

**A STUDY ON NON-PERFORMING ASSETS OF NEPAL INVESTMENT
BANK LIMITED & KUMARI BANK LIMITED**

A Thesis

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RECOMMENDATION

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DECLARATION

I, hereby, declare that the work reported in this thesis entitled “**A Study On Non-Performing Assets Of Nepal Investment Bank Limited & Kumari Bank Limited**” submitted to office of the Dean, Faculty of Management, Tribhuvan University, is my original work done for the partial fulfillment of the requirement for the Masters of Business Studies (MBS) under the supervision of **Prof. Dr. Kamal Deep Dhakal** Shanker Dev Campus., Putalisadak, Kathmandu.

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ABBREVIATION

AMC	:	Assets Management Company
ATM	:	Automatic Teller Machine
CEO	:	Chief Executive Officer
CRR	:	Cash Reserve Ratio
CV	:	Coefficient of Variation
JVB	:	Joint Venture Bank
KBL	:	Kumari Bank Limited
NIBL	:	Nepal Investment Bank Limited
NPA	:	Non-Performing Assets
NPAT	:	Net Profit after Tax
NPL	:	Non-Performing Loan
NPM	:	Net Profit Margin
NRB	:	Nepal Rastra Bank
RBB	:	Rastriya Banijya Bank
ROA	:	Return on Assets
ROE	:	Return on Equity
TA	:	Total Assets
TD	:	Total Deposit
TL	:	Total Loan

CHAPTER-I

INTRODUCTION

1.1 General Background of the Study

Once the distributed loan is not returned timely by clients and becomes overdue then, it is known as Non Performing Assets for the bank. Reduction of NPA has always been a significant problem for every commercial bank. NPA may be defined broadly as the Bad Debt; however, it in terms of banking sector consists of those loans and advances which are not performing well and likely to be turn as bad debt. NPA as per the current directives of Nepal Rastra Bank, NRB, has been categorized as classified loans and advances. NPA has severe impacts on the financial institutions. On the one hand, the Investment becomes worthless as expected return cannot be realized and on the other, due to the provision required for the risk mitigation the profitability is directly affected. The existence of the bank can be questioned in this situation. Thus, interest along with principal has to be recovered timely and without any obstacles.

To start with performance in terms of profitability in a benchmark for any business enterprises, including the banking industry, however increasing nonperforming assets have a direct impact on banks profitability as legally banks are not allowed to book income on such assets.

Loans and Advances dominate the assets side of balance sheet of any bank. Similarly, earning from such loans and advances occupy major space in income statement of the banks. However it is very important to be reminded that most of the bank failures in the world are due to shrinkage in the value of the loan and advances. Hence loan is known as risky assets. Risk of non-repayment of loan is known as credit risk or default risk. Performing loans have multiple benefits to the society while non-performing loans erodes even existing capital.

Performing assets are those loans that repay principal and interest to the bank from the cash flow it generates. Loans are risky assets, though a bank interest most of its resources in granting loans and advances. If an individual bank has around 10% non-

performing assets or loans, it sounds the death knell of that bank other remaining the same. The objectives of bound loan policy are to maintain the financial health of the banks, which result in safety of depositor's money increases in the returns to the shareholders. Since the loan is a risky asset there is inherent risk in every loans, however, the bank should not take risk above the certain degree irrespective of the returns prospects.

1.1.1 Brief Introduction of Selected Banks

Kumari Bank Limited (KBL)

Kumari Bank Limited is a well-established commercial bank. Its promoters represent a group of highly reputed Nepalese. Managed by experienced and dynamic professionals, Kumari Bank's competitive banking services have become a hall-mark amongst its ever increasing customer base.

In the review period, capital management of the Bank has been quite satisfactory. The core and supplementary capital of the Bank at the end of F/Y 2011/12 were Rs. 2.20 billion and Rs. 25.15 million, taking the total capital to Rs. 2.45 billion. The Bank has been able to maintain Capital Adequacy Ratio at 13.76% at the yearend against the statutory requirement of 10% by the Central Bank (Nepal Rastra Bank).

The Bank continues to provide innovative and modern banking products and services leveraged by the latest available technological know-how to enable our valued customers to have the competitive edge. The bank's products and services cover the whole range of banking requirements of our customers, from retail banking, SME banking to corporate banking. The Bank since its inception has been providing IT based solutions like internet banking, SMS banking and globally accepted electronic VISA debit cards.

To cater to the ever increasing Nepalese Diasporas across the world, the Bank has launched its own e-remittance platform Kumari Remit, and has received immense reception from remitters. Apart from Kumari Remit, the Bank in F/Y 2010/11

introduced Kumari Mobile Cash, a revolutionary service that uses mobile phones to provide access to financial services. The first of its kind in Nepal, this service pioneers the “mobile wallet” concept, which allows users to store cash balances in their mobile phones. Users are then able to deposit and withdraw cash from their mobile phones, and use the stored cash value to remit to anyone, anytime, anywhere, with the push of a few buttons. Even in days to come, the Bank will continue to embrace the latest technological innovations to provide value addition to its customers.

Acting as a conduit to the economic activities of the country and to cater to the needs of customers, the Bank has given continuity to expanding branches across the country. In F/Y 2011/12, the Bank added 10 more branches, making the total number of branches 28. The Bank has also added more Automated Teller Machine (ATMs) in the review period. By the end of F/Y 2011/12, the Bank has a total of 33 ATMs.

Table: 1.1

Share Capital Structure of KBL

Authorized Capital	Rs. 1,600,000,000
Issued Capital	Rs. 1,485,000,000
Paid up Capital	Rs. 1,485,000,000
Value per share	Rs. 100

Source: www.kumaribank.com

Investment Bank Limited (NIBL)

Nepal Investment Bank Ltd. (NIBL), previously Nepal Indosuez Bank Ltd., was established in 2043 as a joint venture between Nepali and French partners. The French partner (holding 50%) of the capital) was Credit Agricole Indosuez, a subsidiary of one of the largest banking groups in the world. When Credit Agricole Indosuez decided to divest, a group of companies comprising of bankers, professionals, industrialists and businessmen acquired 50% of the holdings of Credit Agricole Indosuez in Nepal Indosuez Bank in 2060. The name of the Bank was changed to

Nepal Investment Bank Ltd. upon approval of the Bank's Annual General Meeting, Nepal Rastra Bank and Company Registrar's Office.

The bank has 40 branches. And bank's target is to open up to 50 branches all over the country. The bank witnessed encouraging recognition from the market of the new name and management. Bank has been able to enhance its services to its customers by providing them extended banking hours and keeping the bank open for 365 days. The products of the bank, namely vehicle financing, Ezee saving scheme and Locker services, received favorable responses from the market. Bank has been awarded "Bank of the Year 2003", "Bank of the year 2005" "Bank of The Year 2008" by the London based Financial Times Group's The banker, Making it the first all Nepali managed bank ever to received the award. The bank was selected for these honors because it meets the stringent criteria set by the banker. The award is based on the growth and performance in terms of capital, assets, and return on equity and management quality.

It was judged as the best bank in Nepal by The Banker's editorial team which consists of high profile senior business and banking figures. The bank has implemented its own financial switch system which provided online transaction from different delivery channels such as ATM, POS terminals. The bank set another milestone in introducing updated technology by launching and international "Visa Electron Debit Card" the first of its kind in Nepal, which will provide convenient banking to customers. The card will also give easy access to cash at the bank's ATMs as well as at other bank's ATMs and payments at merchant's establishments having POS terminals.

The first non-government bank to launch loan against gold and silver. It has so far issued over 250000 cards making it the leader in the industry within a span of over one and half year. The bank recently launched the 'premier Banking cell' that caters to its high net worth clients and renders consultancy services in taxation, legal, insurance and travel and tours, NIBL has also started a concept of '15 minute banking for the convenience of its customers. Besides these the effort to introduce updated technology and to deliver to customers the best services, will in near future, introduce and international Credit Card (VISA) for which all preliminary arrangement, namely

searing of membership, approval etc. have already achieved. Bank expects to launch the credit cards with in fiscal year and an application has also been forwarded to Master card for acquiring and issuing business. The bank has E-banking and mobile banking and became the member of International “master card”.

Table: 1.2

Share capital structure

Authorized Capital	Rs. 4,000,000,000
Issued Capital	Rs. 2,409,097,700
Paid up Capital	Rs. 2,409,097,700
Value per share	Rs. 100

Source: www.nibl.com

1.2 Statement of the Problems

Financial companies and institutions are nowadays facing a major problem of managing the Non Performing Assets (NPA) as these assets are proving to become a major setback for the growth of the economy. Undoubtedly, the world economy has slowed down. Globally stock markets have tumbled and business itself is getting hard to do with the simple reason that the banks (creditor) money in the form of funds gets blocked. Under such a situation, it goes without saying that banks are no exception and are bound to face the heat of a global downturn.

Assets are the most critical factor in determining the strength of any bank. The primary factors that can be considered are the quality of the loan portfolio, mix of risk assets and the credit administration system. The lower NPL ratio indicates better risk assessment and robust credit management system are in place and vice-versa. At the same time higher loan loss provisions indicate poor credit management; it also indicates adequate reserve for possible loan loss, protecting the balance sheets of respective banks. The Problems of NPA are as follows;

- Owners do not receive a market return on their capital in the worst case, if the banks fails, owners lose their assets. In modern times this may affect a broad pool of shareholders.
- Depositors do not receive a market return on saving. In the worst case if the bank fails, depositors lose their assets or uninsured balance.
- Banks redistribute losses to other borrowers by charging higher interest rates, lower deposit rates and higher lending rates repress saving and financial market, which hamper economic growth.
- Nonperforming loans symbolize bad investment. They misallocate credit from good projects, which do not receive funding, to failed projects. Bad investment ends up in misallocation of capital, and by extension, labor and natural resources.
- Nonperforming asset may spill over the banking system and contract the money stock, which may lead to economic contraction. This spillover effect can channelized through liquidity or bank insolvency.

As the bank has to meet various challenges this study will be helpful to the bank to identify and solve some of its weakness and problems. In every organization, the resources are scare and out of these scare resources, the objective of the organizations is to be accomplished. Increase in revenue and control over expenditure significantly contributes to improve the profitability as well as the overall financial performance of an organization by the help of the best utilization of resources.

The following research questions are developed for the study.

