in the economic growth of nation can be estimated to be prominent. The very challenging job of commercial banks is to collect the scattered idle resources from the small savers. Actually, commercial banks pool the fund in the sizable volume in order to feed the fund requirement of productive sector promote trade and industrialization in the country there by raising the employment opportunity and earned to the labours and materials suppliers to such industries and traders.

Commercial banks play very important role in this up growing economy. Regardless the various services they provide today, in general, commercial banks can be defined as an organization that lends money to people and institution who promise to repay the loan with interest over a specified period of time. Nepal Rastra Bank is the father figure of commercial banks. NRB created them and it guides them all the ways as how to work. More than that, NRB has full control over the functions of commercial banks established all over the country. It has provided guidelines to the commercial banks, which is more or less like a boundary drawn by the NRB for the functions of the commercial banks which basically is for the security of depositors, who deposit their savings in the banks.

An attempt of studying the lending practices of the commercial banks of Nepal is made in the thesis report. Four reputed commercial banks were taken as the sample for the study and the study is made around those four commercial banks namely NABIL bank, Everest Bank Ltd, Bank of Kathmandu Ltd and Nepal Investment Bank Ltd. The quantitative analysis, for the findings and conclusion, were made of the data collected from these commercial banks.

The findings were drawn analysis the five years data of above mentioned commercial banks. Different ratios were calculated to get the results for conclusions. Since the topic of the study revolves around the lending practices, the distribution of loans and advances, their recovery, and the ratios of those items that are related to the distribution and recovery of loans and advances are calculated.

## 5.2 Conclusion

The measurement of lending strength in relative terms has revealed that NIBL has the highest investment to loans and advances and investment ratio. This ratio gives the portion of risk free investment out of total loans and advances and investment. NABIL has the highest loans and advances and investment to total deposit ratio referring that it has the maximum mobilization of deposits than others.

The absolute measure of lending strength reveals that NABIL has the highest mean of loans and advances with a fluctuating trend but similarly it also has the highest standard deviation. Considering the most years' data off all the four commercial banks under the study are all in the line with directives provided. In case of term loan, NRB directives have set the standard of 75% but the punishment of providing loan loss provision is the same. None of the commercial banks have ever exceeded this limit; none of them have ever reached even 60% till date.

The measurement of efficiency in lending has revealed that loan loss provision to total loan & advances ratio is pretty satisfactory since according to NRB directives loan loss provision indicates provision against both performing and non-performing loans. Thus, the increase in good loan increases the loan loss provision.

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