

# CHAPTER - I

## INTRODUCTION

### 1.1 Background of the Study

Banking sector plays a vital role for the country's economic development. Bank is a resource mobilizing institution, which accepts deposit from various sources, and invests such accumulated resources in the fields of agriculture, trade, commerce, industry and tourism etc.

With the development of liberalized and market oriented economy, the banking and financial system is also expanding gradually, resulting with the introduction innovative financial services and instruments (Aryal, 2060: 63).

The banking sector is mainly responsible for collecting household savings in terms of different types of deposit and regulating them in the society by lending in different sectors. The banking sector has now reached to the remote areas of the country and has experienced a good deal in the growth of the economy. By lending their resources in small scale industries under intensive banking program has enabled the banks to share in the economic growth of the economy.

There are various types of banking institutions, which are performing different functions in the context of Nepal. It can be divided into three parts: The Central Bank, Commercial Banks and other financial institutions, which are also known as financial intermediaries. All of these financial intermediaries deal with money or money related transactions.

Banks collect the funds from public who have savings and disperse the fund to the person who is in need of it. This way, whole infrastructure of national development, direction of economy, rate of progress and even the habit of people

is being the function of banking systems. Banks function of lending ensures required volume of capital to resources mobilization. The primary issue of economic development is to increase the investment in productive sector. The increase in investment impacts positively in every sector of economy such as employment, production, income, government revenue, international trade etc.

The banking business has its genesis from its function of lending. Lending is the most fundamental function of a bank. The pace of time has changed the portfolio of banking business from its primary functions such as merchant banking, credit card business, documentary credit, traveler cheque businesses etc. Lending has its different forms. It can be divided into fund based and non-fund based lending. The fund based lending can be further divided into cash credit overdrafts, demand and term loans, bills purchased and discounted and export packing credit, project finance, consortium finance, loan syndication, bridge loan etc.

The history of organized modern banking system begins in Nepal only after the establishment of a commercial bank i.e. Nepal Bank Ltd. in 30<sup>th</sup> Kartik 1994 B.S. with an authorized capital of Rs. 10 million and paid up capital Rs. 842 thousands. With the opening of NABIL bank in 1985 A.D. the door of opening commercial banks was opened to the private sector. Then whole lot of commercial banks was expanded in Nepal. Today probably, all the banks are running in profit. There is some inefficiency of public sector banks which have lead to the success of other private banks. Among the commercial banks, Bank of Kathmandu is the one. It was established on 28<sup>th</sup> Falgun 2051 B.S. with paid up capital of Rs.436.6 million. During the establishment of this bank the shares were divided among Nepalese partners, general public and Sian commercial bank of Thailand with 45%, 25% and 30% respectively. Sian commercial bank of Thailand withdrew its shares later on .Now 42% shares of this bank are held by Nepalese promoters and rest by general public.

## **1.2 Focus of the Study**

The study is focused on the relationship between banker and its clients and overall performance of Bank of Kathmandu and at which level the Bank of Kathmandu has been able to provide its services and obtain business and study about the sector of investment. Its focus is on the strict government rules and regulation that has limited the sector of expansion. The main focus of the study is to highlight the lending, investment and deposit policies of Bank of Kathmandu expecting that the study can bridge the gap between deposits and investment policies. On the other hand, the study would provide information for the management of the Bank that would help them to take corrective actions. The uplifting of the development of a nation depends largely upon the development of its economic growth. Bank is an institution, which helps in collecting and mobilization of savings. The role of commercial banks in the uplifting of the economic growth of the country is very important and the internal management of the bank greatly influences the development of the economy of the nation. This research focuses on the study of financial performance of Bank of Kathmandu.

## **1.3 Statement of the Problem**

Some of the commercial banks are continuously making profit and satisfying their shareholders and returning them adequate profit. This has attracted the potential customers to deposit their money into banks, as there are very few sectors to make a profitable investment and the investors are always reluctant to risk. They do not take initiation to invest in other sectors. Therefore commercial banks have a lot of deposits but very little investment opportunity. They are even discouraging people by offering very low interest rate and minimum threshold balance. This will definitely make inverse impact on economy of the country. This has decelerated the pace of economic development. Lack of sound investment policy is another reason for a commercial bank not to properly utilize its deposits that is making loan and advances or lending for a profitable project. This condition will lead the

commercial bank to the position of liquidation. They face so many difficulties to mobilize their deposit fund on the profit making investment, so they can achieve sufficient return from the investment and satisfy their shareholder. The lack of knowledge on financial risk, interest rate risk, management risk, business risk, liquidity risk, default risk and purchasing risk, granting loan against insufficient deposit, overvaluation of goods pledge, land and building mortgaged, risk averting decision regarding loan recovery and negligence in recovery of overdue loan are some of the basic lapses and the result of unsound credit policy sighted in the banks.

A sound banking system providing varieties of banking services to fulfill commerce, trade, industry and agricultural needs of the country is of crucial importance for Nepal. In this way that commercial banks are the backbone of the economy of a country, it is highly useful to make the present study on the Bank of Kathmandu Ltd. This study enables us to see clear vision of the status of the banks like how effective and attractive its profitability position is, how its income and expenditure status is and how far it has achieved success of any business enterprises. But the financial performance of the enterprises in Nepal is quite dismal and has not been able to contribute towards the generation of surplus.

The financial performance of any financial institution can be evaluated with the aid of balance sheet and profit & loss account. The bank must provide with the statistical information about their business. The information must be provided in a prescribed form for the publication. However, the details of the information regarding loan disbursement are not accessible in the both banks. So, the evaluation of financial performance of the banks has been done with the aid of balance sheet and profit & loss account only.

#### **1.4 Objective of the Study**

The main objective of this research is to examine the financial performance of Bank of Kathmandu Ltd .The specific objectives of this study are as follows:

- i. To evaluate the liquidity, efficiency of assets, efficiency of assets management and profitability position of the banks under study.
- ii. To find out the positive factors that enhanced the performance of the banks and to provide suggestions and recommendations on the basis of findings.
- iii. To find out the relationship between deposit, loan and advances, investment, net profit and total outside assets.
- iv. To examine the growth rate of the bank in terms of deposit, loan and advances, investment, net profit and total outside assets trends of the bank.
- v. To analyze the trends of deposit utilization towards total investment and loans and advances.
- vi. To provide a useful feedback for academic institutions, bank employees, trainees and investors and also for financial person, policy maker and other persons concerned with bank.

Objective of the study is to identify the problems being faced by the commercial banks at the present economy and their solution. The economy of Nepal is poor and is on downward trend. In the same place commercial banks are emerging like mushroom and they have to fight for their survival by providing best services to their customers.

#### **1.5 Importance of the Study**

There is less availability of research work, journal and journal and articles in the financial performance of commercial banks as well as other financial institutions in the context of Nepal. This study on financial performance of the bank analyzes the different indicators such as liquidity ratio, capital structure ratio, profitability ration, EPS, trend of different components of assets and liabilities, net profit etc.

This provides valuable information that is necessary for the management of the bank, which would help them to analyze the current situation and take corrective action. The success and prosperity of the bank relies heavily up in the successful investment of collected resources to the important sector of economy. Good investment policy has a positive impact on economic development of the country and vice versa. So the investment policy of commercial banks should be in accordance with the spirit of the economic upliftment of the people.

### **1.6 Limitation of the Study**

This study attempts to evaluate the financial performance of two banks. In this fast changing world it is difficult to cope with the pace of the changing technology. Due to the arrival of unforeseen difficulties every study is accompanied by some natural limitations. Some of those limitations are:

- i. This is the study of only financial performance of Bank of Kathmandu Ltd. So this will not provide overall performance of other banks.
- ii. Mostly the data used in this study might be of secondary type. Hence, any misrepresentation, mistakes, omissions etc, will affect the outcome of the study.
- iii. Some of the statistical as well as financial tools of comparison and analysis shall be used in this study. So any drawback and weakness of those tools may adversely affect the outcome of the study.

### **1.7 Organization of the study.**

The Study is divided in the following chapters as prescribed by the university.

Chapter - I: Introduction

Chapter - II: Review of Literature

Chapter -III: Research Methodology

Chapter - IV: Data Analysis and Presentation

Chapter - V: Summary, Conclusion and Recommendations

## Chapter - I: Introduction

First chapter includes background of the study, focus of the study, statement of the problem, objective of the study, importance of the study, limitations of the study and organization of the study.

## Chapter - II: Review of Literature

Second chapter includes conceptual framework, review of related studies.

## Chapter -III: Research Methodology

Third chapter includes research design, analysis of Data.

## Chapter - IV: Data Analysis and Presentation

Fourth chapter includes data presentation and analysis and major findings of the study.

## Chapter - V: Summary, Conclusion and Recommendations

Fifth chapter includes summary, conclusions & recommendations, bibliography and appendices

## **CHAPTER - II**

### **REVIEW OF LITERATURE**

#### **2.1 Conceptual Framework**

Many banking functions such as safeguarding funds, lending, guaranteeing loans, and exchanging money can be traced to the early days of recorded history. In medieval times the Knights Templar, an international military and religious order, not only stored valuables and granted loans but also arranged for the transfer of funds from one country to another.

“The history of banking development, we can not forget the bank of Casa de San Giorgio in Genoa, was established in 1148; Bank of Venice was established in 1157 and Bank of Genoa was established in 1148. In modern bank started to take rapid speed in forming & functioning from 17<sup>th</sup> century. During this period, Bank of Milan, Bank of Florence and Bank of St. George were established in Genoa. In 1609 the Bank of Amsterdam was established in Germany and the Bank of England was established in England. In the context of Nepal, for the first time, the Nepal Bank Limited was established in 1994 and the Central Ban of Nepal (Nepal Rastra Bank) was established in 1957” ( Bhandari : 5)

In the 17th century, English goldsmiths provided the model for contemporary banking. Gold was stored with these artisans for safe keeping, and was expected to be returned to the owners on demand. The goldsmiths soon discovered that the amount of gold actually removed by owners was only a fraction of the total stored. Thus, they could temporarily lend out some of this gold to others, obtaining a promissory note for principal and interest. In time, paper certificates redeemable in gold coin were circulated instead of gold. Consequently, the total value of these banknotes in circulation exceeded the value of the gold that was exchangeable for the notes.

Two characteristics of this fractional-reserve banking remain the basis for present-day operations. First, the banking system's monetary liabilities exceed its reserves. This feature was responsible in part for Western industrialization, and it still remains important for economic expansion, though a risk of creating too much money is a rise in inflation. Second, liabilities of the banks (deposits and borrowed money) are more liquid—that is, more readily convertible to cash—than are the assets (loans and investments) included on the banks' balance sheets. This characteristic enables consumers, businesses, and governments to finance activities that otherwise would be deferred or cancelled; at the same time, it opens banks to the risk of a liquidity crisis. When depositors en masse request payment, the inability of a bank to respond because it lacks sufficient liquidity means that it must either renege on its promises to pay or pay until it fails. A key role of the central bank in most countries is to regulate the commercial banking sector to minimize the likelihood of a run on a bank, which could undermine the entire banking system. The central bank will often stand prepared to act as lender of last resort to the banking system to provide the necessary liquidity in the event of a widespread withdrawal of funds. This does not equal a permanent safety net to save any bank from collapse, as was demonstrated by the Bank of England's refusal to rescue the failed investment bank Barings in 1995.

### **Commercial Bank**

“Banks which are established to accept deposit and grant loan to the industries, individuals and traders with a view to earn profit are known as commercial banks” (Pandey: 30).

Commercial banks are the heart of the financial system. They hold the deposits of many persons, government establishment and business unit. They make fund available through their lending and investing activities to borrows, individual business firms and services from the producers to customers and the financial

activities of the government. They provide a large portion of the medium of exchange and they are media through which monetary policy is affected. These facts show that the commercial banking system of the nations is important for the functioning of the economy.

Banks, organizations that carry out the business of banking, take deposits and then using those deposits to make loans. In essence, a bank aims to make a profit by paying depositors a lower rate of interest than the rate the bank charges borrowers. In accounting terms, deposits are considered liabilities (because they have to be repaid), and loans are considered assets, though some become bad debts. Banks in most countries are supervised by a central bank, such as the Bank of England in the United Kingdom, the Bundes bank in Germany, the Nepal Rastra Bank in Nepal and the Federal Reserve System in the United States.

There are many different types of bank, and the banking structure varies from one country to another. Broadly speaking, banks fall into the following categories; but, as a result of increased competition and an increase in the range of services offered by banks, the differences between categories have been blurred.

Bank of Kathmandu, one of the companies, with its own legal entities performs business activities for the purpose of earning profits. There are number of stakeholders of the bank such as shareholders, management, depositors, employees and workers, clients and government who are keep to know about the result of its financial activities performed during a certain period of time. Therefore, in order to communicate the results of business operations and financial position to its stakeholders, the company prepares and publishes the statement of its financial affairs on a periodical basis. The statement so prepared facilitates as financial statements analysis.

### **2.1.1 Concept of Financial Performance**

Financial statements are written reports of financial affairs of a company. They report and communicate the results of its business operations for a particular period of time and its financial position at the end of that period. The result of the company's business operations are revealed by the net profit it has earned during the period. The financial position of the company is determined by presenting the picture of its assets, liabilities and shareholders' equity at the end of the period. Generally, therefore, the financial statements of the company include its income statement and balance sheet. Moreover, the company is required to prepare and publish cash flow statement at the end of the period, besides profit and loss account and balance sheet.

The following are the objectives of financial statements.

- ) To provide the financial information to the users.
- ) To provide useful financial information for predicting, comparing and evaluating potential cash flows of the business.
- ) To help the users to know regarding earning power of the business.
- ) To provide information to judge management's ability to utilize resources effectively.
- ) To provide statement of financial position concerning assets and liabilities of the business.
- ) To provide the financial statements on periodic basis to make the comparison of progress of the business.
- ) To provide useful information for financial forecasting.

The following are the importance of financial statements.

- ) It provides the information relating to existing profit, earning per share, possibility of growth, cost information and other necessary financial information.

- )] It provides the information relating to the chances of business promotion and capacity of the business.
- )] It provides the information to the employees relating to changes increments of salary, bonus, job security, employee's welfare schemes etc.
- )] It provides the information to the creditors and bankers and other financial institutions to know the capability to repay the amount and interest as and when repayment becomes due.
- )] It provides the information to the government to know the amount of tax on the revenues.
- )] It provides the information to the customers about new product research, social responsibility and other policies of the business.
- )] It provides the information to the potential investors to know the earning potential of the business.

The following are the limitations of financial statements.

- )] It provides the information relating to only monetary facts.
- )] It records the financial information relating to historical in nature.
- )] It is only interim report.
- )] It is influenced by accounting concept.
- )] It fails to disclose the adequate information.
- )] It ignores the effect of price level changes.
- )] It is prepared primarily for shareholders.

Financial performance means financial activities of the company directed towards achieving its value maximizing objective. For the better financial activities, effective and efficient decisions are necessary and those better financial activities contribute to excellent financial performance which in turn results to growth of the organization.

Financial performance is very important to decision maker. The growth and development of a company is fully affected by financial performance and it is correct when true facts and figures are sort out. Generally income statement and balance sheet are prepared to know the result of operation and financial position of the company respectively.

Financial statements are used to study the financial performance of the company. Financial statements provide information about a company's position at a point in time as well as its operative over same periods.

“From an investor's standpoint, predicting the future is what financial statement is all about, while from management's standpoint, financial statement analysis is useful both as a way to anticipate future conditions and, more important, as a starting point for planning actions that will influence the future course of events” (Weston and Brigham, 1996:96).

Financial performance as a part of financial management is the main indicator of the success or failure of the company. All the stakeholders viz. shareholders, debenture holders, financial institutions, government expect the sound financial condition of the company. However, financial aspect is one of the most neglected aspects of public enterprises in Nepal. But, joint venture banks have been analyzing their financial performance in order to take corrective actions in timely manner. In the context of Nepal, commercial banks are playing vital roles for the economic growth of the country and Bank of Kathmandu is the one. It has achieved a great success in terms of market share and profitability because of its professional and reliable services to customers. Therefore, it would be clear and transparent to analyze the financial performance of this bank by using various measuring financial tools.

### **2.1.2 Financial Statement Analysis**

Financial analysis is the process of identifying the financial strength and weakness of the concern. It is performed to determine the liquidity, solvency, efficiency and profitability of the organization. It gratifies of the needs of the concerned parties like potential investors, shareholders, government, general public, short term as well as long term creditors and management itself about their vested interest providing them with adequate information.

Analyzing financial statements is a process of evaluating financial statements is a process of evaluating the relationship between component parts of financial statements to obtain a better understanding of a firm's position and performance.

Analysis of financial statements is performed to take managerial and financial decisions. Financial analysis refers to the process of extracting and studying information in financial statements for use in management decision making.

Financial Analysis is a process of identifying the financial strength and weakness of the firm by properly establishing relationship between the item of balance sheet and the profit and loss account.

Thus, financial strength, weakness and position are reflected by financial analysis. In financial analysis, financial statements such as income statement and balance sheet are mainly analyzed through different tools and techniques.