- What is the overall impact of the NPA on the profitability of the Commercial Banks?
- Is there any relationship between NPA and the profitability of the Commercial Banks?
- What percentage of total assets and total lending is occupying by non-performing assets of Nepalese commercial banks?

- Whether or not Nepalese commercial banks is following NRB's regulation regarding their lending's, especially to maintain the provision for non-performing assets?

1.3 Objectives of the Study

The improper strength, weakness, opportunity and threat analysis is another reason for rise in NPA. Increase in NPA has now become the major issue for every commercial bank. Every bank now has put the NPA management under the top priority and is functioning to reduce the major part of it from the assets side of their balance sheet. The main objective of this research is to examine and study of level of non-performing loans in total assets, total deposit and total lending of Nepalese commercial banks. The specific objectives are as follows:

- To find out the proportion of non-performing loan in the selected commercial banks.
- To study the level of non-performing loans in total assets, total deposit and total lending of Nepalese commercial banks.
- To analyze the relationship between NPA and net profit, loan & advance, total assets and deposit of sample banks.

1.4 Significance of the Study

The success and prosperity of the bank heavily depends upon the successful implementation and investment is collected resources, which develops the economy of the country. Good investment policy of the bank has positive impact on economic development of the country and vice versa. Therefore success of any bank does not depend upon how much money a bank able to lend? But it depends upon the quality of loan. So success of any bank depends upon the amount of performing loan/assets. Performing assets are those loans that repay principal and interest to the bank from the cash flow it generates.

Increasing non-performance loan followed by increasing loans and loan loss provision is one of the challenges faced by commercial banks in the present context. Proper loan provision and loan loss provision helps to get financial strength of the bank. The research will be able to give the some of the present issued, latest information and data regarding non-performing loan and loan loss provision. Not only that, this study gives the real picture of the current non-performance assets to its shareholders.

This study mainly concerned with the analysis of level of non-performance assets, total deposit and total lending of different Nepalese commercial banks. Therefore, it is significant to find out the level of non-performing assets and to find out whether the banks maintained loan loss provision in accordance to NRB's directives or not. It also examines the effects of NPA in ROE and ROA of the bank and points out the defect inherent in it and provide package of suggestion for its improvement if found any.

1.5 Limitations of the Study

This study is simply a partial study for the fulfillment of M.B.S. degree, which had to be finished within limited period. Hence this study is not far from several limitation of its own kind, which weakens the heart of the study. It has certain limitations as follows:

- This study has employed secondary data published by and collected from selected banks.
- The study is focused on the Nepalese commercial banks only. Hence, the findings may not be applicable to all other banks finance companies and other companies of Nepal.
- The study covers a period of 5 fiscal years which will be tabulated and processed for drawing conclusion.
- The accuracy of the research work will be dependent on data provided by concerned organization.
- This study concentrates only on those factors, which are related with nonperforming assets of Nepalese commercial banks. It does not consider other aspects of the banks.

- Profitability of an organization is caused by many factors. This study, however, covers only those factors, that are directly affected by the non-performing assets of the Commercial Banks.

1.6 Organization of the Study

To make the study precise and attractive in presentation, this research work has been divided into five chapter namely Introduction, Review of literature, Research methodology, data presentation and analysis and finally summary, conclusion and recommendations.

Chapter I: Introduction

The first chapter includes narrow aspects of this study like General background of the study, Statement of the problem, Objective of the study, Focus of the study, Significance of the study along with limitation of the study.

Chapter II: Review of Literature

The second chapter incorporates that the conceptual thoughts and related study regarding the subject matter.

Chapter III: Research Methodology

The third chapter discussed the “Research Methodology” used in the study. In comprise research design, nature & source of data, data gathering method along with different statistical and financial tools used.

Chapter IV: Presentation and Analysis of Data

The fourth chapter deals with the “Data Presentation and Analysis of Data” and scoring the empirical finding out the study through definite course of research methodology.

Chapter V: Summary, Conclusion & Recommendations

The last chapter named as “Summary, Conclusion & Recommendation” is followed by the basic conclusion of the study based in the fourth chapter. On the basis of the summary, conclusion is taken out and recommendation has also been presented for consideration.

At the beginning of the thesis recommendation, viva voce sheet, declaration, acknowledgement, table of content and abbreviation are also submitted. And finally, bibliography and appendix are presented at the end of the study.

CHAPTER-II

REVIEW OF THE LITERATURE

Every study is very much based on past knowledge; the past knowledge provides foundation to the present study. This chapter helps to take adequate feed back to broaden the information based and inputs to this study, therefore this chapter has its own important in this study. For this several journals, reports and articles published in different journals and newspaper are being reviews and are categorized in two heading.

- Conceptual framework
- Review of related studies

2.1 Conceptual Framework

2.1.1 Concepts of Commercial Banks

Commercial institutions are those financial institutions, which deals in accepting the deposits of people and institutions and giving loan against securities. They provide working capital needs of trade, industry and even to agricultural sectors. Moreover commercial banks also provide technical and administrative assistance to trade, industries and business enterprise. Commercial banks are a corporation which accepts demand deposits, subject to check and make short term loans to business enterprises, regardless of the scope of its other services.

Commercial banks are the heart of financial system. They hold the deposits of many persons, government establishment and business units. They make fund available through their lending and investing activities to borrowers, individual, business firms and government establishment units.

Therefore commercial banks are those banks that pool together the saving of community and arrange for their productive use. They supply the financial needs of modern business by various means. Commercial banks are restricted to invest their funds in corporate securities. Their business is confined to financing the short terms

needs of trade and industry. They cannot finance in fixed assets. A part from financing, they also lender services like collection of bills and cheque, safe keeping of valuables, financial advising etc to their customers (Vaidya, 2001: 38).

The American institute of Banking has laid down the four major function of Commercial bank such as receiving and handing of deposits, handing payments of its clients making loans and investments and creating money by extension of credit (Principle of Bank Operation, USA: 609).

Principally, commercial banks accept deposits and provide loans, primarily to business firms, thereby facilitating the transfer of funds on the economy (Albrol and Gupta, 1971:65).

In the Nepalese context, banking and financial institution act, 2063 defines “A commercial bank as one which exchange money, deposits money, accepts deposits, gratt loans and performs commercial banking functions” (Commercial Bank Act 2063).

A commercial banks can be define as an institution which deals in money in words of the Crowther “ Banks collect money from those who have it to spar or who are saving it out of their income and lend this money out against goods security to those who requires it” (Crowther, 1985:58).

However, central bank is the main bank of the any nation that directs and controls all the banks whose existence is in the country. In Nepal, Nepal Rastra Bank is the central bank of the country. All the commercial banks perform their functions under rules, regulations and the directives provided by Nepal Rastra Bank.

Under the free enterprise system like U.S.A. the interest of nation as well as those of individuals and stockholders are supposed to be best served by vigorously seeking profit. But the profit cannot be the sole objective of the any enterprise. It should not be evaluated just on the ground of profit earned. Neither the bank nor the community will be best serve if the banker unreasonably scarifies the safety of theirs fund or the liquidity of their bank in an effort to increase income (Vaidya, 2001: 24)

From the above many definition, commercial banks including joint venture banks, they are mainly receiving the money from depositor and invest in different sectors. So that banks are the main source of development of a nation. In the context of Nepal, it is a poor and least developed county having low per capita income and GDP. As a result, many economic problems such as inflation, devaluation of money trade, trade deficit, budget deficit etc arises. For the sake of removing these problems, many joint ventures are being incorporated in our country by sharing Nepal's and foreign investment towards making more profit by using the funds in profitable sectors. Therefore bank should be invested in different sector which helps in the growth of national economy.

2.1.2 Evolution of banking system in Nepal

There are several types of banks but among them commercial banks play significant contribution in the financial system of the country. They pool together the savings of the community and arrange for their productive use. They supply the financial needs of modern business by various means. They accept deposits from public on condition that they are repaid on demand or on short notice. Their business is confined to financing the short-term and medium term needs of trade and industry such as working capital financing.

Commercial Bank Act, 2031 B.S. (1974A.D.) of Nepal has defined the commercial banks as an organization, which exchanges money, accepts, grants loans and performs commercial banking functions and which is not a bank meant for co-operative, agriculture, industries or for such specific purpose. (Bank and Financial Institution Ordinance 2005)

It is the fact that financial sector plays a vital role for the economic development of a country. Even before the establishment of a banking system in Nepal, financial transactions were in practice as undertaken by some moneylenders like sahu-mahajans, zamindars, relatives, friends, and few informal organizations limited to ethnic group such as guthi. The borrowing from the other and the informal organization was limited and based on personal understanding. At that time people

deposit their gold, silver and valuable goods for the sake of security. Thus, the private moneylenders can be taken as forerunner of the concept of financial institution.

However, the private money lenders supported the economic development of a country, the transactions undertaken by them was totally based on their personal understanding. No legal restriction was against them and their monopolies in transactions were the reasons for covering the interest in personal understandings and exploiting the people. Thus, it was then realized the need to establish financial intermediaries in supporting the economic development of a country.

Nepal has been ruled over by many rulers like Kirati, Lichchhavi, Malla, Ranas, and Shahs. Mostly Kirati, Lichchhavi and Malla regimes, who were concerned with the construction of temples, pati-pouwa, chautaris, etc. At that period neither the people nor the government needed to think about the economic development of the country. According to ancient Vanshawali in fourteenth century, the ruler of the Kathmandu Jayasthiti Malla segregated the local domiciles into 64 different classes according to profession they had undertaken. Tankadhari was one of those classes who used to deal in coins and precious metals such as gold. These Tankadharis were said to have carried out the borrowing and lending of money (coins). Hence, Tankadharis can be regarded as the traditional bankers of Nepal.

After long time, during the Rana regime, only handfuls prime minister thought about the economic development of the country. They established some offices in 1993 B.S. (1936 A.D.) Tejarath Addawas established during the tenure of Prime Minister Ranoddip Singh Rana as a first institutionized credit house. Tejarath Adda provided loans under the security of gold and silver to the government employees and public. The government established its various branches and sub-branches at different places of the country for the sake of benefits of people. In the overall development of the banking system in Nepal, the Tejarath Adda may be regarded as the father of modern banking institution and for a quite long time it rendered a good service to the government employees as well as to the general public. The government also implemented the rules against the vast interest rate taken by moneylenders. Thus, the government financial institution occupies an important role in the banking history of

Nepal. To fulfill the growing need of economy in Nepal, banking activities were performed only after the establishment of Nepal Bank Limited in 1994 B.S. (1937 A.D.) as the first commercial bank in Nepal. This bank was established under the Nepal Bank Act 1994 B.S.