The analysis of financial statement is necessary, the reason is that Profit and loss account, Balance Sheet and Funds flow statement provide so many information. Different tools are used to analyze the financial performance of the company. Ratio Analysis is an important tool for analysis the company's financial performance. Ratio Analysis is an important technique of financial statement analysis. Accounting ratios are useful for understanding the financial position of the company. Different users such as investors, management, bankers and

creditors use the ratios to analyze the financial statement of the company for their decision making purpose.

The above definition reveals that information is collected through the analysis of financial statements, which may be useful for different purposes. For example, to know the position and performance of the company.

The following are the important objectives of financial statement analysis.

- i. To know about the profitability: The financial statement analysis provides information about the profitability of the company in terms of investment. The profitability scenario helps shareholders to decide whether to continue holding its shares and other potential investors to decide whether to invest in its shares or not.
- ii. To judge solvency: An analysis of financial statements is helpful for judging the short-term and long-term solvency of the company. The banks with such information will be in a position to decide whether it should extend loan or not.
- iii. To measure: The analysis of statements helps to measure the financial strengths and weaknesses of the company, which is essential for deciding its future course of action.
- iv. To assess managerial performance: The financial statement analysis is essential for measuring the company's managerial performance, which is important to decide about rewarding the management or taking action against it.
- v. To make future planning: The financial statement analysis provides relevant information about the present position of the company. The present position of the company provides guidelines for making future plans of the company by deciding what courses of action it should take to achieve its objectives.

The financial statement analysis is important for different reasons.

- i. Holding of share: Shareholders are the owners of the company. Time and again, they may have to take decisions whether they have to continue with the holdings of the company's shares or sell them out. The financial statement analysis is important as it provides meaningful information to the shareholders in taking such decisions.
- ii. Decisions and plans: The management of the company is responsible for taking decisions and formulating plans and policies for the future. They, therefore, always need to evaluate its performance and the effectiveness of their actions to realize the company's goal in the past. For that purpose, financial statement analysis is important to the company's management.
- iii. Investment decisions: The prospective investors are those who have surplus capital to invest in some profitable opportunities. Therefore, they often have to decide whether to invest their capital in the company's shares. The financial statement analysis is important to them, because they can obtain useful information for their investment decision making purpose.
- iv. Extension of credit: The creditors are the providers of loan to the company. Therefore, they may have to take decisions as to whether they have to extend their loans to the company and demand for higher interest rates. The financial statement analysis provides important information to them for their purpose.
- v. Higher Benefits: The employees of the company sometimes may have to decide whether they have to demand for higher benefits such as wages and salaries from management. The financial statement analysis is significant to them, because it provides them with meaningful information to raise their voice for their cause.
- vi. Short term loans: The banks provide short term loans to the company for meeting its working capital needs. Therefore, they may have to decide whether to extend or increase short term loans to the company. In such a

- situation, they may have to resort to financial statement analysis as it provides them relevant information to reach a decision.
- vii. Compliance with law: The financial statement analysis is significant to comply with the prevailing rules and laws. The analysis may also be used to assess corporate taxes.

### **2.1.3 Factors Affecting Financial Structure**

Some of the empirical factors that affect the financial structure of the firm are given below.

#### **i. Growth Rate of Sales**

The future growth rate of sales is a measure of the extent to which the earnings per share of a firm are likely to be magnified by leverage. If sales and earnings grow at a rate of 8 to 10 percent a year, for example, financing by debt with limited fixed charges should magnify the returns to owner of the stock. However, the common stock of a firm whose sales and earnings are growing at a favorable rate commands a high price: this favors equity financing. The firm must weigh the benefits of using leverage against the opportunity of broadening its equity base when its common stock prices are high.

#### **ii. Cash Flow Stability**

Cash flow stability and debt ratios are directly related. With greater stability in sales and operating earnings, a firm can incur the fixed charges of debt with less risk than when its sales and earnings are subject to substantial declines. When operating cash flow is low, the firm may have difficulty meeting its fixed interest obligations.

### **iii. Industry Characteristics**

Debt-servicing ability is dependent on the profitability, as well as the volume of sales. Hence, the stability of profit margins is as important as the stability of sales. The ease with which new firms can enter the industry and the ability of competing firms to expand capacity both influence profit margins. A growth industry promises higher profit margins, but such margins are likely to narrow if the industry is one in which the number of firms can be easily increased through additional entry.

### **iv. Asset Structure**

Asset structure influences the sources of financing in several ways. Firms with long-lived fixed assets, especially when demand for their output is relatively assured, use long-term mortgage debt extensively. Firms that have their assets mostly in receivables and in inventories whose value is dependent on the continued profitability of the individual firm rely less on long-term debt financing and more on short-term financing.

### **v. Management Attitudes**

The management attitudes that most directly influence the choice of financing are those concerning control of the enterprise and risk. Large corporations whose stock is widely owned may choose additional sales of common stock because such sales will have little influence on the control of the company.

In contrast, the owners of small firms may prefer to avoid issuing common stock in order to be assured of continued control. Because they generally have confidence in the prospects of their companies and because they can see the large potential gains to themselves resulting from leverage, managers of such firms are often willing to incur high debt ratios.

## **vi. Lenders Attitudes**

Regardless of managements' views, lenders' attitudes determine financial structures. The corporation discusses its financial structure with lenders and gives much weight to their advice. But, if management seeks to use leverage beyond norms for the industry, lenders may be unwilling to accept such debt increases. They emphasize that excessive debt reduces the credit standing of the borrower and the credit rating of the securities previously issued. The lenders' point of view has been expressed by a borrower, who stated, "Our policy is to determine how much debt we can carry and still maintain an Aa bond rating, then use that amount less a small margin for safety" (Clark, 2003:59).

### **2.1.4 Concept of Ratio Analysis**

Accounting ratios are important for judging the firm's efficiency in terms of its operation and management. They help judge how well the firm has been able to utilize its assets and earn profits. Accounting ratios are also used to establish future trends of its financial performance. As a result, they help to formulate the company's future plans. It is essential for a company to know how well it is performing over the years and as compared to the other firms of the similar nature. Besides, it is also important to know how well its different divisions are performing among themselves in different years. Ratio analysis facilitates such comparison.

"The relationship of one term to another expressed in simple mathematical form is known as ratio" (Kennedy and Mc Mullen, extract from Koirala, 2005:260).

"A ratio is simply one number expressed in terms of another. It is found by dividing one number by another" (Anthony, Extract from Koirala, 2005:260).

From the above definitions, it is clear that a ratio is a relationship between two numerical variables. Since absolute numerical figure on its own does not speak much, ratio which is a relative expression between at least two numerical figures has to be calculated to obtain meaningful information thereof.

Ratio analysis is a process of determining and presenting the quantitative relationship between two accounting figures to evaluate the strengths and weaknesses of a business. It is important from the point of view of investors, creditors and management for analysis and interpretation of a company's financial health. It is also useful analysis of financial statement for judging the company's operating efficiency, identifying strengths and weaknesses and comparing its performance with other companies.

The following are the important advantage of the accounting ratios.

- i. Analysis financial statements: Ratio analysis is an important technique of financial statement analysis. Accounting ratios are useful for understanding the financial position of the company. Different users such as investors, management, bankers and creditors use the ratios to analyze the financial statement of the company for their decision making purpose.
- ii. Judging efficiency: Accounting ratios are important for judging the company's efficiency in terms of its operations and management. They help judge how well the company has been able to utilize its assets and earn profits.
- iii. Locating weaknesses: Accounting ratios can also be used in locating weaknesses of the company's operations even though its overall performance may be quite good. Management can then pay attention to the weaknesses and take remedial measures to overcome them.
- iv. Formulating plans: Although accounting ratios are used to analyze the company's past financial performance, they can also be used to establish

future trends of its financial performance. As a result, they help formulate the company's future plans.

- v. Comparing performance: It is essential for a company to know how well it is performing over the years and as compared to the other firms of the similar nature. Besides, it is also important to know how well its different divisions are performing among themselves in different years. Ratio analysis facilitates such comparison.
- vi. Inter-intra firm comparison: A firm may like to compare its performance with that of other firms and of industry in general. The comparison is called inter firm comparison. If the performance of different units belonging to the same firm is to be compared, then it is called intra firm comparison. Such comparison is almost impossible without proper accounting ratios. Even the progress of a firm from year to year can not be measured without the help of ratios.

## **2.2 Review of Journals and Articles**

After liberalization policy of government of Nepal, number of banks and financial institutions has been increased. As a result, the financial system has been experiencing and facing tough competition among the players of the financial systems. But in most of the cases, they are concentrated on the urban areas and due to the insecurity most of the banks and financial institutions have closed down their rural branches. Rastriya Banijya Bank and Nepal Bank Limited have closed their branches in different parts of the country. But after peace agreement and election of constituent assembly, they are going to establish their branches in these areas. Majority of Nepalese people are still out of the banking facility. Commercial banks and financial institutions are focusing their activities in urban areas.

**Govinda Bahadur Thapa** (1994), expresses his views in his research paper “*Financial System of Nepal*” that the commercial banks including foreign joint venture banks seem to be doing pretty well in mobilizing deposits. Likewise, loans and advances of these banks are also increasing. But compared to high credit needs particularly by newly emerging industries, the bank still seems to lack adequate funds. The banks are increasing their lending to non –traditional sectors along with the traditional sectors. Out of all commercial banks (excluding two recently opened regional commercial banks), Nepal Bank Ltd. and Rastriya Banijya Bank are operating with a nominal profit, the later turning towards negative from time to time. Because of growing competition and limitation of investment sectors, the spread between interest income and interest expenses is declining. These banks have not been able to increase their income from commission and discount. On the contrary, they have got heavy burden of personal and administrative overheads. Similarly, due to accumulated overdue and defaulting loans, profit position of these banks has been seriously affected. On the other hand, the foreign joint venture banks have been functioning in an efficient way. They are making profit year after year and have been distributing bonus to their employees and dividends to their shareholders.

He concludes that by its very nature of the public sector, these two domestic banks couldn't compete with the private sector banks, so only remedy to the problems of these banks, as the government decided, is to hand over the ownership as well as the management of these banks to the private hands.

**Radhe S. Pradhan**, (2003), in his research paper “*Role of Saving, Investment and Capital formation in Economic Development, A case of Nepal*,” has studied about the strong role and impact of saving, investment and capital formation on economic development of Nepal. This study is based on secondary data only. The necessary data on saving, investment, capital formation and gross domestic

product has been collected for the period of 1974/75 to 2000/01. The role and impact of saving, investment and capital formation on economic development were analyzed by using various regression models. The regression equations used in this study have been estimated at current prices as well as in real terms with the entire study period divided into different sub periods.

The results presented in this paper suggest that in all cases, GDP is significantly associated with saving, investment and capital formation both at current prices and in real terms. The results of the empirical analysis led to three important conclusions: First, saving, investment and capital formation have positive impact on economic development. Second, the current values and past values of saving, investment and capital formation have positive impact on economic development but the current values have the largest impact. Third, there is a strong role played by saving and capital formation on economic development while weak role-played by investment.

**Upendra Kumar Paudel** (2064 B.S.) expresses his view in his article “*The Changing Scenario of Nepalese Banking and Financial Institutions*” that the Nepalese economy is rapidly integrated with the global economy with its outward oriented policies followed by membership of WTO, SAFTA and BIMSTEC and the country is in process of institutional restructuring of financial sector. The face of banking has changed tremendously after the adoption of financial liberalization policy since 1980s. Hence, Nepal is in process to make banking system more transparent and international delivery standard. Banks need to go beyond peripheral issues and tackle significant issues like improvement in profitability, efficiency and technology, while achieving economies of scale through available cost effective solutions. These are some of the major issues that need to be addressed by banks in recent scenario, for their success and not just survival, in the changing milieu. As a regulator of country’s financial and banking institutions,

Nepal Rastra Bank always directly and indirectly advised banks and financial institutions to increase their financial base. The plan for capital enhancement is one of the best solution to increase capital strength of banks and complying basle accord. The financial performance of joint venture and private small banks are efficient and making fairly good levels of profit, while government dominated banks are still less efficient in the face of increased competitive environment. Growing economic sophistication, global financial integration, trade and investment interdependence and revolution in information and communication technology are influencing in the banking sector tremendously.

### **2.3 Review of Thesis**

**A. K. Jha** (2001), in his thesis entitled, “*A Comparative Study on Financial Performance of NGBL and NSBI*” has pointed out following objectives.

- i. To evaluate liquidity position of the bank.
- ii. To analyze comparative financial performance of both bank.
- iii. To study the comparative position of both banks.
- iv. To offer a package of suggestion to improve the financial performance.

His research analysis of the study is:

- i. The banks have been successful in using the depositors fund properly in Loan and Advances over the study periods.
- ii. Both banks have meets the standard of current ratio, i.e. 2:1.
- iii. Net profits of both banks are in increasing trend.

The major findings of this study are as follows.

- i. Liquidity position, in terms of cash and bank balance to total deposit of NGBL is found to be higher than that of NSBI.
- ii. The loan and advances ratio of NSBI is higher than NGBL which implies that NSBI is successful in utilizing the outsiders' fund.

- iii. Long term debt to total assets of NGBL is slightly higher than NSBI which implies more use of long term debt.
- iv. Earning per share of NSBI is very low in comparison to NGBL.

**Prabhu Narayan Pradhan** (2004), in his thesis, “*A Comparative Study on Financial Performance of HBL and SCBNL*” has pointed the following objectives.

- i. To analyze comparative financial performance of bank.
- ii. To evaluate liquidity position of both banks.
- iii. To identify the relationship between interest earned and operating profit.
- iv. To offer a package of suggestion to improve the financial performance.

His research analysis includes:

- i. Current ratios for both the banks are satisfactory.
- ii. Although Cash reserve ratio is managed by both banks as per Nepal Rastra Bank directives, both banks have not paid sufficient insight towards cash management. Their cash reserves have fluctuated in a high degree.
- iii. The Bank has increased investment in government securities.
- iv. Deposit utilization of both Banks is less effective. The analysis of growth ratios shows that growth ratios of total deposit, loan and advances, total investment and net profit of HBL are less than that of SCBNL.

The major findings of this study are as follows.

- i. Cash Reserve of both banks is below the standard. This might effect the liquidity position of these banks.
- ii. SCBNL’s loan and advances to total deposit ratio are significantly lower than that of HBL.
- iii. SCBNL is strongly recommended to follow liberal lending policy and invest more and more percentage amount of total deposits in loan and advances.

- iv. HBL is strongly recommended to increase its EPS and DPS to keep investors within the bank.

**Babu Kaji Karki** (2005), in his thesis, “*A Comparative Analysis of Financial Analysis of Financial Performance of NABIL and SCBNL*” has pointed out following objectives.

- i. To evaluate liquidity position of both banks.
- ii. To analyze comparative financial performance of both banks.
- iii. To study the comparative position of both banks.
- iv. To identify the relationship between interest earned and operating profit.

His analysis includes:

- i. The total assets of NABIL and SCBNL are in increasing regularly.
- ii. The amount of loan and advances of both banks are in increasing order.
- iii. The return on total assets is in fluctuating trend during the study period.

His major research findings are:

- i. SCBNL has efficiently operated its long term fund, deposit and assets to generate more profit.
- ii. Liquidity position of NABIL bank is favorable in many cases it seems expensive. The proposed recommendations for these banks are to reduce its excessive non-performing assets and invest on income generating current assets while SCBNL must strengthen the liquidity position.
- iii. Comparatively SCBNL’s profit ability is better than that of NABIL.

**Anita Jha** (2007), in his thesis, “*Financial Performance of Nepal Insurance Company Ltd*” has the following objectives.

- i. To analyze the financial position and insurance practices of NICO.

- ii. To evaluate the performance in terms of liquidity, profitability, turnover and cash flow position of NICO.
- iii. To identify the future trend of different indicator in relation to the general insurance and to determine the empirical relationship between the variables.

His analysis includes:

- i. The total assets of NICO are in increasing regularly. The average total assets turnover ratio is 0.17.
- ii. EPS of NICO in 10 years period is fluctuated and highly decrease in FY 2060/61 and 2061/62 which is unfavorable condition of NICO performance of NICO.
- iii. Net profit of NICO fluctuated year to year. There is inverse relationship between gross total income and net profit. The gross total income is in increasing trend but net profit is in decreasing trend so net profit margin also decreases regularly.

His major research findings are:

- i. The liquidity position of NICO is good. Current ratio is higher than standard 2:1.
- ii. The total assets turnover ratio of NICO is fluctuating.
- iii. Fixed Assets Turnover ratio is in increasing trend from FY 2052/53 to 2061'62.
- iv. The net profit to total income ratio is decreasing continuously from base year to last year over the study period except FY 2056/57.

**Manoj K. Gautam**, (2008), in his thesis, "*Financial Performance Analysis of Nepal SBI Bank Ltd in the Framework of Camel*" has the following objectives.

- i. To examine the capital adequacy of the bank.
- ii. To assess the quality of the bank's assets.

- iii. To analyze the efficiency of the bank's management.
- iv. To find out the liquidity position of the bank.