At beginning, 49% of the ownership belongs to the promoters as well as general public and remaining belongs to government. The incorporation of Nepal Bank Ltd. is the real starting of the banking institution in Nepal? The bank started the act of consolidating the scattered capital since its establishment in order to mobilize it in productive sector. It developed systematic tradition in culture of modern banking system in Nepal. Such system could be able to establish a strong base for the enlistment of national economy. Besides, it also acted as central bank for more than three decades.

Nepal Rastra Bank was established in Baisakh 14, 2013 B.S. (26 April 1956 A.D.) under Nepal Rastra Bank Act, 2012 B.S. (1955 A.D.), the central bank of Nepal. It is totally owned by government. NRB is heavily assisting for the development of the whole economy. It is giving timely directives to all financial institutions operating and conducting in all over the country.

After a long period, the second commercial bank namely Rastriya Banijya Bank (EBL) has been established in 2022 B.S. (1965 A.D.) with cent percent government ownership. This bank has been established under the Rastriya Banijya Bank Act 2021 B.S. (1964 A.D.) Both Nepal Bank Limited. (NBL) and Rastriya Banijya Bank (EBL) have made a remarkable contribution by providing reliable banking services to the Nepalese people. Its contribution is well noted in terms of capital formation to the small dispersed saving into meaningful capital investment in order to flourish industry, agriculture, and commercial sector in the country.

The government introduced Commercial Bank Act in Nepal in 2033 B.S. (1976 A.D.) to cover the vast field of financial sector. This act has helped to emerge number of commercial bank with a view to maintain economic interest in comfort of the public in

general facilitated to provide loan for agriculture, industry, trade and make a available banking services to the country and people.

Among vacuum in the banking sector got some rays of hope only when the government forwarded the economic liberalization policy in 2039 B.S. (1982 A.D.) and decided to allow foreign banks to operate their activities in Nepal in joint venture model. Joint Venture Banks can be defined as an association of two or more parties having common objectives and goals so as to get maximum satisfaction. Basically at that time, it was envisioned that joint venture banks (JVBs) would support the country in various ways.

In Nepalese context the main purpose of joint venture is top develop economic forces in order to achieve distinguished result, which the partners separately could not achieve. Nowadays, joint venture banks (JVBs) are playing dynamic and vital role in economic development of the country.

The EBL Bank Ltd. is the first joint venture bank established in 2041 B.S. (1984 A.D.) and started its operation with modern banking services. In the same way, Nepal Indosuez Bank (currently Nepal Investment Bank), the second joint venture bank established in 2042 B.S. (1985 A.D.) with an objective to encourage efficient banking services and facilities. Likewise Standard Chartered Bank is operated in 2044 B.S. (1987 A.D.).

With the satisfactory result of joint venture banks, Nepalese promoters are highly encouraged and as a result, commercial banks are introduced with cent percent domestic investment. At present, Nepal Industrial and Commercial Bank (NIC), Lumbini Bank Ltd., Machhapuchhre Bank Ltd., Bank of Kathmandu, Nepal Credit and Commerce Bank Ltd., Laxmi Bank Ltd., Siddhartha Bank Ltd., Kumari Bank Ltd. came into operation with cent percent domestic investment by Nepalese promoters which are the plus point of development of banking sector of Nepal. Now, there is a strong competition between commercial bank for the existence so that the growing needs of the customers can easily achieve.

2.1.3 Function of Commercial Banks

Banks can be defined according to the functions they perform. A bank is established with the prime objective of profit maximization. To achieve this, the bank carries out functional activities, principally, commercial banks accept deposits, provide loans, primarily to business firms thereby facilitating the transfer of funds in the economy. Although, in the yester years banks were viewed as acceptor of deposits then provider of loan, but modern commercial banks have to perform overall development of trade, commerce, industry, agriculture including supports for priority and deprived sectors. The growing bank needs and habits of people and competitive environment has made the banking sector challenging and their operation cannot be underemphasized in present context of market globalization. Hence, a bank is a commercial institution licensed as a taker of deposits, concerned mainly with the making and receiving payments on behalf of their customers, accepting deposits, creating money and making short-term loans to private individuals, companies and other organization.

Although profit maximization is a major objective of commercial bank, to achieve this objective commercial bank performs various functions under the mandatory rules and regulations and directives of NRB and the Commercial Bank Act 2031 B.S. (1974 A.D.).

Accepting Deposits: - Accepting a deposit is the most important function of commercial banks. Commercial banks collect money from those who want to deposit in different types of accounts such as:

- Fixed Deposit Account
- Current Deposit Account
- Saving Account

Advancing of Loans:- Commercial banks provide the loans required or credit to various sectors of economy such as industry, trade, agriculture, business-deprived sector etc. In this way bank creates credit facilities. It provides loans from various procedures in different form such as:

- Overdraft
- Cash Credit
- Direct loan with collateral
- Discounting of bills of exchange
- Loans of money at call and short notice

General Utility Functions: - Commercial banks also perform general utility functions such as:

- Issuing of letter of credit to its customers.
- Issuing of bank drafts and travelers cheque etc., for transfer of funds from one place to another.
- Dealing in foreign exchange and financing foreign trade by accepting or collecting foreign bills of exchange.
- Serving as referred to the financial standing and credit worthiness of its customers.
- Underwriting loans to be raised by public bodies and corporations. Providing safety vaults of lockers for the safe custody of valuables and securities of the customers.
- Acting as a trustee and executing the will of the deceased.
- Remittance of money

Agency Function: - Apart from the above functions, commercial banks also perform agency functions for which they act as agent and claim commission on some facilities such as:

- Collection of customer's money from other banks
- Receipt and payment of dividend, interest.
- Security brokerage service.
- Financial advisory service.
- To underwrite the government and private securities (Commercial Bank Act 2031 B.S. (1974 A.D.).

2.1.4 Role of Commercial Banks

The role of commercial bank in the economy is obviously a prime prerequisite for the formulation of the bank policy as the role shape, the nature and character of the bank. The deposit minded banker may under emphasize safety. Often commercial bank performs a number of interrelated functions. There are not only the custodians of the community's money but the suppliers of its liquidity. For these banks customer who seldom borrow from the bank an impartment function may be the acceptance and safe keeping of deposits. But those customers who often take loans from the bank, the credit creation function may be the most important. The commercial bank is different from the other banks especially from central bank. In appearance the main distinction between central bank and a commercial bank is that now- a- days the central bank does not do much banking, but the more fundamental difference is one of aim. The main objective of the commercial bank is to make profit where as the central bank thinks of the effects of its operations on the working of the economic system. The commercial bank has the shareholders and is expected to do the best it can for them but the government by contrast usually owns the central bank. The commercial bank may be few or many and they are to be found business with the general public all over the country. But, there is only one central bank in each country. Its market operations are mainly impersonal and are confined to what is necessary for influencing the country's financial business in the directions citrated by economic policy (Sayers, 1972:17-18).

For all countries of the world and more so far the developing countries like Nepal, fast economic development is one of the most important aspects of the developmental activities. However, it is obvious that unless the development of the most important sector like agriculture, industry, and commerce are achieved, evenomed development is impossible. For all the development, the regular supply of financial resources is a prerequisite. Finance is thus like fuel for providing energy to move the tempo of economic development and financial institution naturally, serve as reservoir for supplying and controlling the stream of that fuel i.e. finance. The commercial banks which are the financial institutions dealing with activities of agriculture industry, trade

and commerce play the most important role for the business activities of the world. The objectives of the commercial banks are to mobilize the idle resources in productive uses collecting them from scattered and various sources. Its role in economic development is thus immense in order to bring out greater mobility of resources to meet the ever increasing needs of financing of the various economic activities. ((Vaidya, 2001: 87).

Presently, the contribution of commercial banks and joint venture banks in agriculture sectors has been expanding. It provides the credit facilities for the development of agriculture on cases where Agricultural Development Banks and Cooperative Societies don't enter into the field. The agriculture sector needs more and more capital for the improved methods of farming viz. the fertilizers, equipment, irrigation facilities etc. require obviously more investment. Thus role of commercial bank in promoting agriculture sector is increasing in many of other countries, especially in developing countries like Nepal. The economy of our country is dominated by agricultural sector. This could be exemplified from the figures that about 73 percent of the total population is engaged on agriculture and about 35 percent of the national income comes from the agriculture. Similarly 51 percent of the export trade is in agricultural product. Also if we take into account of the major industries of Nepal, they are mainly based on agriculture. This is very clear that in such a country the financial help to the agriculture sector is most urgent and indispensable for strengthening the base of national economic structure.

The role of commercial bank is indispensable for industrial development of Nepal. Due to insufficiency of capital, industries are depending more and more upon the supply of capital by the banks. It wouldn't be exaggeration to state that commercial banks are mainly responsible for whatever the industrial development has been achieved by Nepal. However many other financial institutions like ADB/N, NIDC have already been established for the development of agriculture and industrial sector of the country. The commercial banks are also continuously participating in these activities. Being a mountainous country, many places are very remote and sometimes it requires many weeks to approach some of the places. Due to lack of transport and

communication facilities and other geographical causes, the country has been still facing the problem of imbalances economic growth. The scattered capital of the country is unable to solve the problem of imbalance of the economy growth. Commercial banks have their appropriate role to play here by expanding their branches in the different Hilly and Tarai regions available loan to the local people. In industrial sector, commercial banks are providing the necessary financial help for the industrial establishment in the country. They provide short and medium term loan to industries to purchase machineries, tools, raw materials etc. and to introduce new and developed techniques of production.

So the role of commercial banks is extremely important for the development of industries, trade commerce, agriculture, hotel, transport etc. of the country. In fact, no nation can develop itself without the development of these banks. It is not only true in the capitalist countries but also true in the socialist countries and mixed economic countries like Nepal as well. (Vaidya, 2001: 78).

There are several types of banks but among them commercial banks play significant contribution in the financial system of the country. They pool together the savings of the community and arrange for their productive use. They supply the financial needs of modern business by various means. They accept deposits from public on condition that they are repaid on demand or on short notice. Their business is confined to financing the short-term and medium term needs of trade and industry such as working capital financing.