His analysis includes:

- i. The percentage of substandard loan to total loan is in decreasing order. While total loan is in increasing trend, percentage of substandard loan to total loan is in decreasing trend except in the FY 2005.
- ii. The total loan of the bank has gone up throughout the study period whereas the portion of the total past due loan in total loan is fluctuating. The assets quality of the bank is satisfactory.
- iii. Bank has not met the standard of provision for substandard loan to total substandard loan.

His major research findings are:

- i. The percentage of substandard loan to total loan ranges from 3.03% to 0.02% in the study period.
- ii. The ratio of provision for substandard loan to total substandard loan has fluctuated in the study period. 26.12% is the highest percentage made in the FY 2002. In rest of the study period it is less than 25%. Thus, it is found in the analysis of data that the bank has not made adequate provision for substandard loan prescribed by NRB.
- iii. The ratio of provision for doubtful debt to total doubtful debt ranges from maximum of 52.17% to the minimum of 15.64%. It is found that the provision of the bank was not adequate.

**Anjan Bhandari**, (2008), in his thesis, "*Financial Performance Analysis of Himalayan Bank Limited*" has the following objectives.

- i. To evaluate the financial performance of HBL in terms of liquidity, efficiency of assets and cost management.

- ii. To examine the soundness of the profitability and operating efficiency of HBL.
- iii. To evaluate earning generating capacity.

His analysis includes:

- i. Net income of the bank is Rs. 212.13 million in the FY 2002/03 which has reached to 263.05 million in the FY 2003/04. The average ratio of Net income to total deposit is 1.36. It is analyzed that the bank has not mobilized the total deposit to generate income in satisfactory level.
- ii. The return on total assets is in fluctuating trend during the study period.

His major research findings are:

- i. Price earning ratio is good enough for the study period.
- ii. Correlation coefficient between deposit and loan and advances is positive which indicates that increase in deposit will increase in loan and advances.
- iii. It is found that the operating efficiency of the bank is in increasing trend.
- iv. Bank seems to be successful in making investment in profitable sector.

## **CHAPTER – III**

### **RESEARCH METHODOLOGY**

#### **3.1 Concept of Research Methodology**

Research Methodology describes the research design used, the method of data collection, variables and control employed, reliability of instruments selected or constructed and the satisfied tools and procedure used in the analysis. In other words, research methodology describes the methods and process applied in entire aspects of the study.

The basic objective of this study is to evaluate the overall financial performance of the Bank of Kathmandu and to suggest for the improvement of its performance. To achieve the mentioned objectives, an appropriate research methodology has to be allowed. Thus, in this chapter focuses have been made on research design, nature and sources of data and tools used for analysis. Data of the FY 2002/03 to 2007/08 have been presented and analyzed through appropriate financial and statistical tools. With the help of this analysis we can evaluate the performance and financial position of Bank of Kathmandu Ltd.

#### **3.2 Research Design**

The main objective of the study is to analyze, examine and interpret the financial performance of Bank of Kathmandu Ltd by analyzing the financial statements. This study is intensive study based on the analysis of past six year's financial performance of Bank of Kathmandu Ltd.

Research is a theory building activities. Theory is a relationship between two or more facts. The research design refers to the conceptual structure within the research which is conducted. A research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to

the research purpose with the economy in procedure. Thus research design is a plan for the collection and analysis of data. The first step of the study is to collect necessary information and data concerning the study of Bank of Kathmandu Ltd. In this study descriptive research design is used to meet the objective of study. Descriptive research design has been used for clearing the situation on the basis of presented data and facts. The data is carefully studied and analyzed systematically under specific major heading so as to meet the objective. Beside this, the accumulated data is described and tabulated systematically. In this study, Ratio Analysis has been designed to analyze the overall performance. Also, mean, standard deviation, co-efficient of variance, correlation co-efficient are calculated and trend analysis has been presented.

### **3.3 Nature and Sources of Data**

The various data required for the study, but mainly the study is conducted on the basis of secondary data. The sources of secondary Data are the Bank's annual reports, financial statements of the bank. Previous thesis has been taken as other sources of data during the study. The published financial data are mostly used in this study to analyze the overall performance of Bank of Kathmandu Ltd.

This study is mainly based on secondary data which are the annual reports especially from Balance Sheet and Profit & Loss Account published by Bank of Kathmandu Ltd. Thus the sources of data are the published annual reports and data are of secondary nature.

### **3.4 Sampling Size**

Now-a-days, a number of commercial banks have been established in the different parts of the country. Here out of them, Bank of Kathmandu is taken into consideration for the purpose of study using the data of six years from the fiscal year 2002/03 to 2007/08

### **3.5 Data Collection and Processing Procedure**

The secondary data published by Bank of Kathmandu Ltd for different years are collected from the bank. The required financial data and information have been collected from the Balance Sheet and Profit & Loss Account of the bank. The collected secondary data were compiled and processed in order to achieve the objective of the study. The data extracted from annual reports have been processed and interpreted considering the requirement of the study. This study is basically used the secondary data which are collected firstly and tabulated systematically. Simple statistical analysis like percentage are calculated, presented and analyzed in descriptive way. Similarly, the financial ratios and statistical tools are widely used for the analysis and interpretation of the overall performance of Bank of Kathmandu Ltd.

The data are tabulated on the following series:

1. The financial data have been presented according to time series of six years starting from the year.
2. The data are analyzed with the help of financial ratios and statistical tools such as mean, standard deviation, co-efficient of variance and correlation co-efficient.

### **3.6 Analytical Tools**

The tabulated data are analyzed with the help of various fundamental financial and statistical tools. The following financial tools have been used to analyze the data. Statistical tools help to find out the trends of financial position of the bank. It also analyzes the relationship between variables and helps to make appropriate investment policy.

### **3.6.1 Financial Ratios**

Ratio analysis is a powerful tool of financial analysis. In financial analysis, a ratio is used as an index or yardstick for evaluating the financial position and performance of a firm. Ratio helps to summarize the large quantities of financial data and financial performance.

#### **3.6.1.1 Liquidity Ratios**

A firm that intends to remain a viable business entry must have enough cash in hand to pay its bills as they come due. In other words, the firm must remain liquid. One way to determine whether this is a case is to examine the relationship between a firm's current assets and approaching obligations. Liquidity ratios are quick measures of a firm's ability to provide sufficient cash to conduct a business.

##### **a. Current Ratio**

Current Ratio is also known as short term solvency ratio or working capital ratio. This ratio is to assess the short term financial position of a firm. In other words, it is an indicator of firm's ability to meet its short term obligation. Current ratio is calculated by using following formula.

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Current assets are cash and those cash equivalent of business which can be converted into cash within a short period of time not exceeding a year. Current liabilities are those obligations of a firm, which are to be paid within a short period of time not exceeding a year.

In this study current assets include cash, bank balance, money at call, prepaid expenses, loan and advances and miscellaneous assets.

Similarly current liabilities include deposit except fixed deposit, bills payable, sundry creditors, outstanding expenses, provision of taxation.

**b. Cash and Bank Balance to Current Assets**

This ratio measures the proportion of most liquid assets viz. cash and bank balance among the total current assets of the bank. Higher ratio shows the bank's ability to meet its demand for cash. The ratio is computed by dividing cash and bank balance by current assets, presented as under,

$$\text{Cash and Bank Balance to Current Assets Ratio} \times \frac{\text{Cash and Bank Balance}}{\text{Current Assets}}$$

**c. Loan and Advances to Current Assets**

Bank loan and advances are the main assets used as a source of income in the commercial banks. The ratio shows the proportion of current assets, which are invested as loans and advances to generate the income.

It shows the relationship between loan and advances to current assets or it shows the bank's liquidity capacity of discounting and purchasing the bills, and providing loan, overdraft facilitates to customers. Loan and Advances to Current Assets Ratio is expressed as:

$$\text{Loan and Advances to Current Assets Ratio} \times \frac{\text{Loan and Advances}}{\text{Current Assets}}$$

**d. Fixed Deposit to Total Deposit**

Fixed Deposit is the high interest bearing deposit which can be withdrawn only after its maturity. It is calculated by dividing the amount of fixed deposit by the amount of total deposit.

This ratio shows the proportion of fixed deposit in the total deposit. The higher the ratio, the higher the cost of fund for the bank. This is because fixed deposit carries relatively higher interest rate. However the bank can manage its liquidity requirements more precisely. The formula for this ratio is given by,

$$\text{Fixed Deposit to Total Deposit} \times \frac{\text{Fixed Deposit}}{\text{Total Deposit}}$$

#### **e. Saving Deposit to Total Deposit**

Saving deposit is the low interest bearing deposit than the fixed deposit. These deposits are not as freely withdrawal as current deposit. This ratio is calculated in order to find out the proportion of total deposit which is interest bearing and short term. It can be calculated by dividing the amount of saving deposit by the amount of total deposit.

This ratio shows the proportion of saving deposit in the total deposit. The higher the ratio, the higher the liquidity requirements to meet unscheduled withdrawals by the depositors. However, the bank can manage its source of financing with moderate cost. The formula for this ratio is given by:

$$\text{Saving Deposit to Total Deposit} \times \frac{\text{Saving Deposit}}{\text{Total Deposit}}$$

#### **f. Cash and Bank Balances to Total Deposit**

The countries where capital market is not well developed, the cash reserve requirement can be used not only to control the credit of commercial bank but also to influence the investment portfolio of the commercial banks.

Regarding cash reserve, Nepal Rastra Bank has guided to all the commercial banks to maintain at least 5.5% of their deposit as reserve.

Cash and Bank Balances to Total Deposit Ratio reflect the ability of bank's immediate funds to meet their current deposit, margin, call and saving deposit. Higher the ratio shows higher liquidity position and ability to cover the deposits and vice versa.

In this study, cash and bank balance includes total cash in hank and total cash at banks. Similarly, deposit includes all types of deposits.

Cash Reserve Ratio (CRR) is calculated by dividing the cash and bank balance by the amount of total deposit, which is presented as:

$$\text{Cash Reserve Ratio} \times \frac{\text{Cash and Bank Balance}}{\text{Total Deposit}}$$

### **3.6.1.2 Activity Ratios**

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

#### **a. Loan and advances to Total Deposit Ratio**

Commercial banks utilize the outsider's fund for profit generation purpose. Loans and Advances to Total Deposit Ratio shows whether the bank are successful to utilize the outsiders fund i.e. total deposit for the profit generating purpose on the loan and advances or not.

This ratio measures the extent to which the banks are successful to utilize the outsider's fund. It can be calculated by dividing the amount of loan and advances by the amount of total deposit, which is expressed as below:

Loan and Advances to Total Deposit Ratio  $\times \frac{\text{Loan and Advances}}{\text{Total Deposit}}$

### **b. Loan and advances to Fixed Deposit Ratio**

This ratio indicates how much of loan and advances is granted against fixed deposit. Fixed deposit is the higher interest rate payable deposit. Hence, bank must utilize fixed deposit properly. Loan and advances to fixed deposit ratio indicate how properly the fixed deposit is utilized.

This ratio measures how many times the amount is used in loans and advances in comparison to fixed deposit. Fixed deposit is high interest bearing obligation where as loan and advances are the major sources of investment to generate income for the commercial banks.

This ratio is calculated by dividing the amount of loan and advances by fixed deposit which is given below.

Loan and Advances to Fixed Deposit Ratio  $\times \frac{\text{Loan and Advances}}{\text{Fixed Deposit}}$

### **c. Loan and Advances to Saving Deposit Ratio**

Loan and advances to saving deposit indicate about what proportion of saving deposit is employed to loan and advances. Saving deposit is also an interest payable deposit. So, the bank must earn interest from investment to pay the interest on such deposit. Loan and advances to saving deposit measure what proportion of saving deposit is utilized to invest on loan and advances.

This ratio measures how many times the second high interest bearing deposit is utilized for income generating purpose. This ratio can be calculated by dividing the amount of loan and advances by the amount of saving deposit. The formula for calculating loan and advances to saving deposit ratio is given by,

Loan and Advances to Saving Deposit Ratio  $X \frac{\text{Loan and Advances}}{\text{Saving Deposit}}$

### **3.6.1.3 Assets Management Ratios**

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

#### **a. Total Debt to Shareholders' Equity Ratio**

An accounting ratio obtained by dividing total debt to total equity is called debt to equity ratio. This ratio relates all external liabilities to owners recorded claims. It is also known as 'External-Internal Equity Ratio'. It is determined to measure the firm's obligations to creditors in relation to the funds invested by the owners. So it is the great test of the financial strength of the company. The debt equity ratio indicates the relationship between the long term funds provided by creditors and the firm's owners. The total debt refers to the total current liabilities plus the borrowing from other banks. It is commonly used to measure the degree of financial leverage of the firm. The following formula is applied for calculating the total debt to shareholders' equity ratio.

Total Debt to Shareholders' Equity Ratio  $X \frac{\text{Total Debt}}{\text{Shareholders' Equity}}$

#### **b. Total Debt to Total Assets Ratio**

Debt to total assets ratio reflects the financial contribution of outsiders on total assets of the firm. It also measures the financial security of the outsiders. Generally, creditors prefer a low debt ratio and their earnings on the one hand and to maintain their concentrated control over the firm on the others. As this ratio is

like the debt-equity ratio, it gives results similar to the debt-equity ratio in respect of the capital structure of the firm. Higher the debt ratio indicates higher financial risk as well as increasing claims of outsiders in total assets.

Total debt to total assets ratio is the relationship between creditors fund and owners capital. This ratio is calculated by dividing the total debt of the bank by its total assets which is presented below.

$$\text{Total Debt to Total Assets Ratio} = \frac{\text{Total Debt}}{\text{Total Assets}}$$

### **c. Shareholders' Equity to Total Assets Ratio**

Shareholders' equity to total assets ratio indicates the proportion of the assets which is financed from ownership capital of the firm. This ratio also reveals the relationship between shareholders' fund and owners' capital. This ratio shows the share of shareholders' fund on the total assets. It can be calculated as following:

$$\text{Shareholders' Equity to Total Assets Ratio} = \frac{\text{Shareholders' Equity}}{\text{Total Assets}}$$

### **3.6.1.4 Profitability Ratios**

Profit is the difference between total revenues and total expenses. However, profitability is a measure of efficiency and the search for it provides and incentives to achieve efficiency. The profitability of a firm can be measured by its profitability ratios and profitability ratios are those ratios which indicate degree of success in achieving desired profit levels.

#### **a. Interest Earned to Total Assets Ratio**

Interest earning is the major source of commercial banks. This ratio is calculated to find out percentage of the interest earned in comparison to total assets. This ratio shows how much interest has been generated by mobilizing the assets.

Generally, banks earn interest through the provision of loans and advances, overdraft and investment in securities. This ratio is calculated by using following formula.

$$\text{Interest Earned to Total Assets Ratio} \times \frac{\text{Interest Earned}}{\text{Total Assets}}$$

### **b. Net Profit to Total Deposit Ratio**

This ratio measures the degree of net profit earned by using total deposits. In other words, it reveals that the relationship between net profit after tax and the total deposits. This ratio is a mirror of banks overall financial performance as well as its success in profit generation, the reason is that deposits and earning by utilizing it are the main aspects of commercial banks.

The collected deposits are mobilized in investment and loans to get profit. This ratio indicates the percentage of profit earned by using the total deposit. It is calculated by dividing the amount of Net Profit by the amount of Total Deposit which is presented below.

$$\text{Net Profit to Total Deposit Ratio} \times \frac{\text{Net Profit}}{\text{Total Deposit}}$$

### **c. Net Profit to Total Asset Ratio**

This ratio is useful measurement of the profitability of all financial resources invested in the bank's assets. The Return on Assets or Net Profit to Total Asset Ratio is calculated by dividing the amount of Net Profit by the amount of Total Assets. The formula is given below.

$$\text{Net Profit to Total Assets Ratio} \times \frac{\text{Net Profit}}{\text{Total Assets}}$$

#### **d. Net Profit to Net Worth Ratio**

The objective of every bank is to earn more profit. If the banks utilize its equity properly, then only the bank can earn maximum profit. Equity capital is a bank's own capital. The return on capital shows the extent to which a bank is successful to mobilize its equity. It is the measuring rod of the profitability of a bank. A high ratio indicates the success of bank in mobilizing its equity capital and vice-versa. Net Worth or Shareholders' Equity refers to the owner's claim on the assets of the bank. The Return on Equity measures the earning on the owner's investment. This ratio indicates how well the banks have used the resources of the owners. It is calculated by dividing net profit after tax by net worth which is presented below.

$$\text{Net Profit to Net Worth Ratio} = \frac{\text{Net Profit After Tax}}{\text{Net Worth}}$$

#### **e. Net Operating Profit to Total Asset Ratio**

Net operating profit is the profit before interest and taxes. This ratio is useful to measure the profitability ratio before interest and taxes of all financial resources invested in the bank's assets. The following formula is used to calculate the Net Operating Profit to Total Assets Ratio:

$$\text{Net Operating Profit to Total Assets Ratio} = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

#### **f. Net Profit to Risky Asset Ratio**

Risky assets refer to those assets, which are invested in loans and advances and bills purchased and discounted. The ratio is calculated by dividing the amount of net profit by the amount of risky assets which is shown below.

$$\text{Return on Risky Assets} = \frac{\text{Net Profit After Interest \& Taxes}}{\text{Risky Assets}}$$

### **3.6.1.5 Market Based Ratios**

The true owners of any business firms are the common stockholders who invest their fund in the firm because of their expectation of future returns. From the point of view of stockholders the following financial ratios indicate the financial performance of the business firm.

#### **a. Earning Per Share (EPS)**

Earning per share is one of the most widely quoted statistics when there is a discussion of a company's performance. It is the profit after tax figure that is divided by the number of common shares to calculate the value of earning per share. This figure tells us what profit has been earned by the common shareholders for every share held. A company can decide whether to increase or reduce the number of shares on issue. This decision will alter the earning per share.

The EPS represents the amount earned on behalf of each outstanding share of common stock. They are closely watched by investors and consider an important indicator of the firm's success. EPS is calculated by using the following formula.

$$\text{EPS} = \frac{\text{Net Profit After Tax}}{\text{No. of Common Shares Outstanding}}$$

#### **b. Dividend Per Share (DPS)**

The total return to the shareholder over any given time consists of the dividend received plus the growth in the share price. Many shareholders and potential investors pay very close attention to dividend. They look at the absolute dividend per share and for a history of stable but growing payments. Usually shareholders expect a high percentage of dividends and an institution offering a high DPS is regarded as efficient in fulfilling their expectations. This also helps to increase the credibility of the firm.

DPS is calculated to know the proportion of earning distributed to the shareholders for each share. Dividend per share can be calculated by using the following formula.

$$\text{DPS} \times \frac{\text{Earning Paid to Shareholders}}{\text{No. of Common Shares Outstanding}}$$

### **c. Dividend Payout Ratio**

Dividend Payout Ratio expresses the relationship between a firm's earning and cash paid out in dividend. In other words, this ratio shows what proportion of earning is paid out as dividend and how much is retained for the growth of firm. Usually a higher dividend payout ratio is preferred by shareholders although firms have a great need of fund.

This ratio represents the percentage of the profit distributed as dividend and the percentage of retained as revenue and surplus for the growth of the bank.

Dividend Payout Ratio can be calculated by using following formula.

$$\text{Dividend Payout Ratio } \text{fDPR} \times \frac{\text{Dividend Per Share}}{\text{Earning Per Share}} | 100$$

### **3.6.1.6 Income and Expenditure Analysis**

Income and expenditure are the main indicators of the financial performance of any business organization. The income and expenditure statement provides a financial summary of the firm's operating results during the period specified. In this study the analysis of operating income and expenditure has been made as per following details.

- a. Operating Income
- b. Operating Expenses

**3.6.2 Statistical tools** some important statistical tools will be used to achieve the objective of this study. In this study statistical tool such as mean, standard deviation, coefficient of variation, coefficient of correlation and trend analysis will be used.

### 3.6.2.1 Z Score

A study by Altman developed a statistical model that found the financial ratios predicting bankruptcy. In order to analyze the profitability of Bankruptcy score, the calculation has been made by using Altman's model. The calculation is based on the following equation where five financial ratios have been used to predict the Bankruptcy Score.

$$Z \text{ Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

$$X_1 = \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$X_2 = \frac{\text{Retained Earning}}{\text{Total Assets}}$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

$$X_4 = \frac{\text{Total market Vaue of Stock}}{\text{Book Value of Total Debt}}$$

$$X_5 = \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

$X_1$  = Working Capital to Total Assets

$X_2$  = Cumulative Retained Earning to Total Assets

$X_3$  = EBIT to Total Assets

$X_4$  = Market Value of Equity to Book Value of Total Liabilities

$X_5$  = Total Investment to Total Assets

### 3.6.2.2 Mean

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

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

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

$\sum X$  = Summation of the values

N = No. of Observations

**3.6.2.3 Standard deviation:** standard deviation is the most popular and most useful measure of dispersion and gives uniform, correct and stable results. The chief characteristics of Standard deviation is that it is based on mean, which gives uniform and dependable results. Furthermore, Standard Deviation is always a positive number and is superior to the mean deviation.

$$\text{Standard Deviation (s.d.)} = \sqrt{\frac{\sum f_x Z_x^2}{N}}$$

**3.6.2.4 Co-efficient of variation:** The calculated standard deviation gives an absolute measure of dispersion. Hence where the mean value of the variables is not equal, it is not appropriate to compare two pairs of variables based on standard deviation only. The coefficient of variation measures the relative dispersion. Greater the CV the more variable or less consistent, less uniform, less stable and less homogenous the ratio and vice-verse. The coefficient of variation (C.V.) is given by the following formula in the percentage basis:

Coefficient of variation

$$\text{(C.V.)} = \frac{\text{s.d.}}{\bar{X}} \times 100$$

### 3.6.2.5 Measures of Correlation

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

$$\text{Coefficient of Correlation } (r) = \frac{n \sum xy - \sum x \sum y}{\sqrt{n \sum x^2 - (\sum x)^2} \sqrt{n \sum y^2 - (\sum y)^2}}$$

### 3.6.2.6 Trend Analysis

Trend analysis is very useful and commonly applied statistical tool to forecast the future events in quantitative terms on the basis of tendencies in the dependent variables of the past. This analysis takes the historical data as the basis of forecasting.

This method of forecasting the future trend is based on the assumptions that the past tendencies of the variables are repeated in the future. The future trend is forecasted by using the following formula.

$$Y = a + b X$$

Where,

Y = dependent variable

a = arithmetic mean

b = ratio of change

X = independent variable

## **CHAPTER - IV**

### **DATA PRESENTATION AND ANALYSIS**

In this chapter, an attempt has been made to analyze the financial performance of Bank of Kathmandu Ltd for its operational period of six years from FY 2002/03 to 2007/08. The collected data for this study are presented in tabular form and analyzed with the help of financial tools i.e. Ratio Analysis, Income and Expenditure Statement Analysis and Statistical tools such as Z Score, mean, standard deviation, co-efficient of variance and correlation co-efficient.

#### **4.1 Ratio Analysis**

Ratio Analysis is a powerful tool of financial analysis. In financial analysis, a ratio is used as an index or yardstick for evaluating the financial position and performance of a firm. Ratio helps to summarize the large quantities of financial data and to make qualitative judgment about firm's financial performance. Now Oxford intermediate learner's dictionary has defined the term ratio as "The relation between two numbers which shows how much bigger one quantity is than another".

A popular way to analyze the financial statements is to compute ratios. Thus, ratio analysis is a diagnostic tool that helps to identify problem areas and opportunities within a firm.

The basic input to ratio analysis is the balance sheet for the periods to be examined. The study consists of the following ratios to analyze the financial performance of Bank of Kathmandu Ltd.

### 4.1.1 Liquidity Ratios

#### A. Current Ratio

The Current Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.1

**Table 4.1**  
**Current Ratio of Bank of Kathmandu Ltd**

(Rs.in'000)

Fiscal Year	Current Assets	Current Liabilities	Current Ratio
2002/03	5,535,026	4,874,749	1.14
2003/04	6,935,310	6,565,885	1.06
2004/05	7,170,961	6,288,928	1.14
2005/06	8,785,517	8,528,842	1.03
2006/07	11,253,195	10,350,949	1.09
2007/08	14,130,130	12,476,675	1.13
Mean			1.10
Standard Deviation			0.04
CV			3.64%

*Source: Appendix 1*

The above calculated table shows that the current assets of Bank of Kathmandu Ltd has always exceeded the current liabilities for the study period of six years from FY 2002/03 – 2007/08. The bank has the highest current ratio of 1.14 in FY 2002/03 and FY 2004/05 and the lowest current ratio of 1.03 in FY 2005/06 with an average current ratio of 1.10 during the study period. In general terms, the bank has been able to meet its short term obligations. The bank has lowest standard deviation which shows that the bank is able to maintain its ratio in similar level during the study period. Also, the CV shows that the consistency of its current ratio is high.

## B. Cash and Bank Balance to Current Asset Ratio

The cash and bank balance to current assets ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 -2007/08 is presented below in Table 4.2.

**Table 4.2**

### **Cash and Bank Balances to Current Assets Ratio of Bank of Kathmandu Ltd**

(Rs.in'000)

Fiscal Year	Cash & Bank Balance	Current Assets	Ratio in Percentage
2002/03	692,712	5,535,026	12.52
2003/04	782,883	6,935,310	11.29
2004/05	740,520	7,170,961	10.33
2005/06	728,697	8,785,517	8.29
2006/07	1,315,904	11,253,195	11.69
2007/08	1,440,467	14,130,130	10.19
Mean			10.72
SD			1.344
CV			12.54%

*Source: Appendix 2*

The above table shows that cash and bank balance to current assets ratio of the Bank of Kathmandu Ltd differ from maximum of 12.52% in FY 2002/03 to the minimum of 8.29% in the FY 2005/06 with an average of 10.72% during the study period of six years. The analysis shows the fluctuating trend of ratios which means decreasing and increasing trend of ratios in study period. The standard deviation of cash and bank balance to current assets ratio of Bank of Kathmandu Ltd is 1.344. There is no more deviation. But the CV of cash and bank balance to current assets is more than current assets to current liabilities.

### C. Loan and Advances to Current Asset Ratio

The loan and advances to Current Assets Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.3.

**Table 4.3**

#### **Loan and Advances to Current Assets Ratio of Bank of Kathmandu Ltd.**

(Rs.in'000)

Fiscal Year	Loan and Advances	Current Assets	Ratio in Percentage
2002/03	4,542,700	5,535,026	82.07
2003/04	5,646,698	6,935,310	81.42
2004/05	5,912,579	7,170,961	82.45
2005/06	7,259,083	8,785,517	82.63
2006/07	9,399,328	11,253,195	83.53
2007/08	12,462,638	14,130,130	88.20
Mean			83.38
SD			2.245
CV			2.69%

*Source: Appendix 3*

The above table shows that loan and advances to current assets ratio of the bank varies from maximum of 88.20% in FY 2007/03 to the minimum of 81.42% in the FY 2003/04 with an average of 83.38% during the study period of six years. The analysis indicates that the disbursement of loan and advances with respect to current assets is in increasing trend from the FY 2002/03 during the study period. The standard deviation of Loan and Advances to Current Assets of Bank of Kathmandu Ltd is 2.245. The CV of Loan and Advances to Current Assets of Bank of Kathmandu Ltd is 2.69%. It is less and it shows the more uniformity and consistency of the ratio.

#### **D. Fixed Deposit to Total Deposit Ratio**

The Fixed Deposit to Total Deposit of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.4

**Table 4.4**

#### **Fixed Deposit to Total Deposit Ratio of Bank of Kathmandu Ltd.**

(Rs.in'000)

Fiscal Year	Fixed Deposit	Total Deposit	Ratio in Percentage
2002/03	1,990,935	6,170,711	32.26
2003/04	2,279,713	7,741,645	29.45
2004/05	2,878,868	8,975,781	32.07
2005/06	2,709,754	10,485,359	25.84
2006/07	3,037,171	12,388,927	24.52
2007/08	3,703,176	15,833,738	23.39
Mean			27.92
SD			3.531
CV			12.65%

*Source: Appendix 4*

The above table shows that the ratio of fixed deposit to total deposits of Bank of Kathmandu Ltd differs from maximum of 32.26% in the FY 2002/03 to the minimum of 23.39% in the FY2007/08 with an average of 27.92% during the study period of six years. The analysis indicates that the share of fixed deposit in the total deposit is fluctuating. The standard deviation of Fixed Deposit to Total Deposit of Bank of Kathmandu Ltd is 3.531. The CV of Fixed Deposit to Total Deposit of Bank of Kathmandu Ltd is 12.65%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

### E. Saving Deposit to Total Deposit Ratio

The saving deposit to total deposit ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 to FY 2007/08 is presented below in Table 4.5

**Table 4.5**  
**Saving Deposit to Total Deposit Ratio of Bank of Kathmandu Ltd.**

(Rs.in'000)

Fiscal Year	Saving Deposit	Total Deposit	Ratio in Percentage
2002/03	2,268,548	6,170,711	36.76
2003/04	2,873,809	7,741,645	37.12
2004/05	3,447,445	8,975,781	38.41
2005/06	4,581,964	10,485,359	43.70
2006/07	5,527,292	12,388,927	44.61
2007/08	6,596,110	15,833,738	41.66
Mean			40.38
SD			3.114
CV			7.71%

*Source: Appendix 5*

The above table shows that the saving deposit to total deposit ratio of Bank of Kathmandu Ltd differ from the maximum of 44.61% in the FY 2006/07 to the minimum of 36.76% in the FY 2002/03 with an average of 40.38% during the study period. The analysis indicates that the share of saving deposit to the total deposit is in rising order. The standard deviation of Saving Deposit to Total Deposit Ratio of Bank of Kathmandu Ltd is 3.114. The CV of Saving Deposit to Total Deposit of Bank of Kathmandu Ltd is 7.71%. It is less and it shows the more uniformity and consistency of the ratio.

## F. Cash and Bank Balances to Total Deposit Ratio (Cash Reserve Ratio)

The Cash Reserve Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.6

**Table 4.6**  
**Cash Reserve Ratio of Bank of Kathmandu Ltd.**

(Rs.in'000)

Fiscal Year	Cash & Bank Balances	Total Deposit	Ratio in Percentage
2002/03	692,712	6,170,711	11.23
2003/04	782,883	7,741,645	10.11
2004/05	740,520	8,975,781	8.25
2005/06	728,697	10,485,359	6.95
2006/07	1,315,904	12,388,927	10.62
2007/08	1,440,467	15,833,738	9.10
Mean			9.38
SD			1.458
CV			15.54%

*Source: Appendix 6*

The above calculated table shows that the Cash Reserve Ratio of Bank of Kathmandu Ltd differ from the maximum of 10.62% in the FY 2006/07 to the minimum of 6.95% in the FY 2005/06 with an average of 9.38% during the study period. The scrutiny specifies that the bank has accomplished to maintain cash reserve ratio as per the directives of Nepal Rastra Bank. The standard deviation of Cash Reserve Ratio of Bank of Kathmandu Ltd is 1.458. The CV of Cash and Bank Balances to Total Deposit of Bank of Kathmandu Ltd is 15.54%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

#### 4.1.2 Activity Ratio (Turnover Ratio)

##### A. Loan and Advances to Total Deposit Ratio

The loan and advances to total deposit Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.7.

**Table – 4.7**

##### **Loan and Advances to Total Deposit Ratio**

(Rs.in'000)

Fiscal Year	Loan & Advances	Total Deposit	Ratio in Time
2002/03	4,542,700	6,170,711	0.74
2003/04	5,646,698	7,741,645	0.73
2004/05	5,912,579	8,975,781	0.66
2005/06	7,259,083	10,485,359	0.69
2006/07	9,399,328	12,388,927	0.76
2007/08	12,462,638	15,833,738	0.79
Mean			0.73
Standard Deviation			0.043
CV			5.89%

*Source: Appendix 7*

The above calculated table shows that loans and advances to total deposit of Bank of Kathmandu Ltd fluctuates from maximum of 0.79 times in the FY 2007/08 to the minimum of 0.66 times in the FY 2004/05 with an average of 0.73 times during the study period of six years. The analysis designates that the bank is mobilizing its total deposits in loans and advances adequately and it has efficiently utilized its total deposits for loan and advances purpose. The standard deviation of Loan and Advances to Total Deposit of Bank of Kathmandu Ltd is 0.043. The CV of Loan and Advances to Total Deposit of Bank of Kathmandu Ltd is 5.89 %. It is less and it shows the more uniformity and consistency of the ratio.

## B. Loan and Advances to Fixed Deposit Ratio

The loan and advances to Fixed Deposit Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.8

**Table 4.8**

### **Loan and Advances to Fixed Deposit Ratio**

(Rs.in'000)

Fiscal Year	Loan & Advances	Fixed Deposit	Ratio in Time
2002/03	4,542,700	1,990,935	2.28
2003/04	5,646,698	2,279,713	2.48
2004/05	5,912,579	2,878,868	2.05
2005/06	7,259,083	2,709,754	2.68
2006/07	9,399,328	3,037,171	3.09
2007/08	12,462,638	3,703,176	3.37
Mean			2.66
Standard Deviation			0.454
CV			17.07%

*Source: Appendix 8*

The above calculated table shows that the loan and advances to fixed deposit of Bank of Kathmandu Ltd varies from maximum of 3.77 times in the FY 2007/08 and the minimum of 2.05 times in the FY 2004/05 with an average of 2.66 times during the study period of six years. The scrutiny indicates that the involvement of fixed deposit to loan and advances is more or less constant. The standard deviation of Loan and Advances to Fixed Deposit of Bank of Kathmandu Ltd is 0.054. The CV of Loan and Advances to Fixed Deposit of Bank of Kathmandu Ltd is 17.07%. It is moderate. So the ratio is satisfactory.