2.1.5 Definition of Loan and Advances

Loan is defined as a thing that is lent to someone a sum of money. Likewise, debt means a sum of money owed to somebody. However, in financial terms loan or debt means principal or interest available to the borrower against the security. Debt means the money that bank owes or will lend to individual or person.

Likewise, the term loan is defined as a lending. Delivery by one party to and receipt by another party of sum of money upon agreement expressed to implied, to repay it with or without interest. Anything furnished for temporary use to a person at his

request on condition that it shall be returned, or its equivalent in kind, with or without compensation for its use. Loan includes:

- The creation of debt by lenders payment of or agreement to pay money to the debtor or to a third party for the account of the debtor.
- The creation of debt by a credit to an account with the lender upon which the debtor is entitled to draw immediately.
- The creation of debt pursuant to a lender credit card or similar arrangement.
- The forbearance of debt arising from a loan. (Albrol and Gupta, 1971:65).

Further, debt means Principal and interest provided to debtor by banks or financial institutions, with or without the pledge of immovable or moveable property of other securities of guarantees or without guarantee, and the word also mean over dues of the transactions beyond balance or fees, commission and interest incurred in that relation

The supreme court of India has defined the debt during the decision of the case of United Bank of India vs. DRT. Sudhir Gupta states that In the case in hand, there cannot be any dispute that the expression debt has to be given the widest amplitude to mean any liability which is alleged as dues from any person by a bank during the course of any business activities undertaken by the bank either in cash or otherwise, whether secured or unsecured, whether payable under a decree or other of any court or otherwise and legally recoverable on the date of the application. (Albrol and Gupta, 1971:65).

2.1.6 Concepts of Non Performing Assets

Non Performing Assets [NPA] means the amount of loan that the individual commercial bank had provided and the consumer has not paid it until the time is already matured. Once the distributed loan is not returned timely by clients and becomes overdue then, it is known as Non Performing Assets for the bank. Reduction of NPA has always been a significant problem for every commercial bank. NPA may be defined broadly as the Bad Debt; however, it in terms of banking sector consists of

those loans and advances which are not performing well and likely to be turn as bad debt. NPA as per the current directives of Nepal Rastra Bank, NRB, has been categorized as classified loans and advances. NPA has severe impacts on the financial institutions. On the one hand, the Investment becomes worthless as expected return cannot be realized and on the other, due to the provision required for the risk mitigation the profitability is directly affected. The existence of the bank can be questioned in this situation. Thus, interest along with principal has to be recovered timely and without any obstacles (K.C. 1978: 67).

To start with performance in terms of profitability in a benchmark for any business enterprises, including the banking industry, however increasing nonperforming assets have a direct impact on banks profitability as legally banks are not allowed to book income on such assets (Manamohan, 2002 : 06).

Loans and Advances dominate the assets side of balance sheet of any bank. Similarly, earning from such loans and advances occupy major space in income statement of the banks. However it is very important to be reminded that most of the bank failures in the world are due to shrinkage in the value of the loan and advances. Hence loan is known as risky assets. Risk of non-repayment of loan is known as credit risk or default risk. Performing loans have multiple benefits to the society while non-performing loans erodes even existing capital.

Performing assets are those loans that repay principal and interest to the bank from the cash flow it generates. Loans are risky assets, though a bank interest most of its resources in granting loans and advances. If an individual bank has around 10% non-performing assets or loans, it sounds the death knell of that bank other remaining the same. The objectives of bound loan policy are to maintain the financial health of the banks, which result in safety of depositor's money increases in the returns to the shareholders. Since the loan is a risky asset there is inherent risk in every loans, however, the bank should not take risk above the certain degree irrespective of the returns prospects.

2.1.7 Classification of NPA

As per the NRB directives NPA are said as classified loans. And this includes sub-standard, doubtful and loss categories as defined by new NRB directives. The circular further says a NPA is a credit facility in respect of which interest has remained unpaid for two quarters. According to the circulars, the loans are classified based on weakness and dependence on collateral securities into four categories and prescribed the provisioning rate as follows.

Table: 2.1
Classification of Loan and Advances

Classifications of loan and advances	Criteria for Provisioning	Provision
Pass	Not past due and past due for a period up to 3 Months. [Performing loans]	1%
Substandard	Past due for a period of 3 months to 6 months	25%
Doubtful	Past due for a period of 6 month to 1 years	50%
Bad Loan	Past due for a period of more than 1 years or Advances which have least possibility of	100%

Source: Nepal Rastra Bank, Directives for commercial banks.

2.1.8 Meaning of Profit

Profit, from Latin means “to make progress”. It is defined in various ways. In economics, profit is the concept of reward of the entrepreneur for risk taking and management. In business operations, it is the gain from manufacturing, merchandising and selling operations after all expenses are met. Since profit is added to net worth, it may be measured by the increase in net worth over that of the previous accounting period. The amount of concern’s profit thus may be determined not only through the profit and loss statement but also by the comparison of the earned surplus or net worth in the balance sheet which, however, is the residue of profits after dividends and any other appropriations and does not reveal details of sources of income and expenses, which are found in profit and loss account. In speculative transactions, profit is the

excess of the net selling price over the costs (including all charges) of the security or commodities traded in. (Woelfel, 1999 A.D., P.540)

Profit is a motivating factor behind many managerial activities. Much has been written about the role (as opposed to the method of calculation) of profit. Profit plays three roles in the capitalistic society. Profit is the financial reward of risk taking; profit is the financial reward for having monopoly power; profit is the financial reward for the efficient management. The promise of profit provides a strong incentive to owners and managers to act efficiently. "Profit is essential for every enterprise to survive in the long run as well as to maintain capital adequacy through retained earning. It is also necessary to accept market for both debts and equity to provide funds for increased assistance to the productive sectors." (Robinson, 1991: 22)

Account and economics are two disciplines in which profit is viewed in different concept. Pure economic profit is the increase in wealth that an investor has from making an investment, taking into consideration all costs associated with that investment including the opportunity cost of capital. Accounting profit is the difference between retail sales price and the costs of manufacture. A key difficulty in measuring either definition of profit is in defining costs. Accounting profit may be positive even in competitive equilibrium when pure economic profits are zero.

In economics, a firm is said to be making an economic profit when its revenue exceeds the total (opportunity) cost of its inputs. According to Adam Smith (The father of economics), Profit is the sum remaining after the payment of all wages (wage) in economics includes payments to officers of corporations, to proprietors, to partners and to farmers, as well as to what we today term(labor), and rent on the unimproved value of land, as the return to capital.

Profit in the accounting sense is the net figure of difference between all types of measurable revenues and all measurable costs. In accounting, profit is expressed only on explicit and measurable accounting terms and on the book value basis. However, in economics, profit is measured in the realizable terms. "Profit in the accounting sense is the excess of revenue receipts over the costs incurred in producing this revenue.

This concept of profit is also known as residual concept. But, in economics, both implicit and explicit costs are deducted from total sales revenue in determining profits. (Cauvery, 1997, 122-123)

As a matter of fact over the years there has been quite an evolution as to what particular items should be deducted from gross income to arrive at an “accounting” profit. Thus, “accounting” profit is a concept of man-made legislation, of the courts, of the Security of Exchange Commission, of accounting organizations; a concept, which has always been in evolution. “Economic” profit on the other hand, is a concept of a natural law of economics, and like the law of gravitation has remained and will remain unchanged over the ages. However, the profit under discussion is concerned with accounting profit, which in a simple language, is the positive and fruitful difference between two revenues and total expenses over a period of time, Multiple meaning of the word "profits" have always been troublesome. Accountants have made energetic efforts in recent years to discard the word for that purpose and to refer to the conventional concept as business income a natural term at avoids any overlap with economic theory. The most important points of difference between the economists and accountants are as follows:

- The inclusiveness of costs i.e. what should be subtracted from revenue to get profit.
- Meaning of depreciation
- The treatment of capital gains and losses
- The price level basis of valuation of assets and liabilities

Although there may be arguments in favor and against profit generating almost all firms require earning it. Their rate of earning differs from firm to firm and time to time.

2.1.9 Effects of NPA on Profitability of Banks

Under the circumstances assets that do not earn any income to the bank affect the profits in a number of ways, which are explained as follows (Pandey, 1999: 145).

Profitability Impact

The resources locked up in NPA are borrowed at a cost and have to earn a minimum returns to service this cost.

- NPA on the one hand do not earn any income but on the other hand drain the profits earned by performing assets through the claim on provisioning requirements.
- Since they do not earn interest they bring down the yield on advances and the net interest margin or spread.
- NPA have a direct impact on assets and returns on equity, the two main parameters for measuring profitability of the commercial banks.
- Return on assets will be affected because while the total assets include the NPA they do not contribute to profits which are the numerators in the ratio.
- Return on equity is also affected as provisioning eats more and more into profits Earned.
- The cost of maintaining these include administration costs, legal costs and cost of procuring the resources locked in them.
- NPA bring down the profits, affects the shareholders value and thus, adversely affect the investor confidence.

As a whole, the impact of NPA can be assessed with the following

- Lower ROE and ROA
- Lower image and rating of banks
- Disclosure reduces investor's confidences.
- Increases costs/difficulties in raising capital.

- NPA do not generate income.
- They require provisioning.
- Borrowing cost of resources locked in
- Opportunity loss due to non-recycling of funds.
- 100% risk weight on net NPA for CRR.
- Capital gets blocked in NPA.
- Utilizes capital but does not generate income to sustain the capital that is locked.
- Recapitalization by government comes with string.
- Administration and recovery costs of NPA.
- Effects in employee morale and decision. (Vaidya, 2001:65).

2.1.10 Causes and Measures of NPA in Different Countries

In China

Causes

- Moral Hazard: The SOEs believe that there the government will bail them out in case of trouble and so they contribute to take high risks and have not really strived to achieve profitability and to improve operational efficiency.
- Bankruptcy laws favors borrowers and law courts are not reliable enforcement vehicles.
- Political and social implications of restructuring bi SOEs force the government to keep them afloat.
- Banks are reluctant to lend to the private enterprises due to
- Non- standard accounting practices.
- While an NPA of an SOE is financially undesirable, an NPA of a private enterprise is both financially and politically undesirable.