### C. Loan and Advances to Saving Deposit Ratio

The loan and advances to saving deposit ratio of Bank of Kathmandu Ltd for the period of FY 2002/2003 – 2007/08 is presented below in Table 4.9

**Table 4.9**  
**Loan and Advances to Saving Deposit Ratio**

(Rs.in'000)

Fiscal Year	Loan & Advances	Saving Deposit	Ratio in Time
2002/03	4,542,700	2,268,548	2.00
2003/04	5,646,698	2,873,809	1.96
2004/05	5,912,579	3,447,445	1.72
2005/06	7,259,083	4,581,964	1.58
2006/07	9,399,328	5,527,292	1.70
2007/08	12,462,638	6,596,110	1.89
Mean			1.81
Standard Deviation			0.152
CV			8.40%

*Source: Appendix 9*

The above calculated table shows that loan and advances to saving deposit of the Bank of Kathmandu Ltd fluctuates from maximum of 2.00 times in the FY 2002/03 and the minimum of 1.58 times in the FY 2005/06 with an average of 1.81 times during the study period of six years. The analysis designates that the contribution of saving deposits to loan and advances is in fluctuating trend but in satisfactory level. The standard deviation of Loan and Advances to Saving Deposit of Bank of Kathmandu Ltd is 0.0152. The CV of Loan and Advances to Saving Deposit of Bank of Kathmandu Ltd is 8.40%. It is less and it shows the more uniformity and consistency of the ratio.

### 4.1.3 Leverage Management Ratios

#### A. Total Debt to Shareholders' Equity Ratio

The total debt to shareholders' equity ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.10

**Table 4.10**  
**Total Debt to Shareholders' Equity Ratio**

(Rs.in'000)

Fiscal Year	Total Debt	Shareholders' Equity	Ratio in Time
2002/03	5,929,952	463,581	12.79
2003/04	7,847,709	463,581	16.93
2004/05	7,865,159	720,738	10.91
2005/06	9,531,691	839,734	11.35
2006/07	13,421,945	981,978	13.67
2007/08	14,287,513	1,342,073	10.65
Mean			12.72
SD			2.163
CV			17.00%

*Source: Appendix 10*

The above calculated table shows that Debt to Equity Ratio of Bank of Kathmandu Ltd differs from maximum of 16.93 times in the FY 2003/04 to the minimum of 10.65 times in the FY 2007/08 with an average of 12.72 times during the study period of six years. The analysis indicates that the bank has the high debt ratio, which means the creditors have invested more in the bank than the owners. The standard deviation of Total Debt to Shareholders' Equity of Bank of Kathmandu Ltd is 2.163. The CV of Total Debt to Shareholders' Equity of Bank of Kathmandu Ltd is 17.00%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

## B. Total Debt to Total Assets Ratio

The total debt to total asset ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 -2007/08 is presented below in Table 4.11.

**Table 4.11**  
**Total Debt to Total Assets Ratio**

(Rs.in'000)

Fiscal Year	Total Debt	Total Assets	Ratio in Percentage
2002/03	5,929,952	7,444,817	79.85
2003/04	7,847,709	9,496,345	82.64
2004/05	7,865,159	9,888,533	79.54
2005/06	9,531,691	12,278,329	77.60
2006/07	13,421,945	14,570,099	92.12
2007/08	14,287,513	17,721,925	80.62
Mean			82.06
SD			4.739
CV			5.78%

*Source: Appendix 11*

The above calculated table shows that debt to total assets of Bank of Kathmandu Ltd differ from maximum of 92.12% in the FY 2006/07 to the minimum of 77.60% in the FY 2005/06 with an average of 82.06% during the study period of six years. This analysis indicates that the bank has the high debt-equity ratio, which means creditors have invested more in the bank than owners. So this shows the role of creditors in the bank is higher than the owners. The standard deviation of Total Debt to Total Assets of Bank of Kathmandu Ltd is 4.739. Low CV shows the more uniformity and consistency of the ratio.

### C. Shareholders' Equity to Total Assets Ratio

The Shareholders' Equity to Total Assets Ratio of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.12.

**Table 4.12**  
**Shareholders' Equity to Total Assets Ratio**

(Rs.in'000)

Fiscal Year	Shareholders' Equity	Total Assets	Ratio in Percentage
2002/03	463,581	7,444,817	6.23
2003/04	463,581	9,496,345	4.88
2004/05	720,738	9,888,533	7.29
2005/06	839,734	12,278,329	6.84
2006/07	981,978	14,570,099	6.74
2007/08	1,342,073	17,721,925	7.57
Mean			6.59
SD			0.875
CV			13.28%

*Source: Appendix 12*

The above calculated table shows that the total shareholders' equity to total assets of the Bank of Kathmandu Ltd varies from maximum of 7.57% in the FY 2007/08 to the minimum of 6.23% in the FY 2002/03 with an average of 6.59% during the study period of six years. The above analysis indicates that an average of 6.59% of total assets of the bank is financed through Equity Capital and the rest from Debt Capital. The standard deviation of Shareholders' Equity to Total Assets of Bank of Kathmandu Ltd is 0.875. The CV of Shareholders' Equity to Total Assets of Bank of Kathmandu Ltd is 13.28%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

#### 4.1.4 Profitability Ratio

##### A. Interest Earned to Total Assets Ratio

Interest Earned to Total Assets Ratio of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.13.

**Table 4.13**  
**Interest Earned to Total Assets Ratio**

(Rs.in'000)

Fiscal Year	Interest Earned	Total Assets	Ratio in Percentage
2002/03	434,033	7,444,817	5.83
2003/04	469,505	9,496,345	4.94
2004/05	607,096	9,888,533	6.14
2005/06	718,121	12,278,329	5.85
2006/07	819,004	14,570,099	5.62
2007/08	1,034,158	17,721,925	5.84
Mean			5.70
SD			0.373
CV			6.54%

*Source: Appendix 13*

The above calculated table shows that interest earned to total assets of the Bank of Kathmandu Ltd differ from maximum of 6.14% in the FY 2004/05 to the minimum of 4.94% in the FY 2003/04 with an average of 6.20% during the study period of six years. This analysis indicates that the total assets are not more fluctuating during the study period. The standard deviation of Interest Earned to Total Assets of Bank of Kathmandu Ltd is 0.373. The CV of Interest Earned to Total Assets of Bank of Kathmandu Ltd is 6.54%. It is low and it shows the more uniformity and consistency of the ratio.

##### B. Net Profit to Total Deposit Ratio

The Net Profit to Total Deposit Ratio of Bank of Kathmandu Ltd for the period of 2002/03 – 2007/08 is presented below in Table 4.14.

**Table 4.14**  
**Interest Earned to Total Deposit Ratio**

(Rs.in'000)

Fiscal Year	Net Profit	Total Deposit	Ratio in Percentage
2002/03	82,128	6,170,711	1.33
2003/04	127,473	7,741,645	1.65
2004/05	139,530	8,975,781	1.55
2005/06	202,441	10,485,359	1.93
2006/07	262,387	12,388,927	2.12
2007/08	361,497	15,833,738	2.28
Mean			1.81
SD			0.33
CV			18.23%

*Source: Appendix 14*

The above table shows that Net Profit to Total Deposit of Bank of Kathmandu Ltd varies from maximum of 2.28% in the FY 2007/08 to the minimum of 1.33% in the FY 2002/03 with an average of 1.81% during the study period of six years. This analysis indicates that the Net Profit earned in comparison to the total deposit is in increasing trend. In general, it reveals that the bank is mobilizing funds effectively and efficiently. The standard deviation of Net Profit After Tax to Loan and Advances of Bank of Kathmandu Ltd is 0.33. The CV of Net Profit After Tax to Loan and Advances of Bank of Kathmandu Ltd is 18.23%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

### **C. Net Profit to Total Assets Ratio**

The Net Profit to Total Assets Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.15.

**Table 4.15**  
**Net Profit to Total Assets Ratio**

(Rs.in'000)

Fiscal Year	Net Profit	Total Assets	Ratio in Percentage
2002/03	82,128	7,444,817	1.10
2003/04	127,473	9,496,345	1.34
2004/05	139,530	9,888,533	1.41
2005/06	202,441	12,278,329	1.65
2006/07	262,387	14,570,099	1.80
2007/08	361,497	17,721,925	2.04
Mean			1.56
SD			0.311
CV			13.94%

*Source: Appendix 15*

The above calculated table shows that Net Profit to Total Assets of Bank of Kathmandu Ltd differ from maximum of 2.04% in the FY 2007/08 to the minimum of 1.10% in the FY 2002/03 with an average of 1.56% during the study period of six years. This analysis indicates that Net Profit of a Bank is in increasing trend. It shows that the bank has utilized its total assets effectively to generate income. The standard deviation of Net Profit to Total Assets of Bank of Kathmandu Ltd is 0.311. The CV of Net Profit After Tax to Loan and Advances of Bank of Kathmandu Ltd is 13.94%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

#### **D. Net Profit to Net Worth Ratio (Return On Equity)**

The Net Profit to Net Worth Ratio of Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.16.

**Table 4.16**  
**Net Profit to Net Worth Ratio**

(Rs.in'000)

Fiscal Year	Net Profit After Tax	Net Worth	Ratio in Percentage
2002/03	82,128	892,486	9.20
2003/04	127,473	1,012,368	12.59
2004/05	139,530	990,209	14.09
2005/06	202,441	1,069,342	18.93
2006/07	262,387	993,253	26.42
2007/08	361,497	1,342,050	26.94
Mean			18.03
SD			6.754
CV			37.46%

*Source: Appendix 16*

The above calculated table shows that Return on Equity of the Bank of Kathmandu Ltd varies from maximum of 26.94% in the FY 2007/08 to the minimum of 9.20% in the FY 2002/03 with an average of 18.03% during the study period of six years. The analysis indicates that the profit earning in relation with shareholders' equity of Bank of Kathmandu Ltd is relatively good, which exhibits the better utilization of shareholders' fund. The standard deviation of Net Profit to Net Worth of Bank of Kathmandu Ltd is 6.754. The CV of Net Profit to Net Worth of Bank of Kathmandu Ltd is 37.46%. It is more and more CV shows the less uniformity and consistency of the ratio.

#### **E. Net Operating Profit to Total Assets Ratio**

The Net Operating Profit to Total Asset Ratio of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.17.

**Table 4.17**  
**Net Operating Profit to Total Assets Ratio**

(Rs.in'000)

Fiscal Year	Net Profit Before Tax	Total Assets	Ratio in Percentage
2002/03	122,142	7,444,817	1.64
2003/04	184,645	9,496,345	1.94
2004/05	204,293	9,888,533	2.07
2005/06	301,208	12,278,329	2.45
2006/07	421,715	14,570,099	2.89
2007/08	527,899	17,721,925	2.98
Mean			2.33
SD			0.491
CV			21.07%

*Source: Appendix 17*

The above calculated table shows that Net Operating Profit to Total Assets of the Bank of Kathmandu Ltd differ from maximum of 2.98 % in the FY 2007/08 to the minimum of 1.64% in the FY 2002/03 with an average of 2.33% during the study period of six years. The analysis indicates that the net operating profit, earned in comparison to total assets is in increasing trend. The standard deviation of Net Operating Profit to Total Assets of Bank of Kathmandu Ltd is 0.491. The CV of Net Operating Profit to Total Assets of Bank of Kathmandu Ltd is 21.07%. It is more and more CV shows the less uniformity and consistency of the ratio.

## F. Net Profit to Risky Assets Ratio

The Net Profit to Risky Assets Ratio of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table – 4.18.

**Table – 4.18**

### **Return on Risky Assets Ratio**

(Rs.in'000)

Fiscal Year	Net Profit After Tax	Loan and Advances	Ratio in Percentage
2002/03	82,128	4,542,700	1.81
2003/04	127,473	5,646,698	2.26
2004/05	139,530	5,912,579	2.36
2005/06	202,441	7,259,083	2.79
2006/07	262,387	9,399,328	2.79
2007/08	361,497	12,462,638	2.90
Mean			2.49
SD			0.383
CV			15.38%

*Source: Appendix 18*

The above calculated table shows that Return on Risky Assets of the Bank of Kathmandu Ltd differ from maximum of 2.90% in the FY 2007/08 to the minimum of 1.81% in the FY 2002/03 with an average of 2.49% during the study period of six years. This analysis indicates that profit made from risky assets i.e. loan and advances is in increasing trend. The standard deviation of Net Profit to Risky Assets of Bank of Kathmandu Ltd is 0.383. The CV of Net Profit After Tax to Loan and Advances of Bank of Kathmandu Ltd is 15.38%. It is moderate and it shows the satisfactory uniformity and consistency of the ratio.

#### 4.1.5 Market Based Ratios

##### A. Earning Per Share (EPS)

The Earning Per Share (EPS) of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table – 4.19.

**Table 4.19**  
**Earning Per Share**

(Rs.in'000)

Fiscal Year	Net Profit After Tax	No. of Share Outstanding	EPS (in Rs.)
2002/03	82,128	4,636	17.72
2003/04	127,473	4,636	27.50
2004/05	139,530	4,636	30.10
2005/06	202,441	4,636	43.67
2006/07	262,387	6,031	43.50
2007/08	361,497	6,031	59.94
Mean			37.07
SD			13.678
CV			36.90

*Source: Appendix 19*

The above calculated table shows that EPS of the Bank of Kathmandu Ltd varies from maximum of Rs. 59.94 in the FY 2007/08 to the minimum of Rs. 17.72 in the FY 2002/03 with an average of Rs. 37.07 during the study period of six years. The above analysis indicates that the EPS of the Bank of Kathmandu Ltd is quite good in overall years. The standard deviation of Earning Per Share of Bank of Kathmandu Ltd is 13.678. The CV of Earning Per Share of Bank of Kathmandu Ltd is 36.90. It is more and more CV shows the less uniformity and consistency of the ratio.

## B. Dividend per Share (DPS)

The Dividend Per Share (DPS) of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.20.

**Table 4.20**  
**Dividend Per Share**

(Rs.in'000)

Fiscal Year	Earning Paid to Shareholders	No. of Shares Outstanding	DPS (in Rs.)
2002/03	23,179	4,636	5.00
2003/04	46,358	4,636	10.00
2004/05	69,537	4,636	15.00
2005/06	222,519	4,636	48.00
2006/07	120,628	6,031	20.00
2007/08	253,954	6,031	42.11
Mean			23.35
SD			16.101
CV			68.96%

*Source: Appendix 20*

The above calculated table shows that DPS of the Bank of Kathmandu Ltd is differ from maximum of Rs. 48.00 in the FY 2005/06 to the minimum of Rs. 5.00 in the FY 2002/03 with an average of Rs. 23.35 during the study period of six years. Dividend Per Share of the Bank of Kathmandu Ltd is not satisfactory till the FY 2004/05 but after that is satisfactory. The standard deviation of Dividend Per Share of Bank of Kathmandu Ltd is 16.101. The CV of Dividend Per Share of Bank of Kathmandu Ltd is 68.96%. It is more and more CV shows the less uniformity and consistency of the ratio.

### C. Dividend Payout Ratio (DPR)

The Dividend Payout Ratio of the Bank of Kathmandu Ltd for the period of FY 2002/03 – 2007/08 is presented below in Table 4.21.

**Table 4.21**  
**Dividend Payout Ratio**

(Rs.in'000)

Fiscal Year	DPS (in Rs.)	EPS (in Rs.)	Dividend Payout Ratio
2002/03	5.00	17.72	28.22
2003/04	10.00	27.50	36.36
2004/05	15.00	30.10	49.83
2005/06	48.00	43.67	109.92
2006/07	20.00	43.50	45.98
2007/08	42.11	59.94	70.25
Mean			56.76
SD			27.089
CV			47.73%

*Source: Appendix 21*

The above calculated table shows that Dividend Payout Ratio of the Bank of Kathmandu Ltd varies from maximum of Rs. 109.92 in the FY 2005/06 to the minimum of Rs. 28.22 in the FY 2002/03 with average of Rs. 56.76 during the study period of six years. The above analysis indicates the irregular dividend payout ratio of the bank. The standard deviation of Dividend Payout Ratio of Bank of Kathmandu Ltd is 27.089. The CV of Dividend Payout Ratio of Bank of Kathmandu Ltd is 47.73%. It is more and more CV shows the less uniformity and consistency of the ratio.

#### 4.1.6 Income and Expenditure Analysis

Income and Expenditure are the main indicators of the financial performance of any business organization. The income and expenditure statement provides a financial summary of the firm's operating results during the period specified. So, the attempts have been made to analyze the income and expenditure statement of Bank of Kathmandu Ltd to evaluate the financial performance of the bank. In this study the analysis of operating income and expenditure has been made as per following details.

##### 4.6.1 Operating Income

The operating income refers to the income received from different sources like Rent of self Deposit Vault, Issue and Renew of Credit Card and Renew of ATM Card, Telex, T.T., Commission & Discount, Service charge etc.

Total Operating Income of the Bank of Kathmandu Ltd from FY 2002/03 – 2007/08 is presented below in Table 4.22.