Measures

- Reducing risk by strengthening banks, raising disclosure standards and spearheading reforms of the SOEs by reducing their level of debt.
- Laws were passed allowing the creation of asset management companies, foreign equity participation in securitization and asset-backed securitization.
- The government, which bore the financial loss of debt discounting. Debt/equity swaps were allowed in case a growth opportunity existed.
- Incentives like tax breaks, exemption from administration fees and clear-cut asset evaluation norms were implemented. (Robinson, 1951:89)

Thailand

Causes

- Liberalized capital and current account and external borrowings with inaccurate assessment of exchange rate risk and risk of capital flight in a crisis.
- A legal system that made credit recovery time consuming and difficult.
- Real estate speculators took massive loans projecting high growth in demand and prices of properties. When this did not materialize all the loans went bad.
- Steep interest rate rise turned a lot of loans into NPAs
- Inability to correctly assess credit risk.

Measures

- Amendments were made to the Bankruptcy Act.
- Corporate Debt Restructuring Plan (1998) focused on capital support facilities for bank recapitalization and setting up of AMCs.

- New rules governing NPA exit procedures based on international standards were introduced.
- Privatization of government entities was mooted, but faced strong political oppositions for fear of a social backlash.
- Adoption of international standards for loan classification and provisioning.
- Caps on Foreign equity ownership in financial institutions were removed.

Korea

Causes

- Directed Credit: Protracted periods of interest rate control and selective credit allocations gave rise to an inefficient distribution of funds. The Chapbooks focus on increasing market share and pursuing diversification with little attention to profitability caused tremendous stress on the economy.
- The compressed growth policy via aggressive, leveraged expansion worked well as long as the economy was growing and the ROI exceeded the cost of capital. This strategy backfired when slowing demand and rising input costs placed severe stress on their profitability.
- Lack of Monitoring-Banks relied on collaterals and guaranteed in the allocation of credit, and little attention was paid to earnings performance and cash flows.
- Contagion effect from South East Asia coincided with a period of structural adjustments as well as a cyclical downtime in Korea.

Measures

- Speed of action:- the speedy containment of systemic risk and the domestic credit crunch problem with the injection of large public funds for bank recapitalization were critical steps towards normalizing the financial system.

- Corporate Restructuring Vehicles (CRVs) and debt/equity swaps were used to facilitate the resolution of bad loans.
- Creation of the Korea Asset Management Corporation (KAMCO) and a NPA fund to fund to finance the purchase of NPAs.
- Securitization KAMCOs recoveries came through asset-backed securitization and outright sales. International investors like the Lone Star Fund participated in the process.
- Strengthening of Provision norms and loan classification standards based on forward-looking criteria (like future cash flow) were implemented.
- The objective of the central bank was solely defined as maintaining price stability. The Financial Supervisory Commission (FSC) was created (1998) to ensure an effective supervisory system in line with universal banking practices.

Japan

Causes

- Investments were made Real Estate at high prices during the boom. The recession caused prices to crash and turned a lot of these loans bad.
- Legal mechanisms to dispose bad loans were time consuming and expensive and NPAs remained on the balance sheet.
- Expansionary fiscal policy measures administered to stimulate the economy supported industrial sectors like construction and real estate, which may have further exacerbated the problem.
- Weak corporate governance coupled with a non-bankruptcy doctrine was a moral hazard in Japanese economy.
- Inadequate accounting systems and information flow makes assessment of loan performance outside a bank in Japan difficult.

Measures

- Amendment of foreign exchange control law (1997) and the threat of suspension of banking business in case of failure to satisfy the capital adequacy ratio prescribed. Legislation to improve information flow has been passed.
- Accounting standards: Major business groups established a private standard setting vehicle for Japanese accounting standards (2001) in line with international standards.
- Government Supports: The government's committee public funds to deal with banking sector weakness.

2.2 Reviews of NRB Directive

Banks and Financial Institutions Regulation Department NRB (Directive No. 2/070)“*Provisions Relating to Classification of Loans/advances and Loan Losses*” having exercised the powers conferred by Section 79 of the Nepal Rastra Bank Act, 2002, the following Directives have been issued with regard to classification of credit/advances and provisions to be made for its possible loss by the institutions obtaining licenses from this Bank to carry out financial transactions.

1. Classification of loans/advances

Entire loans and advances extended by a licensed institution have to be classified as follows based on expiry of the deadline of repayment of the principal and interest of such loans/advances:-

- a. Pass: Loans/advances which have not overdue and which are overdue by a period up to three months.
- b. Sub-standard: Loans/advances which are overdue by a period from three months to a maximum period of six months.
- c. Doubtful: Loans/advances which are overdue by a period from six-months to a maximum period of one year.

- d. Loss: Loans/advances which are overdue by a period of more than one year.

The loans which are in pass class and which have been rescheduled/restructured are called as "the performing loan, and the sub-standard, doubtful and loss categories are called non-performing loans.

(Note: Loans/advances also include bills purchased and discounted.)

2. Additional provisions relating to pass loans

The following loans may be included in the pass loan:-

- a. Loans/advances extended against the collateral of gold and silver;
- b. Loans/advances of fixed receipts
- c. Loans/advances of Government of Nepal securities and loans/advances made against the collateral of Nepal Rastra Bank bonds;

Provided that the cases of the loans/advances against the fixed receipts or Government of Nepal securities or Nepal Rastra Bank bond as the additional collateral, such loans and advances shall also have to be classified in accordance with the directive referred to into Point No. 1 above.

The working capital loan having the deadline of up to one year for repayment may be included in the pass loan class. In case the interest to be received from the loans of working capital nature is not regular, such loans have to be classified on the basis of the duration of interest to be due.

3. Additional Provisions Relating to Loss Loans

In case there seems any of the following discrepancies in any of the following loans, whether or not the deadline for repayment of which is expired, such loans and advances has to be categorized as the loss loan:

- a. The market price of the collateral cannot secure the loans;
- b. The debtor is bankrupt or has been declared to be bankrupt;

- c. The debtor disappears or is not identified;
- d. In case non-fund based facilities such as purchased or discounted bills and L/C and guarantee which have been converted into fund-based loan, are not recovered within ninety days from the date of their conversion into loan;
- e. Loan is misused;
- f. Expiry of six months of the date of auction process after the loan could not be recovered or a case is pending at a court under the recovery process;
- g. Providing loan to a debtor who has been enlisted in the black-list of Credit Information Bureau Ltd;
- h. The Project/business is not in a condition to be operated or project or business is not in operation
- i. The credit card loan is not written off within 90 days from the date of expiry of the deadline;
- j. While converting the L/C, guarantee and other possible liabilities into a fund-based loan under the regular process, if the said loan is not recovered within 90 days; and
- k. In case of expiry of the deadline of a trust-receipt loan.

(Note: For the purpose of clause No. 3(e) of these Directives, "misuse" means non-use of the amount of the loan for the purpose for which it has been taken; the project is not in operation; the amount accrued from the concerned project or business is not used in repayment of the loan but in other activities; and the word also includes the loan which is proved to have been misused by a supervisor in the course of inspection or supervision or by an auditor in the course of auditing.)

4. Additional Provisions Relating to Term-Loan

In cases of the term loans extended in installments, if the deadline of installment of the principal amount expires, remaining entire loan amount has to be classified based on

expiry of the deadline of the installment amount. Provided that in cases of the installment of the term loan given by licensed institution not having the facility of engaging in overdraft transaction, entire loan amount has to be categorized as loss loan only if the installment amount has crossed the deadline by a period of more than one year. In case the installment amount has crossed the deadline by a period of less than one year, only such installment amount has to be classified in the loss loan with a provision of loan loss. However, this clause shall not be deemed to have hindered if the licensed institution wants to classify the entire loan amount as the loss loan.

(Note: For the purpose of this clause "term loan" means a credit/advances made available having fixed the repayment period of more than one year.)

6. Principal and Interest not allowed to be recovered crossing the overdraft limit

Principal and interests of a loan shall not be allowed to be recovered having overdrawn the current account of a customer so that the overdraft limit is crossed. Provided that this provision shall not be deemed to prohibit to recover the principal and interest having debited the balance in an account of the customer. In case the account is not settled by a period of one month after overdrawn of the account while recovering principal and interest by debiting the account of the customer, the amount overdrawn shall also be included in the loans not recovered and such loans have to be classified in one class lower than the class to which such loans belongs. While debiting the account, overdraft shall not be allowed by crossing the limit provided to the customer.

7. Provisions Relating to Grace Period

Licensed institution shall not normally be allowed to make available term loans with grace period of more than one year. In case longer grace period has to be provided, the reasons for and bases on which such longer period has to be granted, such details shall have to be disclosed and it shall have to be approved by the Board of Directors at the time of approval of the loan.

9. Provision to be maintained for loan loss

For the loans and bills purchase classified according to these Directives, the following loan loss provision shall be maintained based on the remaining amount of principal: loan classification Minimum Provision for loan loss

- a. Pass 1 percent
- b. Sub-standard 25 percent
- c. Doubtful 50 percent
- d. Loss loan/the loan extended to blacklisted 100 percent persons, firms, company or corporate body Provided that in case of the insured loans, it would be required to make provision of only 25 percent of the provision referred to in sub-clause (1)

2.3 Review of Journals/Articles

Pradhan, (2005) in his article '*NPA Some Suggestion to Tackle them Expressed that Unless the Growth of NPA' is Kept in Control*, in journal it has the potential to cause systematic crisis. He has mentioned that a dream of globalization led to huge investment which unfortunately could not be utilized properly due to hesitant liberalization policies. Large corporate bodies misused the credits and delayed payments and contributed indirectly for enhancing NPA ratio. He further argues that lack of vision in appraisal of proposal while loan sanctioning, reviewing or enhancing credit limits, absence of risk management policy of financing, concentration of credit in few group of parties and sector, lack of coordination among various financiers, lack of initiatives to take timely action against willful defaulters, indecision on existing out of bad loans for fear of investigating agencies like special policy, CIAA, Public Accounts Committee of the parliament have also contributed in whatsoever measures to the worsening situation of NPA front. He further pointed out that most crucial reason for the increase in the NPA is the shabby and defaulter friendly legal system. Suggesting the remedy of NPA, he adds that administrative system should be strengthened. Legal reforms should be made and Assets Reconstruction Company

should be formed. Henderson (2003) CEO of RBB during his interview to New Business Age agrees that the challenging target of RBB turn around in restructuring and collection of NPA.