**Table 4.22**  
**Total Operating Income**

*(Rs.in'000)*

Fiscal Year	Operating Income
2002/03	341,841
2003/04	439,979
2004/05	514,390
2005/06	576,665
2006/07	677,081
2007/08	862,963
Mean	568,819

*Source: Annual Report of Bank of Kathmandu Ltd*

The above table shows that the operating income of the Bank of Kathmandu Ltd is in increasing trend from the FY 2002/03 – 2007/08. It shows that the bank is in progressive stage.

#### 4.6.2 Operating Expenses

The expenditure heads of the Bank are Interest expenses, Personnel expenses and Other Operating expenses.

The interest heading is one of the main expenses of the bank. The interest expenses are interest paid to depositors, loan and advances, short term borrowing etc. Office operating expenses includes rent, legal charges, stationery, repair and maintenance of fixed assets etc. Personnel expenses includes Salary, Bonus, Gratuity, Provident Fund and Allowances paid to staff of the bank.

Interest expenses, Personnel expenses and Operating expenses of the Bank of Kathmandu Ltd from FY 2002/03 – 2007/08 is presented below in Table – 4.23.

**Table 4.23**  
**Operating Expenses**

*(Rs.in'000)*

Fiscal Year	Interest Expenses	Personnel Expenses	Operating Expenses	Total
2002/03	276,705	51,682	71,834	400,221
2003/04	286,297	47,726	85,829	419,852
2004/05	241,639	53,822	99,190	394,651
2005/06	308,156	59,120	117,591	484,867
2006/07	339,181	69,740	138,430	547,351
2007/08	417,543	90,602	170,481	678,626
Mean	311,587	62,115	62,115	487,594

*Source: Annual Report of Bank of Kathmandu Ltd.*

## 4.2 Statistical Tool

### 4.2.1 Z Score

A study by Altman developed a statistical model that found the financial ratios predicting Bankruptcy. The Z score has been calculated and analyzed on the basis of relevant information of the Bank of Kathmandu Ltd for the period of six years.

The calculation is based on following equation where five financial ratios have been used to predict the bankruptcy of the Bank of Kathmandu Ltd.

$$\mathbf{Z\ Score = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5}$$

$$X_1 = \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$X_2 = \frac{\text{Retained Earning}}{\text{Total Assets}}$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

$$X_4 = \frac{\text{Total market Vaue of Stock}}{\text{Book Value of Total Debt}}$$

$$X_5 = \frac{\text{Total Investment}}{\text{Total Assets}}$$

Altman's Bankruptcy Score criteria have been presented in Table-24 as below.

**Table 4.24**  
**Criteria to analyze the Z score**

Less than 1.81	Between 1.81 – 2.99	Greater than 2.99
Probability of Failure High	Probability of failure difficult to determine	Probability of failure remote
Predict Failure	Predict failure if score is less than 2.675 Predict success if score is more than 2.675	Predict Success

The above bankruptcy criteria signifies that a firm with a score less than 1.81 is likely to fail and will go into bankruptcy. Similarly, a firm with a score greater than 2.99 will never go into bankruptcy that is of a very rare chance of bankruptcy. However, the score between 1.81 and 2.99 puts the analyst in a difficult situation to predict whether the firm will exist or not.

With the available data and for latest prediction the profitability of bankruptcy of Bank of Kathmandu Ltd has been calculated and analyzed for six fiscal years.

### 1. Calculation of Z Score of the Bank of Kathmandu Ltd. (FY 2002/03)

$$Z \text{ Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

Where,

$$X_1 = X \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$\begin{aligned} \text{Net Working Capital} &= \text{Total Current Assets} - \text{Total Current Liabilities} \\ &= \text{Rs. } 5,535,026 - \text{Rs. } 4,874,749 \\ &= \text{Rs. } 660,277 \end{aligned}$$

$$\begin{aligned} \text{Total Assets} &= \text{Rs. } 7,444,817 \\ \text{So, } X_1 &= \text{Rs. } 660,277 / \text{Rs. } 7,444,817 \\ &= 0.0887 \end{aligned}$$

$$X_2 = X \frac{\text{Retained Earning}}{\text{Total Assets}}$$

Where,

$$\begin{aligned} \text{Retained Earning} &= \text{Rs. } 8,860 \\ \text{Total Assets} &= \text{Rs. } 7,444,817 \\ \text{So, } X_2 &= \text{Rs. } 8,860 / \text{Rs. } 7,444,817 \\ &= 0.0012 \end{aligned}$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

Where,

$$\begin{aligned} \text{EBIT} &= \text{Net Profit before Interest \& Taxes} + \text{Interest Expense} \\ &= \text{Rs. } 122,142 + \text{Rs. } 276,705 \\ &= \text{Rs. } 398,847 \end{aligned}$$

$$\text{Total Assets} = \text{Rs. } 7,444,817$$

$$\begin{aligned} \text{So, } X_3 &= \text{Rs. } 398,847 / \text{Rs. } 7,444,817 \\ &= 0.0536 \end{aligned}$$

$$X_4 = \frac{\text{Total market Vaue of Stock}}{\text{Book Value of Total Debt}}$$

Where,

$$\begin{aligned} \text{Total Market Value of Stock} &= \text{MPS} \times \text{No. of Outstanding Shares} \\ &= \text{Rs. } 198 \times 4,635,809 \\ &= \text{Rs. } 917,890,182 \end{aligned}$$

$$\text{Total Book Value of Debt} = \text{Rs. } 5,929,952,000$$

$$\begin{aligned} \text{So, } X_4 &= \text{Rs. } 917,890,182 / \text{Rs. } 917,890,182 \\ &= 0.1548 \end{aligned}$$

$$X_5 = \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

$$\text{Total Investment} = \text{Rs. } 6,358,849$$

$$\text{Total Assets} = \text{Rs. } 7,444,817$$

$$\begin{aligned} \text{So, } X_5 &= \text{Rs. } 6,358,849 / \text{Rs. } 7,444,817 \\ &= 0.8541 \end{aligned}$$

Now, Substitute the values of these variables in the given equation, we acquire the Z Score of the Bank of Kathmandu Ltd as follows:

$$\begin{aligned} \text{Z Score} &= 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5 \\ &= (1.2 \times 0.0887) + (1.4 \times 0.0012) + (3.3 \times 0.0536) + (0.6 \times 0.1548) + \\ &\quad (0.999 \times 0.8541) \end{aligned}$$

$$= 0.1064 + 0.0017 + 0.1769 + 0.0929 + 0.8532$$

$$= 1.23$$

The Z Score of Bank of Kathmandu Ltd for the FY 2002/03 is 1.23. Since it is less than 1.81, it would have probability of failure high.

## 2. Calculation of Z Score of the Bank of Kathmandu Ltd. (FY 2003/04)

$$Z \text{ Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

Where,

$$X_1 = \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

Net Working Capital = Total Current Assets – Total Current Liabilities

$$= \text{Rs. } 6,935,310 - \text{Rs. } 6,565,885$$

$$= \text{Rs. } 369,425$$

$$\text{Total Assets} = \text{Rs. } 9,496,345$$

$$\text{So, } X_1 = \text{Rs. } 369,425 / \text{Rs. } 9,496,345$$

$$= 0.0389$$

$$X_2 = \frac{\text{Retained Earning}}{\text{Total Assets}}$$

Where,

$$\text{Retained Earning} = \text{Rs. } 6,492$$

$$\text{Total Assets} = \text{Rs. } 9,496,345$$

$$\text{So, } X_2 = \text{Rs. } 6,492 / \text{Rs. } 9,496,345$$

$$= 0.0007$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

Where,

$$\text{EBIT} = \text{Net Profit before Interest \& Taxes} + \text{Interest Expense}$$

$$= \text{Rs. } 184,645 + \text{Rs. } 286,297$$

$$= \text{Rs. } 470,942$$

$$\begin{aligned} \text{Total Assets} &= \text{Rs. } 9,496,345 \\ \text{So, } X_3 &= \text{Rs. } 470,942 / \text{Rs. } 9,496,345 \\ &= 0.0496 \end{aligned}$$

$$X_4 \times \frac{\text{Total market Vaue of Stock}}{\text{Book Value of Total Debt}}$$

Where,

$$\begin{aligned} \text{Total Market Value of Stock} &= \text{MPS} \times \text{No. of Outstanding Shares} \\ &= \text{Rs. } 295 \times 4,635,809 \\ &= \text{Rs. } 1,367,563,655 \end{aligned}$$

$$\begin{aligned} \text{Total Book Value of Debt} &= \text{Rs. } 7,847,709,000 \\ \text{So, } X_4 &= \text{Rs. } 1,367,563,655 / \text{Rs. } 7,847,709,000 \\ &= 0.1743 \end{aligned}$$

$$X_5 \times \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

$$\begin{aligned} \text{Total Investment} &= \text{Rs. } 8,124,108 \\ \text{Total Assets} &= \text{Rs. } 9,496,345 \\ \text{So, } X_5 &= \text{Rs. } 8,124,108 / \text{Rs. } 9,496,345 \\ &= 0.8555 \end{aligned}$$

Now, Substitute the values of these variables in the given equation, we acquire the Z Score of the Bank of Kathmandu Ltd as follows:

$$\begin{aligned} \text{Z Score} &= 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5 \\ &= (1.2 \times 0.0389) + (1.4 \times 0.0007) + (3.3 \times 0.0496) + (0.6 \times 0.1743) + (0.999 \\ &\times 0.8555) \\ &= 0.0467 + 0.0010 + 0.1637 + 0.1046 + 0.8546 \\ &= 1.17 \end{aligned}$$

The Z Score of Bank of Kathmandu Ltd for the FY 2003/04 is 1.17. Since it is less than 1.81, it would have probability of failure high.

### 3. Calculation of Z Score of the Bank of Kathmandu Ltd. (FY 2004/05)

$$\text{Bankruptcy Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

Where,

$$X_1 = \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$\text{Net Working Capital} = \text{Total Current Assets} - \text{Total Current Liabilities}$$

$$= \text{Rs. } 7,170,961 - \text{Rs. } 6,288,928$$

$$= \text{Rs. } 882,033$$

$$\text{Total Assets} = \text{Rs. } 9,888,533$$

$$\text{So, } X_1 = \text{Rs. } 882,033 / \text{Rs. } 9,888,533$$

$$= 0.0892$$

$$X_2 = \frac{\text{Retained Earning}}{\text{Total Assets}}$$

Where,

$$\text{Retained Earning} = \text{Rs. } 988$$

$$\text{Total Assets} = \text{Rs. } 9,888,533$$

$$\text{So, } X_2 = \text{Rs. } 988 / \text{Rs. } 9,888,533$$

$$= 0.0001$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

Where,

$$\text{EBIT} = \text{Net Profit before Interest \& Taxes} + \text{Interest Expense}$$

$$= \text{Rs. } 204,293 + \text{Rs. } 241,639$$

$$= \text{Rs. } 445,932$$

$$\text{Total Assets} = \text{Rs. } 9,888,533$$

$$\text{So, } X_3 = \text{Rs. } 445,932 / \text{Rs. } 9,888,533$$

$$= 0.0451$$

$$X_4 = \frac{\text{Total market Value of Stock}}{\text{Book Value of Total Debt}}$$

Where,

$$\begin{aligned} \text{Total Market Value of Stock} &= \text{MPS} \times \text{No. of Outstanding Shares} \\ &= \text{Rs. } 430 \times 4,635,809 \\ &= \text{Rs. } 1,993,397,870 \end{aligned}$$

$$\text{Total Book Value of Debt} = \text{Rs. } 7,865,159,000$$

$$\begin{aligned} \text{So, } X_4 &= \text{Rs. } 1,993,397,870 / \text{Rs. } 7,865,159,000 \\ &= 0.2534 \end{aligned}$$

$$X_5 = \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

$$\text{Total Investment} = \text{Rs. } 8,510,833$$

$$\text{Total Assets} = \text{Rs. } 9,888,533$$

$$\begin{aligned} \text{So, } X_5 &= \text{Rs. } 8,510,833 / \text{Rs. } 9,888,533 \\ &= 0.8607 \end{aligned}$$

Now, Substitute the values of these variables in the given equation, we acquire the Z Score of the Bank of Kathmandu Ltd as follows:

$$\begin{aligned} \text{Z Score} &= 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5 \\ &= (1.2 \times 0.0892) + (1.4 \times 0.0001) + (3.3 \times 0.0451) + (0.6 \times 0.2534) + \\ &\quad (0.999 \times 0.8607) \\ &= 0.1070 + 0.0001 + 0.1488 + 0.1520 + 0.8598 \\ &= 1.27 \end{aligned}$$

The Z Score of Bank of Kathmandu Ltd for the FY 2004/05 is 1.27. Since it is less than 1.81, it would have probability of failure high.

#### 4. Calculation of Z Score of the Bank of Kathmandu Ltd. (FY 2005/06)

$$Z \text{ Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

Where,

$$X_1 = \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$\text{Net Working Capital} = \text{Total Current Assets} - \text{Total Current Liabilities}$$

$$= \text{Rs. } 8,785,517 - \text{Rs. } 8,528,842$$

$$= \text{Rs. } 256,675$$

$$\text{Total Assets} = \text{Rs. } 12,278,329$$

$$\text{So, } X_1 = \text{Rs. } 256,675 / \text{Rs. } 12,278,329$$

$$= 0.0209$$

$$X_2 = \frac{\text{Retained Earning}}{\text{Total Assets}}$$

Where,

$$\text{Retained Earning} = \text{Rs. } 8,312$$

$$\text{Total Assets} = \text{Rs. } 12,278,329$$

$$\text{So, } X_2 = \text{Rs. } 8,312 / \text{Rs. } 12,278,329$$

$$= 0.0007$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

Where,

$$\text{EBIT} = \text{Net Profit before Interest \& Taxes} + \text{Interest Expense}$$

$$= \text{Rs. } 301,208 + \text{Rs. } 308,156$$

$$= \text{Rs. } 609,364$$

$$\text{Total Assets} = \text{Rs. } 12,278,329$$

$$\text{So, } X_3 = \text{Rs. } 609,364 / \text{Rs. } 12,278,329$$

$$= 0.0496$$

$$X_4 = \frac{\text{Total market Value of Stock}}{\text{Book Value of Total Debt}}$$

Where,

Total Market Value of Stock = MPS × No. of Outstanding Shares

$$= \text{Rs. } 850 \times 4,635,809$$

$$= \text{Rs. } 3,940,437,650$$

Total Book Value of Debt = Rs. 9,531,691,000

$$\text{So, } X_4 = \text{Rs. } 3,940,437,650 / \text{Rs. } 9,531,691,000$$

$$= 0.4134$$

$$X_5 = \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

Total Investment = Rs. 10,633,795

Total Assets = Rs. 12,278,329

$$\text{So, } X_5 = \text{Rs. } 10,633,795 / \text{Rs. } 12,278,329$$

$$= 0.8661$$

Now, Substitute the values of these variables in the given equation, we acquire the Z Score of the Bank of Kathmandu Ltd as follows:

$$\text{Z Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

$$= (1.2 \times 0.0209) + (1.4 \times 0.0007) + (3.3 \times 0.0496) + (0.6 \times 0.4134) + (0.999 \times 0.8661)$$

$$= 0.0251 + 0.0010 + 0.1637 + 0.2480 + 0.8652$$

$$= 1.30$$

The Z Score of Bank of Kathmandu Ltd for the FY 2005/06 is 1.30. Since it is less than 1.81, it would have probability of failure high.

## **5. Calculation of Z Score of the Bank of Kathmandu Ltd. (FY 2006/07)**

$$\text{Z Score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

Where,

$$X_1 = \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$\begin{aligned}\text{Net Working Capital} &= \text{Total Current Assets} - \text{Total Current Liabilities} \\ &= \text{Rs. } 11,253,195 - \text{Rs. } 10,350,949 \\ &= \text{Rs. } 902,246\end{aligned}$$

$$\begin{aligned}\text{Total Assets} &= \text{Rs. } 14,570,099 \\ \text{So, } X_1 &= \text{Rs. } 902,246 / \text{Rs. } 14,570,099 \\ &= 0.0619\end{aligned}$$

$$X_2 = \frac{\text{Retained Earning}}{\text{Total Assets}}$$

Where,

$$\begin{aligned}\text{Retained Earning} &= \text{Rs. } 6,695 \\ \text{Total Assets} &= \text{Rs. } 14,570,099 \\ \text{So, } X_2 &= \text{Rs. } 6,695 / \text{Rs. } 14,570,099 \\ &= 0.0005\end{aligned}$$

$$X_3 = \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

Where,

$$\begin{aligned}\text{EBIT} &= \text{Net Profit before Interest \& Taxes} + \text{Interest Expense} \\ &= \text{Rs. } 421,715 + \text{Rs. } 339,181 \\ &= \text{Rs. } 760,896 \\ \text{Total Assets} &= \text{Rs. } 14,570,099 \\ \text{So, } X_3 &= \text{Rs. } 760,896 / \text{Rs. } 14,570,099 \\ &= 0.0522\end{aligned}$$

$$X_4 = \frac{\text{Total market Value of Stock}}{\text{Book Value of Total Debt}}$$

Where,

Total Market Value of Stock = MPS × No. of Outstanding Shares

$$= \text{Rs. } 1375 \times 6,031,413$$

$$= \text{Rs. } 8,293,192,875$$

Total Book Value of Debt = Rs. 13,421,945,000

$$\text{So, } X_4 = \text{Rs. } 8,293,192,875 / \text{Rs. } 13,421,945,000$$

$$= 0.6179$$

$$X_5 = \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

Total Investment = Rs. 12,391,761

Total Assets = Rs. 14,570,099

$$\text{So, } X_5 = \text{Rs. } 12,391,761 / \text{Rs. } 14,570,099$$

$$= 0.8505$$

Now, Substitute the values of these variables in the given equation, we acquire the Z Score of the Bank of Kathmandu Ltd as follows:

$$\text{Z score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

$$= (1.2 \times 0.0619) + (1.4 \times 0.0005) + (3.3 \times 0.0522) + (0.6 \times 0.6179) + (0.999 \times 0.8505)$$

$$= 0.0743 + 0.0007 + 0.1723 + 0.3707 + 0.8496$$

$$= 1.47$$

The Z Score of Bank of Kathmanu Ltd for the FY 2006/07 is 1.47. Since it is less than 1.81, it would have probability of failure high.

## **6. Calculation of Z score of the Bank of Kathmandu Ltd. (FY 2007/08)**

$$\text{Z score} = 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5$$

Where,

$$X_1 X \frac{\text{Net Working Capital}}{\text{Total Assets}}$$

$$\text{Net Working Capital} = \text{Total Current Assets} - \text{Total Current Liabilities}$$

$$= \text{Rs. } 14,130,130 - \text{Rs. } 12,476,675$$

$$= \text{Rs. } 1,653,455$$

$$\text{Total Assets} = \text{Rs. } 17,721,925$$

$$\text{So, } X_1 = \text{Rs. } 1,653,455 / \text{Rs. } 17,721,925$$

$$= 0.0933$$

$$X_2 X \frac{\text{Retained Earning}}{\text{Total Assets}}$$

Where,

$$\text{Retained Earning} = \text{Rs. } 22,156$$

$$\text{Total Assets} = \text{Rs. } 17,721,925$$

$$\text{So, } X_2 = \text{Rs. } 22,156 / \text{Rs. } 17,721,925$$

$$= 0.0013$$

$$X_3 X \frac{\text{Earning Before Interest \& Taxes}}{\text{Total Assets}}$$

Where,

$$\text{EBIT} = \text{Net Profit before Interest \& Taxes} + \text{Interest Expense}$$

$$= \text{Rs. } 527,899 + \text{Rs. } 417,543$$

$$= \text{Rs. } 945,442$$

$$\text{Total Assets} = \text{Rs. } 17,721,925$$

$$\text{So, } X_3 = \text{Rs. } 945,442 / \text{Rs. } 17,721,925$$

$$= 0.0533$$

$$X_4 X \frac{\text{Total market Vaue of Stock}}{\text{Book Value of Total Debt}}$$

Where,

$$\text{Total Market Value of Stock} = \text{MPS} \times \text{No. of Outstanding Shares}$$

$$= \text{Rs. } 2350 \times 6,031,413$$

$$= \text{Rs. } 14,173,820,550$$

$$\text{Total Book Value of Debt} = \text{Rs. } 14,287,513,000$$

$$\begin{aligned} \text{So, } X_4 &= \text{Rs. } 14,173,820,550 / \text{Rs. } 14,287,513,000 \\ &= 0.9920 \end{aligned}$$

$$X_5 = X \frac{\text{Total Investment}}{\text{Total Assets}}$$

Where,

$$\text{Total Investment} = \text{Rs. } 15,666,705$$

$$\text{Total Assets} = \text{Rs. } 17,721,925$$

$$\begin{aligned} \text{So, } X_5 &= \text{Rs. } 15,666,705 / \text{Rs. } 17,721,925 \\ &= 0.8840 \end{aligned}$$

Now, Substitute the values of these variables in the given equation, we acquire the Z Score of the Bank of Kathmandu Ltd as follows:

$$\begin{aligned} \text{Z Score} &= 1.2 X_1 + 1.4 X_2 + 3.3 X_3 + 0.6 X_4 + 0.999 X_5 \\ &= (1.2 \times 0.0933) + (1.4 \times 0.0013) + (3.3 \times 0.0533) + (0.6 \times 0.9920) + \\ &\quad (0.999 \times 0.8840) \\ &= 0.1120 + 0.0018 + 0.1759 + 0.5952 + 0.8831 \\ &= 1.77 \end{aligned}$$

The Z Score of Bank of Kathmandu Ltd for the FY 2007/08 is 1.77. Since it is less than 1.81, it would have probability of failure high.

The Z Score of Bank of Kathmandu Ltd from FY 2002/03 – 2007/08 is presented below in Table – 4.24

**Table – 4.24**

**Z Score**

Fiscal Year	Z Score
2002/03	1.23
2003/04	1.17
2004/05	1.27
2005/06	1.30

2006/07	1.47
2007/08	1.77
Mean	1.37

The above table shows that bank was struggling in the market during the study period, because the score is below 1.81, where the position of bank was little doubtful and hard to determine the possibility of failure bases on Altman's model of bankruptcy. It is not only the tools by which it is predicted that bank goes to bankruptcy. It is concluded that Bankruptcy Score is in improving trend. So, the bank is performing its activities in better way.

#### **4.2.2 Correlation Co-efficient:**

##### **A. Relationship Between Total Deposit and Loan Advances of Bank of Kathmandu Ltd.**

Correlation Co-efficient (r)	Probable Error (P.E.)	6 × P.E.	Relation
0.99	0.005	0.03	Significance

Correlation Co-efficient between total deposit and loan and advances of Bank of Kathmandu is 0.99. It is perfectly correlated. This implies that there is high degree positive correlation between total deposit and loan and advances. The value of 'r' is greater than '6 P.Er.' this shows that there is significance relationship between these variables.

##### **B. Relationship Between Total Deposit and Net Profit of Bank of Kathmandu Ltd.**

Correlation Co-efficient (r)	Probable Error (P.E.)	6 × P.E.	Relation
0.996	0.002	0.012	Significance

Correlation Co-efficient between total deposit and net profit of Bank of Kathmandu is 0.996. It is perfectly correlated. This implies that there is high

degree positive correlation between total deposit and net profit. The value of 'r' is greater than '6 P.Er.' this shows that there is significance relationship between these variables.

**c.Relationship Between Total Assets and Net Profit of Bank of Kathmandu Ltd.**

Correlation Co-efficient (r)	Probable Error (P.E.)	6 × P.E.	Relation
0.998	0.001	0.006	Significance

Correlation Co-efficient between total asset and net profit of Bank of Kathmandu is 0.998. It is perfectly correlated. This implies that there is high degree positive correlation between total asset and net profit.

**4.2.3 Trend Analysis of Total Deposit of Bank of Kathmandu Ltd.**

**Table- 4.25**

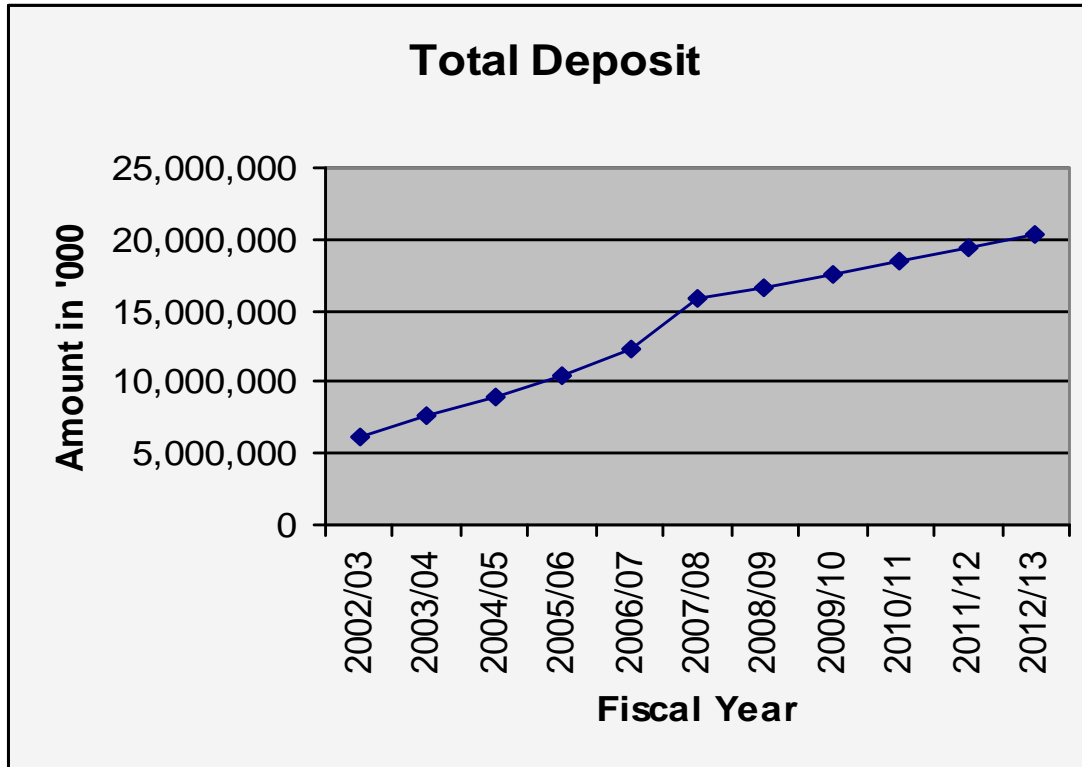
*Rs.in'000*

Fiscal Year	Total Deposit Actual	Fiscal Year	Total Deposit Forecasted
2002/03	6,170,711	2008/09	16,642,683
2003/04	7,741,645	2009/10	17,553,634
2004/05	8,975,781	2010/11	18,464,585
2005/06	10,485,359	2011/12	19,375,535
2006/07	12,388,927	2012/13	20,286,486
2007/08	15,833,738		

*Source: Appendix 25*

Total deposit of Bank of Kathmandu is in increasing trend from the beginning of the study period. Commercial bank must collect scattered money from the people as deposit. The increasing trend of total deposit of bank shows the good performance of the bank.

**Figure - 4.1**



#### 4.2.4 Trend Analysis of Loan and advances of Bank of Kathmandu Ltd.

Table – 4.26

*Rs. In '000*

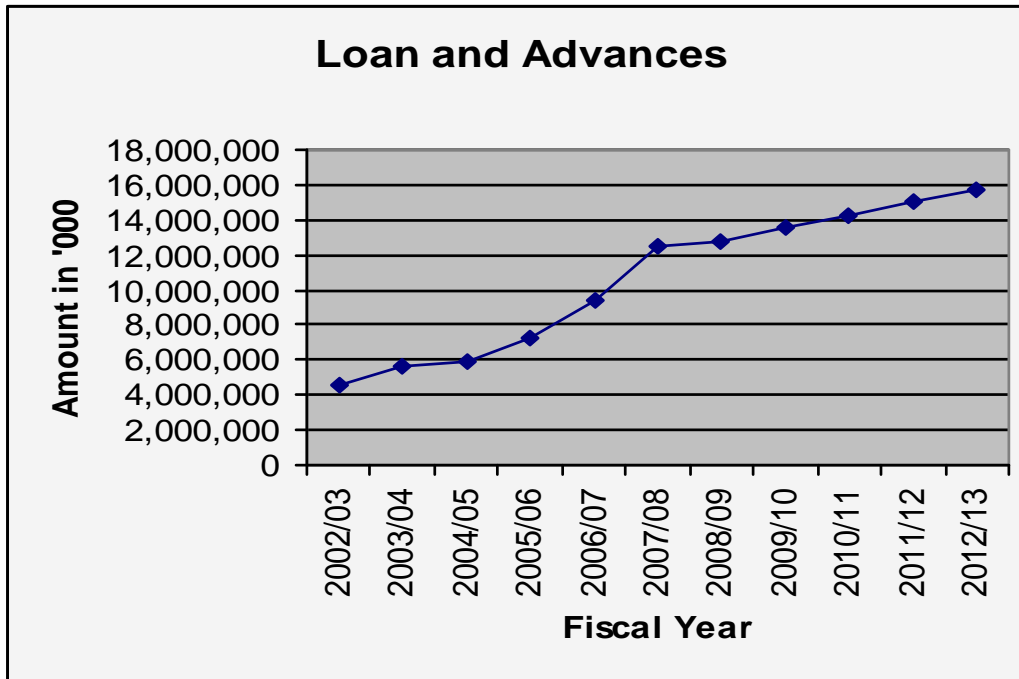
Fiscal Year	Loan and Advances Actual	Fiscal Year	Loan and Advances Forecasted
2002/03	4,542,700	2008/09	12,757,579
2003/04	5,646,698	2009/10	13,503,352
2004/05	5,912,579	2010/11	14,249,125
2005/06	7,259,083	2011/12	14,994,897
2006/07	9,399,328	2012/13	15,740,670
2007/08	12,462,638		

Source : Appendix 26

Bank should invest the amount collected from people in different profitable sector. The trend of loan and advances of bank of Kathmandu has shown that the amount of loan and advances is in increasing trend during the study period. It means, bank

has increased to provide loan every year. Deposits have been mobilized in different sectors. It is good for the development and progress of the bank.

**Figure – 4.2**



#### 4.2.5 Trend Analysis of Total Investment of Bank of Kathmandu Ltd.

**Table – 4.27**

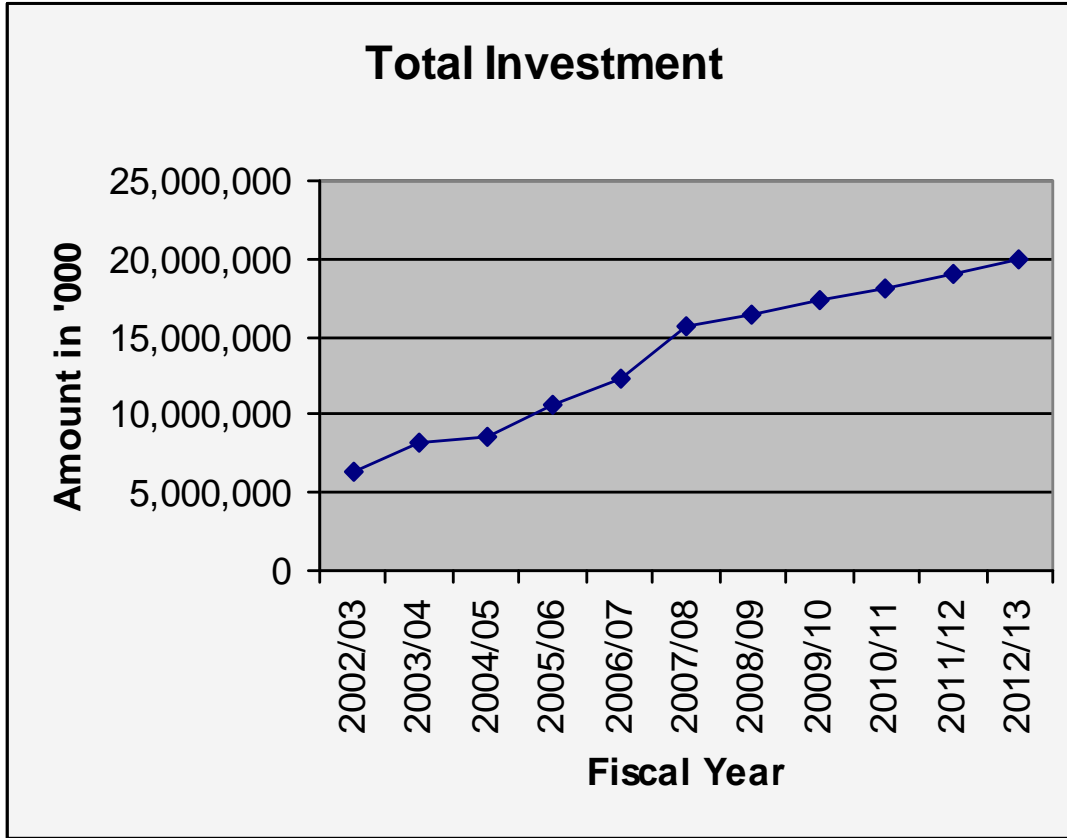
*Rs.in'000*

Fiscal Year	Total Investment Actual	Fiscal Year	Total Investment Forecasted
2002/03	6,358,849	2008/09	16,427,529
2003/04	8,124,108	2009/10	17,305,603
2004/05	8,510,833	2010/11	18,183,677
2005/06	10,633,795	2011/12	19,061,752
2006/07	12,391,761	2012/13	19,939,826
2007/08	15,666,705		

*Source : Appendix 27*

Bank of Kathmandu Ltd has increased to make investment in every year. The increasing trend of investment of bank shows the good performance of the bank.