Basyal, (2006) in the article '*Financial Performance of Commercial Bank*' discussing the financial performance of government owned banks in the article, Placing RBB and NBL under Management Contracts Rational and Opposition agreed that the disappointing performance of these two banks has become serious concern to

all the stakeholders. Further he mentions that they are having with huge level of NPA, which could be termed as the darkest sides of their operational inefficiency and undisciplined financial behavior.

Dhugna, (2007) in his article '*Why Assets Management Co. is considered the Best to Solve the Non-Performing Loan Problem*' as above has tried to highlight one of the approach mainly Assets Management Company (AMC) for resolving the problem of NPL. As per him, AMC is specialize financial intermediary to manage the non-performing and distress loans of banks and financial institutions who buy the NPL from financial institution and take necessary steps to recover the maximum value from the acquired assets. As per his view, if NPLs are not resolved in time there would be inherent direct or indirect costs to the economy. As stated by him NPL may arise due to the external factors like decrease in market value of collateral deterioration borrower's repayment capacity, economic slowdown, borrower's misconduct, improper credit appraisal system, lack of risk management practice, ineffective credit monitoring and supervision system. Hence he suggested that, NPL should be kept at minimum level and the specialized institution such as AMCs should manage the distressed loans.

He says that both traditional approach and AMC are available to deal with NPL problem. Under traditional approach, bank handles the NPLs in its own way especially through recovery unit who focus on continuing negotiation with the borrower and give top priority to the loan recovery. As opined by the writer, this approach is useful in dealing with small business loans where personal touch is adopted but for big loan this

approach does not work. AMCs seem as the only realistic option when the financial sector recovery is the underlying objective in financial system where the institution fails to resolve the NPL problem through their own efforts.

He stated that the main advantage of establishing AMC is that AMC is able to move in an expeditious manner removing the distraction of managing NPLs from the banking system and frees up resources within the financial institution allowing them to concentrate on their core activities.

He concludes, "As in most of the countries, Nepalese Financial System is largely dominated by the banking sector. The banking sector is severely affected by the NPL problem, it is estimated that the NPL of the Nepalese Banking system is around 16%. Therefore there is no doubt that it has serious implication on the economic performance of the country. It will be the eclipse in the development of financial soundness in the economy, if not controlled in time. However, traditional or AMC route can be practiced to get recovery from this sickness of the financial system, the AMC route may be more effective approach to be quick recovery as it has been experience around the world."

Rawal, (2007) in the article *'Measures Adopted to Overcome the Problem of Financial Sector and the NPL'* addressed that financial sector reform measures can be broadly grouped under three heads: (i) restructuring of large two state-owned banks (ii) reengineering of the central banks and (iii) capacity building in the financial sector. In this connection, management of two state-owned banks has been handed over to the expert groups comprising the people within and outside of Nepal; the reengineering and restructuring process of the central bank (Nepal Rastra Bank) is in progress. Side by side, the capacity building in the financial sector is smoothly approaching ahead. Enactment of new NRB Act 2002 which, gives greater autonomy in its operation, enforcement of inspection and supervision directives based on international standard, withdrawal of government/ NRB involvement from the financial institutions, adoption of accommodative monetary measures are the efforts made to build up sound financial environment. Moreover, with a view to strengthening legal arrangements, Debt Recovery Act has been approved and the

Debt consolidate financial sector through an umbrella act Banks and Financial Institutions Act has recently been approved and for the purpose to resolve the problem of non-performing assets- Asset Management Company Act is in the process of being approved. In addition, establishment of Credit Rating Company, strengthening of Credit Bureau and Bankers' Training Center are some of the tasks progressing ahead. With the arrangement of such a legislative, regulatory, supervisory and institutional framework, the financial sector would, hopefully, take a pace for reviving which, in turn, would help NPLs to be reduced.

Sapkota, (2008) has written an article titled '*Portion of NPA in Commercial Banks – High in Public, Low in Private*' which was published in Rajdhani on 19th May 2004. In this article, Mr. Sapkota has stated that the problem of NPL is seen less in private banks in comparison to public banks. The NPA of two big nationalized banks being about 60% of the total loans are very serious situation. He further mentioned that in order to improve this situation and to make healthy banking environment, financial reform program has been brought as its consequences, the management of two big banks was handed to foreign company on a contract but the ratio of NPL was not reduced.

Even most of the privately owned banks has NPA within international standard, some privately owned bank's NPA is higher than international standard. As per international standard 5% NPA is acceptable. He also states that, Nepal's total NPA of banking sector is 30%, which is very high.

Adhikari, (2009) in the article '*Non-performing Loan and its Management*' states in articles that one of the main functions of commercial bank is to management of non-performing loan. Main function of commercial bank and financial institution is accepting deposit and provide loan. In underdeveloped country like Nepal providing Loan and interest income generating through loan is the main source of bank and financial institution. If provided loan become non-performing loan the bank and financial institution suffer from big financial scarcity. One side un-recover interest cannot make income and other side loan itself converts in NPL that make huge effect in financial condition of bank and financial institution. So management of NPL is

crucial factor for any bank and financial institution. In practical, there may be default rate in aggregate banking system. Two commercial banks hold by gvt. Nepal Bank Ltd. and Rastriya Banijya Bank are accounting for the highest number and amount of non-performing assets (NPA) among the other commercial banks.

The main causes of being loan become non performing loan are as follows

- Lack of proper analysis
- Lack of specific loan policy
- Lack of supervision
- slump on aggregate economy
- monopoly on corporate loan and its unsuccessful
- weak in consortium loan
- less responsibility of borrower
- Inadequate in internal Control and Audit
- Inadequate in supervision of Central bank

In this way NPA generate in bank and financial institution. In every Banking s system there is some level of non-performing loan. So, it should be managed differently. Bank manages their loan and credit if nonperforming loans are at acceptable level. But, if bank's NPL are more than acceptable level then is impacts on aggregate financial position of bank and market like be worse. In this case bank should manage and treat its NPL differently. A single unit with expert should be assign for proper and appropriate management of huge amount of non-performing loan. For better management of nonperforming loan assets Management Company or corporation (AMC) is required. Proper management of nonperforming loan and recapitalization, these two important improvements are required for better banking system.

Regmi, (2013) in the article titled '*Non-Performing Assets Management*' the writer stated about the management of NPAs in the commercial banks. He writes, the NPAs includes the non-performing loan, non-banking assets, remaining non-performing loan, suspend interest and unutilized assets. The increasing NPA are the emerging problem in commercial banks, which is the main factor for failure of the banks.

He said, NPAs caused by investment of assets in non-productive sectors, lack of future prediction, lack of proper supervision, monitor, control lack of information and failure of recovery of loan and their interest on time. He also added, the low quality of collateral of loans, failure of projects, and lack of appropriate rules and regulations to punished the bad loan takers. He shows the following NPAs in commercial banks: He added that increasing NPAs directly affects to the banks, investors and human resources. Not only that but also it affects the customer, economy of country, and business activities. Increasing NPA has two types of impact on banks: internal impact and external impact. In internal, it affects directly on profitability and human resources and in external, it affects to customers, investors, management and country's economy.

He concludes that it is high level of NPA like a cancer of banks. Thus, it is necessary to control this cancer on time; otherwise, it becomes a big issue for bankruptcy. NPA have to need microanalysis to protect the banks, investors, customers, human resources and country's economy. For that, a clear 'Road Map' is required. To success the laws and policies, all the stakeholders should take responsibilities.

As the banks experience many difficulties in recovering the loans and advances their large amount is being blocked as non-performing assets. She suggested that there is an urgent need to work out a suitable mechanism through which the overdue loan can be realized.

2.4 Review of Related Thesis

Ghimire, (2006) entitled with '*Non- performing Assets of commercial Banks: cause d and effects*' has following facts and findings.

Objectives;

- To analyze the cause and effects of nonperforming assets in commercial bank.
- To evaluate the impacts of NPA on the profitability of commercial bank.
- To analyze the level of NPA selected commercial banks.

Major findings;

- Nonperforming Assets on overall profitability of the banks tend to have inverse relationship. Profitability of the bank tends to have inverse relationship. Profitability is affected due to provision requirement.
- There is some relationship between credit extend and increment on nonperforming assets.
- It may be significant in case of aggressive credit expansion. Findings showed that Non Banking Assets is credited due to having Nonperforming Assets.

Paudyal, (2007) entitled with, *A study of Non- performing Assets of Commercial Banks of Nepal*, has following facts and findings.

Objectives;

- To find out the proportion of nonperforming loan in the selected commercial banks.
- To evaluate the impact of NPA on the profitability of the commercial banks under the study.
- To analyze the impact of NPA on ROA and ROE of the commercial banks under the study.

Major findings;

- In recent years NABIL Banks has shown significant decrease in Non Performing Assets, which is the result of banks effective credit management and its efforts in recovering bad debts through establishment of recovery cell.
- High degree of negative correlation exists between NPA and ROE of NABIL Bank. The bank should reduce their level of NPA to increase ROE and ROA and Profitability.
- Loan loss provision for Doubtful loan seems to be higher in case of both bank NABIL and SCBNL.

Baral, (2008) entitled with '*A study of Non- performing Loans of Nepalese commercial Banks*' has following facts and findings.

Main Objectives;

- To find out problems of the non performing loans and its effects in ROA and ROE of the Nepalese commercial banks.
- To examine whether the Nepalese commercial banks are following the NRB directives regarding loan loss provision for non performing loan or not.

Major findings;

- The return on assets (ROA) and Return on equity (ROE) of the bank somehow depend upon Non Performing Loan. The bank should reduce its NPLs to increase ROA and ROE of the bank.
- Management inefficiency is one of major cause behind high level of NPA of commercial banks.
- No banks have been following NRB directives regarding loan loss provision.

Shrestha, (2010) entitled '*A study of Non- performing Loan and Loan Loss Provision of Commercial Banks A Case Study of NIBL, HBL and EBL*' the objectives of his studies are;

- To find out the proportion of nonperforming loan in the selected commercial banks.
- To study and analyze the guidelines and provisions pertaining to loan classification and loan loss provisioning.
- To find out the relationship between loan and loan loss provision in the selected commercial bank.
- To study and the impact of loan loss provision on the profitability of the commercial banks.