Figure- 4.3



4.2.6 Trend Analysis of Net Profit of Bank of Kathmandu Ltd.

Table – 4.28

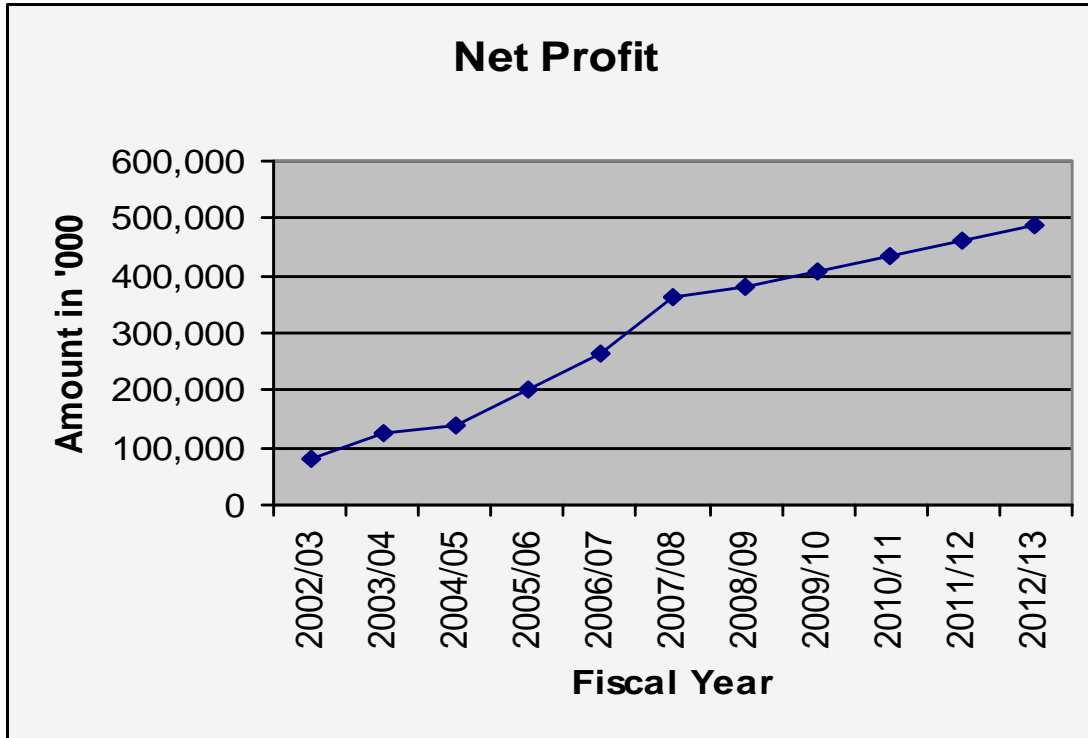
*Rs.in'000*

Fiscal Year	Net Profit Actual	Fiscal Year	Net Profit Forecasted
2002/03	82,128	2008/09	382,359
2003/04	127,473	2009/10	408,995
2004/05	139,530	2010/11	435,630
2005/06	202,441	2011/12	462,266
2006/07	262,387	2012/13	488,902
2007/08	361,497		

Source : Appendix 28

The above table shows that the trend value of net profit of bank is in increasing trend if all other things remaining constant. Total Net Profit of Bank of Kathmandu is in increasing trend from the beginning of the study period. The increasing trend of total Net Profit of bank shows the good performance of the bank.

**Figure – 4.4**



### **4.3 Major Finding of the Study.**

On the basis of Data Analysis and Presentation in sections 4.1, 4.2, and 4.3 of this chapter, the major findings of the study are as following.

#### **4.3.1 Finding from the Ratio Analysis:**

Ratio Analysis involves the method of calculating and interpreting financial ratios in order to assess the firm's financial performance and status. The following are the finding from Ratio Analysis.

##### **A. Finding from Liquidity Ratio:**

- i. The bank has the highest current ratio of 1.14 in the FY 2002/03 and the lowest current ratio of 1.03 in the FY 2005/06 with an average of 1.10 during the study period. It shows that bank has able to meet short term obligation.
- ii. Cash and Bank Balance to Current Assets Ratio of Bank of Kathmandu Ltd differ from maximum of 12.52% in FY 2002/03 to the minimum of 8.29% in the FY 2005/06 with and average of 10.72% during the study period of six years. The analysis shows the fluctuating trend of ratios.
- iii. Loans and Advances are the bills purchased and discounted local and foreign currencies, loans & advances and overdraft which are the main source of income of the commercial banks. Loans and advances of the bank varies from maximum of 88.20% in the FY 2007/08 to the minimum of 81.42% in the FY 2003/04 with an average of 83.38% The Analysis indicates that the disbursement of loans and advances with respect to current Assets is in increasing trend during the study period.
- iv. Fixed deposit is the highest interest bearing deposit and can be withdrawn only after its maturity period. Fixed deposit to total deposit ratio of the Bank of Kathmandu Ltd is differ from maximum of 32.26% in the FY 2002/03 to the minimum of 23.39% in the FY 2007/08 with an average of 27.92% during the study period. The analysis indicates that fixed deposit to total deposit ratio is fluctuating.
- v. Saving deposits are less interest bearing deposit than fixed deposit. These deposits are not as freely withdrawn as current deposit. The saving deposit to total deposit of Bank of Kathmandu Ltd differ from maximum of 44.61% in the FY 2006/07 to the minimum of 36.765 in the FY 2002/03 with an

average of 40.38% during the study period. The analysis indicates that the share of saving deposit in the total deposit is in increasing trend.

- vi. The cash reserve requirements in most of the developed and developing countries has been used extensively as a means to control commercial banks credit. Regarding Cash Reserve, Nepal Rastra Bank has guided all the commercial banks to maintain at least 6.5% of their deposit liabilities as reserve. The cash reserve ratio of Bank of Kathmandu Ltd differ from maximum of 10.62% in the FY 2006/07 to the minimum of 6.95% in the FY 2005/06 with an average of 9.38% during the study period of six years. It has shown that the bank has maintained cash reserve ratio as per the directives of Nepal Rastra Bank.

#### **B. Findings from Activity Ratios.**

- i. Loan and advances to total deposit ratio measures the extent to which the bank is success to utilize the outsiders' fund. Loans and advances to total deposit of Bank of Kathmandu Ltd fluctuates from maximum 0.79 times in the FY 2007/08 to the minimum of 0.66 times in the FY 2004/05 with an average of 0.73 times during the study period. The analysis designates that the bank is mobilizing its total deposit in loans and advances adequately and it has efficiently utilized its total deposit.
- ii. Loans and advances to fixed deposit ratio measures how many times the amount is used in loan and advance in comparison to fixed deposit. Loan and advances to fixed deposit of Bank of Kathmandu Ltd varies from maximum of 3.33 times in the FY 2007/08 to the minimum of 2.05 times in the FY 2004/05 with an average of 2.66 times during the study period. It shows that the involvement of fixed deposit in loan and advances is more or less constant.

- iii. Loans and advances to saving deposit ratio measure how many times the highest interest bearing deposits are utilized for income generating purpose. Loan and advances to saving deposit of Bank of Kathmandu Ltd fluctuates from maximum of 2.00 times in the FY 2002/03 to the minimum of 1.58 times in the FY 2005/06 with an average of 1.81 times during the study period. The analysis designates that the contribution of saving deposit in loan and advances is in fluctuating trend in satisfactory level.

### **C. Finding from Leverage Ratio**

- i. Total debt to shareholders' equity ratio is used to measure the degree of financial leverage of the firm. This ratio of Bank of Kathmandu Ltd differs from maximum of 16.93 times in the FY 2003/04 to the minimum of 10.65 times in the FY 2007/08 with an average of 12.72 times during the study period. The analysis indicates that the bank has the high debt ratio which means the creditors have invested more in the bank than the owners.
- ii. Total debt to total assets ratio is the relationship between creditors' fund and owners' capital. This ratio shows the proportion of outsiders fund used in financing total assets. Total debt to total assets ratio of Bank of Kathmandu from FY 2002/03 – FY 2007/08 differs from maximum of 72.42% in the FY 2006/07 to the minimum of 63.60% in the FY 2004/05 with an average of 68.88% during the study period. This shows the role of creditors in the bank is higher than the owners.
- iii. Shareholders' equity to total assets ratio shows the shareholders' fund on total assets. The maximum and minimum shareholders' equity to total assets ratio of Bank of Kathmandu Ltd is 7.57% in the FY 2007/08 and 6.23% in the FY 2002/03 respectively. The portion of shareholders' equity

is 6.59% in average. It shows that the portion of shareholders' equity is less in the bank.

#### **D. Finding from Profitability Ratio**

- i. Interest earning is the major source of commercial banks. Interest earned to total assets ratio reflects the proportion of interest earned by the bank from the total income. The interest earned to total assets of the Bank of Kathmandu Ltd differ from maximum of 2.04 % in the FY 2007/08 to the minimum of 1.10% in the FY 2002/03 with an average of 1.56% during the study period of six years. This analysis indicates that the interest earned in comparison to the total assets is in increasing trend. It shows that bank has utilized its assets effectively to generate income.
- ii. Net Profit to total deposit ratio indicates the percentage of profit earned by using the total deposit. Net profit to total deposit of the Bank of Kathmandu Ltd varies from maximum of 2.28% to the minimum of 1.13% with an average of 1.81% during the study period. This analysis indicates that net profit earned in comparison to the total deposit is in increasing trend. In general, it reveals that the bank is mobilizing funds effectively and efficiently.
- iii. The Return on Assets ( ROA) or Net Profit to Total Asset Ratio is a useful measurement of the profitability of all financial resources invested in the assets. The analysis reveals that net profit to total assets of the Bank of Kathmandu Ltd differ from maximum of 2.98% in the FY 2007/08 to the minimum of 0.64% in the FY 2002/03 with an average of 2.33% during the study period of six years. The analysis indicates that the profit earning in relation with total assets of Bank of Kathmandu Ltd is in increasing trend.

- iv. Net worth or Shareholders' Equity ratio refers to the owners' claim on the assets of the bank. The Net Profit to Net Worth or Return on Equity (ROE) measures the income on the owners' investment. This ratio indicates how well the bank has used the resources of the owners. Return on Equity of the Bank of Kathmandu Ltd varies from maximum of 26.94% in the FY 2007/08 to the minimum of 9.20% in the FY2002/03 with an average of 18.03% during the study period of six years. The analysis indicates that the profit earning in relation with shareholders' equity of Bank of Kathmandu Ltd is relatively good which exhibits the better utilization of shareholders' fund.

#### **E. Finding from the Market Based Ratio**

- i. The EPS represents the amount earned on behalf of each outstanding share of common stock. The EPS of the Bank of Kathmandu Ltd varies from maximum of Rs. 59.94 in the FY 2007/08 to the minimum of Rs. 17.72 in the FY 2002/03 with an average of Rs. 37.07. It shows the EPS of the Bank of Kathmandu is quite good as it is in increasing way every year.
- ii. Dividend Per Share is calculated to know proportion of earnings distributed to the shareholders per share. The DPS of Bank of Kathmandu Ltd differs from maximum of Rs. 42.11 in the FY 2007/08 to the minimum of Rs. 5.00 in the FY 2002/03 with an average of Rs. 23.35 during the study period. DPS of Bank of Kathmandu Ltd is not satisfactory till the FY 2004/05 but after that it is satisfactory.
- iii. Dividend Payout Ratio represents the percentage of the profits distributed as dividend and the percentage retained as revenue and surplus for the

growth of the bank. Dividend Payout Ratio of Bank of Kathmandu varies from maximum of 109.92 in the FY 2005/06 to the minimum of 28.22 in the FY 2002/03 with an average of 56.76 during the study period. It shows the irregular dividend payout of the bank.

#### **4.8.2 Finding from the Income and Expenditure Analysis**

- i. Income and Expenditure are the main indicators of the financial performance of the business firm. The income and expenditure statement provides a financial summary of the firm's operating results during the period specified. The interest earning are from loans and advances, overdraft, government securities, treasury bills, debentures and others. The operating income of the Bank of Kathmandu Ltd is in increasing trend from the beginning during the study period of six years. It shows that the bank is doing good business.
- ii. The expenditure heads of the bank are interest expenses, personnel expenses and other operating and non-operating expenses of bank. The high rate of interest expenses indicates that the bank has collected more deposits. The second main expenditure heading of the bank is office operating expenses and the third is personnel expenses. The expenditure pattern of the bank is satisfactory. It shows that bank has not made the expenditure unnecessarily.

## **Chapter - 5**

### **SUMMARY, CONCLUSION AND RECOMMENDATION**

#### **5.1 Summary**

Economic development of a country can not be imagined without the development of commerce and trade. No doubt, banking promotes the development of commerce to its extreme since banking itself is a part of commerce. Though the economic development was in snail speed in earlier years, it has caught its full swing with restoration of democracy in the country. The number of commercial banks with foreign collaboration has reached to 25 and other regional commercial banks are also emerging rapidly. Similarly, the finance companies have also been incredibly increasing. It is good sign for overall economic development of the country. Banking helps to collect scattered capital and mobilize in profitable sector. Banking is considered as the platform of money market and capital market. Commercial banks have been able to attain their goals within short span of time because of the qualitative managerial skills; prompt service and using advanced technology as compared to other local traditionally run commercial banks in Nepal.

The present study has been undertaken with a view to examine the financial performance of Bank of Kathmandu Ltd. The present study aimed at analyzing the financial statement of the bank for a period of six years starting from FY 2002/03 to FY 2007/08. The study is mainly based upon secondary data which have been first processed and then, analyzed to find the financial position of bank.

## **5.2 Conclusions**

On the basis of Ratio Analysis of Bank of Kathmandu Ltd, the following results have been revealed.

### **5.2.1 Liquidity Ratio:**

Under liquidity ratios, the ratios calculated to find the financial position of bank are current ratios, cash and bank balance to current assets ratio, loan and advances to current assets ratio, fixed deposit to total deposit ratio, saving deposit to total deposit ratio and cash and bank balances to total deposit ratio. The current ratio of Bank of Kathmandu Ltd is below standard i.e. 2:1 during the study period. Likewise, the cash and bank balance to current assets ratio of bank was found to be fluctuating. However, cash and bank balances of Bank of Kathmandu Ltd meet the unexpected calls made by its customers on saving, current and fixed deposit. Idle cash balance is also burden to the bank.

### **5.2.2 Activity Ratio :**

Loan and advances to total deposit of Bank of Kathmandu Ltd is nearly 1 time. It shows that bank is in better position in terms of utilizing customers' deposit in the form of loan and advances to saving deposit and fixed deposit is also higher.

### **5.2.3 Profitability Ratios:**

All the profitability ratios of Bank of Kathmandu Ltd are in increasing trend during the study period. It shows that bank is doing good business.

### **5.2.4 Other Ratios:**

**a. Debt to Equity Ratio:** The debt equity ratio of the bank is high during the study period. It shows that bank is using more portion of debt than equity. It really

hampers the bank's profitability as interest should be paid. On the other hand, interest is tax deductible item also.

**b. EPS:** The earning per share of the bank is satisfactory as it is in increasing trend from the beginning of the study period.

**c. DPS:** Bank of Kathmandu Ltd paid dividend to its shareholders regularly during the study period. DPS was comparatively low till the FY 2004/05. Then after it increased the amount of dividend except in the FY 2006/07.

### **5.3 Recommendations**

The following recommendations are made to strength Bank of Kathmandu Ltd.

#### **a. Increase Equity Capital:**

There is a need of capital adequacy for the bank. Therefore, the bank should increase the proportion of equity capital in its capital structure.

#### **b. Improve Operational Efficiency:**

Since there is a neck competition among commercial banks. So the bank should strive hard to enhance its operational efficiency. This can be achieved through reduction in operational costs, prompt customer services etc. The bank needs to provide prompt services to win the credibility of the customers, although all operating cost can not be minimized. However, there are some costs which can be reduced by improving operational efficiency. These expenses could be general expenses, fuel, stationery expenses and miscellaneous expenses. Similarly, the training should be given to employees on regular basis to improve the efficiency in their performance so that they can use their expertise more effectively.

#### **c. Improve Liquidity Position:**

The current assets of the bank are found just enough to discharge current liabilities. The current ratio as well as other liquidity ratios was found to be fluctuating. There should be definite policy as how much balance of cash to be maintained to meet the customers' demand on their deposit and other liabilities.

The bank should maintain such balance of cash which neither leads to idleness nor a shortage in the future.

**d. Meet Social Responsibility:**

Most of the commercial banks have established their offices in urban areas. They need to serve rural communities and small fund depositors by operating rural branches. The more branches also help to collect their deposits; higher deposit will help to invest more which consequently means faster economic development of the country.

**e. Invest More in Productive Sectors:**

Banking activities can uplift the overall- economy of the country. Thus, in order to enhance the economic growth of the country, the bank should invest more in productive sectors like industry and manufacturing areas which ultimately increases GDP improve the balance of payment and of course, provide more employment opportunities to the public.

Besides that, the bank should formulate new policies, create new ideas and provides new services like woman's development programs, entrepreneur's development programs, poverty alleviation programs etc. These programs will definitely help the country for infrastructure development and of course, overall economic upliftment of the country.