Major findings;

- The EBL has the highest portion of the loan in total asset followed by NIBL and HBL. He concludes that the EBL shows the risk adverse attitude.
- Likewise the nonperforming loan to the total loan is found in HBL, NIBL and EBL.
- The loan loss provision is also highest in HBL where as the EBL has the least Loan Loss Provision.
- The HBL has the highest portion of loss loan followed by NIBL and EBL.

Khadka, (2011) entitled with '*Non- performing Assets of Nepalese Commercial Banks*' has following facts and findings.

Objectives

- To analyze the non performing assets of the commercial Banks.
- To examine the level of NPAs in total assets, total deposits and lending of commercial banks.
- To examine whether the Nepalese commercial banks are following the NRB directives regarding nonperforming assets or not.

Major findings

- The level of NPA of Nepal Bangladesh Banks limited seemed greater than all of the other banks under the study .similarly, Nepal SBI Banks and Bank of Kathmandu stands at second and third position respectively.
- The position of NABIL Bank Limited seemed to be quite satisfactory because the bank has been reducing its NPA every year and NPA of Nepal Investment Bank has been reducing it at minimum than that of all the other banks.
- It is found that none of the banks have been following the directives of NRB regarding the loan loss provision.

Poudel, (2012) entitled with '*Comparative Financial Performance Appraisal of Joint Venture Banks*' with references to Everest bank limited and Nepal Arab Bank Ltd

His Main Objectives are as follows

- To analyzed relations between different ratios.
- To examine the proportion of Comparative financial performance appraisal of joint venture banks
- To give suggestions and recommendations for the betterment of commercials banks.

His Major Findings are as follows

- His study especially concentrated on the deposit collection of the bank and disbursement of the fund as loan and advances.
- He has focused on utilization and mobilization of funds and resources of Nepal Bank Ltd.
- He recommended that the bank should try to mobilize its resources efficiently by creating new business
- Service ideas which will certainly help for the better utilization of ideal resources and for the economic development of the country.

Adhikari (2013) in his study entitled '*Evaluating the Financial Performance of Nepal Bank Limited*' has calculated and analyzed the different ratios by observing figures of balance sheets of Nepal Bank Limited.

His Main Objectives are as follows:

- To examine the Evaluating the financial performance of Nepal Bank Limited
- To calculated and analyzed the financial and statistical tools by using

His Major findings are as follows:

- The collection of deposit and loan investment done by the commercial banks also to sustain themselves in the environment of competitions.
- The deposit funds in productive sectors and to grants more priority to the local manpower.
- Economic development of a country cannot be imagined without the development of commerce and industry
- He has focused on utilization and mobilization of funds and resources of Nepal Bank Ltd.

2.5 Research Gap

From the study of previous thesis it has found that increasing Non-performing assets is one of the major challenges faced by Nepalese commercial banks in the present context. Some researchers were done in which matter relating to loan loss provision for Non-performing assets or not. Some researcher was done what is the internal and external factors affects the Non performing assets to increase from the loan advances. The previous theses covered only up to the fiscal year 2010/11 but this thesis also based on secondary data provided by concerned Nepalese commercial banks up to the fiscal year 2012/13.

Hence this thesis had attempted to fill this research gap by taking the reference of Nepal Investment Bank and Kumari Bank Limited. This research will be able to deliver some of the present issue, latest information and data relating to Non-performing assets.

CHAPTER-III

RESEARCH METHODOLOGY

Research methodology is the way to solve systematically about the research problem. It is composed of two words, search and methodology which means the process of investigating in values a series of well thought and activates in gathering, recording, analyzing and interpreting the data with the purpose of finding answers to the problem. The entire process by which we attempt to solve the problem is called research while methodology is the method used to list the hypothesis.

Advanced learner's Dictionary of current English defined research as "a careful investigation or inquiry especially through search for new facts in any branch of knowledge". Research is a systematic inquiry of any particular topic and methodology is the method of doing research in well manner. Thus research methodology is a way to solve the problem systematically. It is understood as a science of studying how research is done scientifically. It is analysis of specific topic by a proper method. "Research may be defined as the systematic method of discovering new facts or verifying old facts, their sequences, interrelationship causal explanation and the natural laws which govern them" (Young 1989: 67).

3.1 Research Design

A research design is the arrangement of conditions for collection and analysis of data that aim to combine relevance to the research purpose with economy in procedure. Research design in the plan, structure and strategy of investigation conceived so as to obtain answers to research questions and to objective of this study. To achieve the objective of this study, descriptive and analytical research design has been used. It is the process which gives us an appropriate way to reach research goal. It includes definite procedures and techniques which guide in sufficient way for analyzing and evaluating the study. This study is carried out by using both quantitative and qualitative analysis methods. Mostly, secondary data has been used for analysis, but the discussion and personal interview with the concerned employees of the selected

banks are also used for qualitative analysis. Hence, research design of this study is based on descriptive and analytical method.

3.2 Populations and Sample

The term population for research means all the members or any well defined class of people, event or object. It means that the entire group of people, events or things of interest that a researcher wishes to investigate. A sample is a collection of items or elements from population or universe. Hence, a sample is only a portion or subset of the universe or population. It comprises some observations selected from the population. Sampling may be defined as the selection of some part of an aggregate or totality on the basis of which judgment or inference about the aggregate or totality is made.

The population of the present study is listed as under, the commercial banks operating in banking industry of Nepal.

As this study is about non-performing loans and profitability of commercial banks, all 30 commercial banks of Nepal is taken into account as population and out of the total population two following commercial banks are selected as sample for this study.

- Nepal Investment Bank Limited
- Kumari Bank Limited

3.3 Data Collection Techniques

Data are collected from various sources were in raw form, which are included the annual financial report of concerned banks, the related publications of NRB and relevant websites of concerned banks. Data are collected using both primary and secondary data. Primary data have been obtained through field visit and telephone inquiries. While secondary data are collected through the annual reports of concerned banks which were collected from concerned banks and other reports were downloaded from websites. Various publications of NRB were collected from concerned department of NRB. Various reports, textbooks, journals and unpublished dissertation have been used for analysis.

3.4 Data Analysis Tools

The data collected from different sources are recorded systematically and identified after collection of research data, an analysis of data and interpretation result are necessary. Applying different financial and statistical tool made data analysis. Further to represent the data in simple form bar diagram and graphs have also been used.

3.4.1 Financial Tools

While adopting financial tools, a ratio is used as a barrack for evaluating the financial position and performance to any firm. Financial analysis is the process of identifying the financial strength and weakness of balance sheet and profit and loss account (Pandey, 1999: 108).

Financial analysis's the use of financial statement to analyze a company's financial position and performance (Wild, Stemma & Halsey, 2003).

Ratio Analysis

Ratio analysis is a tool for scanning the financial statement of the firm. A ratio analysis is the widely used tool of financial analysis. A ratio is simply one number expressed in terms of another and as such it expresses the numerical or quantitative relationship between two variables. Ratio analysis reflects the relative strengths and weakness of any organization and also indicates the operating and financial growth of the organization.

Ratio helps to summarize large quantities of financial data and to make quantitative judgment about the firm's financial performance. The relationship between two accounting figure expressed mathematically is known as financial ratio. Even though there are many ratio, only these ratios have been calculated which are related to the subject matter. Following ratios have been computed and analyzed in this study (Pandey, 1999 p.10).

- **NPA to Total Lending Ratio**

This ratio determines the proportion of nonperforming assets to total lending of the bank. Higher ratio indicates bad effect and decrease in the profitability of the bank and lower ratio indicates better performance and increase in the profitability. It is calculated as under:

$$\text{NPA to total lending ratio} = \frac{\text{NPA}}{\text{Toal lending}}$$

- **NPA to Total Deposit Ratio**

This ratio determines the proportion of NPA to total deposit. Loans and advances yield high rate of return but liquidity requirements also needs due consideration. Lower ratio implies the better utilization of total deposits and better earning. This ratio is calculated as follows.

$$\text{NPA to total deposit ratio} = \frac{\text{NPA}}{\text{Total deposit}}$$

- **NPA to Total Assets Ratio**

This ratio determines the proportion of NPA to total assets. Lower the ratio indicates the better performance of the bank and higher the ratio indicates low performance of the bank. It is calculated as under.

$$\text{NPA to total assets ratio} = \frac{\text{NPA}}{\text{Total Assets}}$$

3.4.2 Statistical Tools

Statistical tools are used to analyze the relationship between two or more variables and to find how these variables are related. In this study, following statistical tools are used.

- **Arithmetic Mean or Average**

The mean or average value is a single value within the range of the data that is used to represent all the values in the series. Since an average is somewhere within the range of the data, it is also called a measure of central value. It is calculated by;

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

Where,

$$\bar{X} = \text{Arithmetic Mean}$$

$$\sum X = \text{Sum of values of all items, and,}$$

$$N = \text{Number of items}$$

- **Standard Deviation**

The standard deviation is the measure that is most often used to describe variability in data distributions. It can be thought of as a rough measure of the average amount by which observations deviate on either side of the mean. Denoted by Greek letter's (read as sigma), standard deviation is extremely useful for judging the representatives of the mean. Standard deviation is calculated as;

$$\text{Standard deviation } (\sigma) = \sqrt{\frac{1}{n} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]}$$

Where,

$$\sigma = \text{Standard deviation}$$

$$\sum X^2 = \text{Sum of square of the variables}$$

$$(\sum X)^2 = \text{Square of the sum of x variables}$$

$$n = \text{Number of items}$$

- **Coefficient of Correlation**

Correlation is a statistical tool design to measure the degree of association between two or more variables. In other word if the changes in one variable affects the changes in other variable, then the variable are said to be co-related when it is used to measure the relationship between two variables, then it is called simple correlation. The coefficient of correlation measures the degree of relationship between two sets of

figures. Among the various methods of finding out coefficient of correlation, Karl Pearson's method is applied in the study. The result of coefficient of correlation is always lie between +1 and -1. The formula for the calculation of coefficient of correlation between X and Y is given below.

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2 \times n \sum Y^2 - (\sum Y)^2}}$$

Where,

r_{xy}	=	Correlation between X & Y variables
$\sum XY$	=	Sum of Multiply of Variables X & Y
$\sum X$	=	Sum of Variables X
$\sum Y$	=	Sum of Variables Y
$\sum X^2$	=	Sum of Square of Variables X
$\sum Y^2$	=	Sum of Square of Variables Y

- **Assessment of the Sample Correlation Coefficient (t-test)**

For this study, t-test for significance of an observed and sample correlation coefficient is used.

Set up Hypothesis

Null hypothesis (H_0); $\rho = 0$ i.e. There is no correlation between the considered variables.

Alternative Hypothesis (H_1); $\rho \neq 0$ i.e. There is significant correlation between the considered variables.

Test statistic under H_0 ;

$$t = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2}$$

Where,

r	=	Sample correlation between two variables
r^2	=	Sample correlation Coefficient
n	=	No of Pair of observations

Level of significance: Level of significance $\alpha = 5\%$

Critical Value: Tabulated or critical value of t at α % level of significance for $(n - 2)$ degree of freedom obtain from 't' tables.

Decision: If calculated 't' is less than or equal to tabulated value of 't' it falls in the accepted region and the null hypothesis is accepted and if calculated 't' is greater than tabulated 't' null hypothesis is rejected.

CHAPTER IV

PRESENTATION AND ANALYSIS OF DATA

Presentation and analysis of data is the main body of the study. In this chapter collected data are analyzed and interpreted as per the stated methodology in the previous chapter.

According to that provision, every bank has to classify its total loan and advances (including purchased and discounted bills) as pass loan, substandard loan, doubtful loan and bad loan, on the basis of overdue against schedule. Commercial banks are also directed to maintain loan loss provision as stated in section 11 of directives no. 2 of NRB directives for commercial banks 2059. Main purpose was to find out the level of NPA in Nepalese commercial banks and to take necessary steps to control the level of NPA in future. In this study the data of five fiscal year from F/Y 2008/09 to 2012/13 have been presented and analyze the level of NPA in total assets, total lending and total deposits of the commercial banks. Data are also presented to examine or analyze the efforts to NPA on the profitability of the banks under study.

4.1 Analysis of Individual Commercial Banks

Nowadays Non-Performing Assets (NPA) have been occupying major space in the total assets and total lending of the bank. Commercial banks have been suffering by high level of NPA, and the efforts of the banks have been diverted to reduce it.

Two commercial banks are taken as sample for study. Every sample banks desired variables are analyzed properly. In this analysis, it is attempted to find out periodical NPA and profitability of commercial banks in Nepal and the impact of NPA on profitability is analyzed properly. Each sample Banks and their details have been introduces below.

4.1.1 Kumari Bank Limited (KBL)

Table: 4.1

Total Assets, Total Deposits, Total Lending and Total NPA of KBL

Rs. In Million

Fiscal Year	Total Asset	Total Deposit	Total Lending	Total NPA
2008/09	18538	15710	14593	64
2009/010	20522	17432	14765	75
2010/011	20491	16986	14626	167
2011/012	25131	21985	17614	399
2012/013	28222	25318	19369	776
Mean	22581	19486	16193	296
SD	3977	4031	2189	300
CV	18	21	14	101

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.1

Total Assets, Total Deposits, Total Lending of KBL

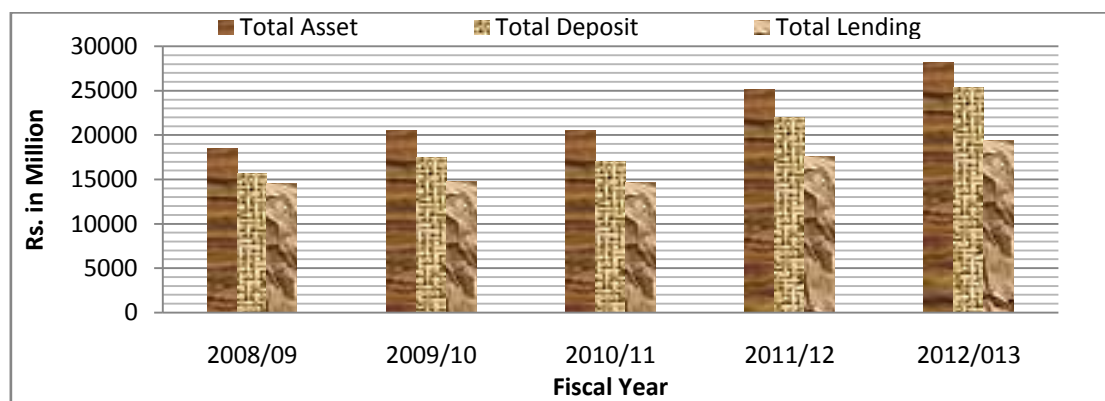


Table 4.1 and Figure 4.1 shows that the total assets, deposit, lending and NPA of KBL. During the study period of five fiscal year total assets is increasing each fiscal year than previous except the fiscal year 2010/011. The average total asset of fiscal year is Rs.22581 million, standard deviation is Rs. 3977 million and coefficient of variation is 18%. Total deposit is increasing each year than previous year except the fiscal year 2010/011, average deposit is Rs. 19468 million, standard deviation is Rs. 4031 million and coefficient of variation is 21%. Total lending is increasing each year

than previous year except the fiscal year 2010/011. The average lending is Rs. 16193, standard deviation is Rs. 2189 and coefficient of variation is 14%. Similarly, NPA of bank is increasing each year than previous year during the study period. The average NPA is Rs. 296 million, standard deviation is Rs. 300 million and coefficient of variation is 101% during the five year study period.

Table: 4.2
NPA to Total Lending Ratio of KBL

(Rs. In Millions)

Fiscal Year	Total NPA	Total Lending	Ratio (%)
2008/09	64	14593	0.44
2009/010	75	14765	0.51
2010/011	167	14626	1.14
2011/012	399	17614	2.27
2012/013	776	19369	4.01
Mean			1.67
SD			1.50
CV			89.51

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.2
NPA to Total Lending Ratio of KBL

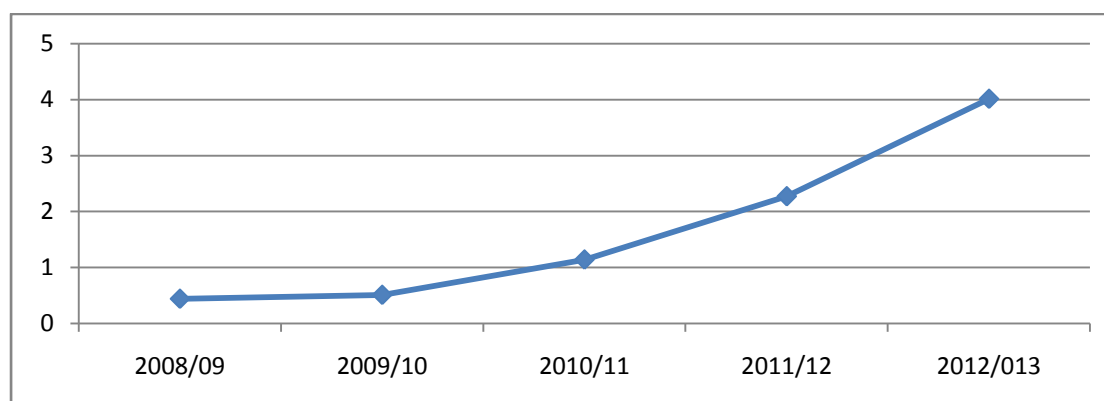


Table 4.2 and Figure 4.2 shows that the NPA to total lending ratio of KBL. This ratio is increasing each year than previous year during the study period. The ratio is 0.44% in the fiscal year 2008/09 after that it is increases each year and finally reaches to

4.01% at the end of fiscal year 2012/013. The average NPA to total lending ratio is 1.67%, standard deviation is 1.50% and coefficient of variation is 89.51% during the five year study period.

Table: 4.3
NPA to Total Deposit Ratio of KBL

(Rs. In Millions)

Fiscal Year	Total NPA	Total Deposit	Ratio (%)
2008/09	64	15710	0.41
2009/010	75	17432	0.43
2010/011	167	16986	0.98
2011/012	399	21985	1.81
2012/013	776	25318	3.07
Mean			1.34
SD			1.12
CV			83.64

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.3
NPA to Total Deposit Ratio of KBL

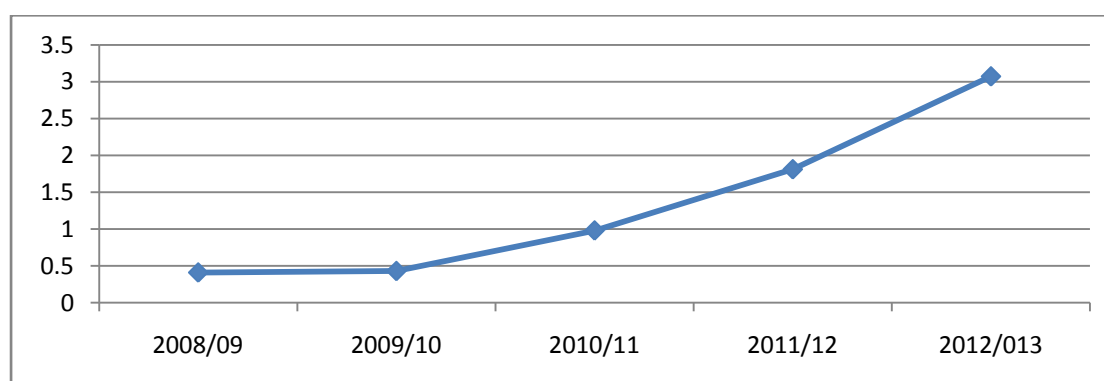


Table 4.3 and Figure 4.3 shows that the NPA to total deposit ratio of KBL. This ratio is increasing each year than previous year during the study period. The ratio is 0.41% in the fiscal year 2008/09 after that it is increases each year and finally reaches to 3.07% at the end of fiscal year 2012/013. The average NPA to total deposit ratio is

1.34%, standard deviation is 1.12% and coefficient of variation is 83.64% during the five year study period.

Table: 4.4
NPA to Total Assets Ratio of KBL

(Rs. In Millions)			
Fiscal Year	Total NPA	Total Assets	Ratio (%)
2008/09	64	18538	0.35
2009/010	75	20522	0.37
2010/011	167	20491	0.81
2011/012	399	25131	1.59
2012/013	776	28222	2.75
Mean			1.17
SD			1.02
CV			86.58

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.4
NPA to Total Assets Ratio of KBL

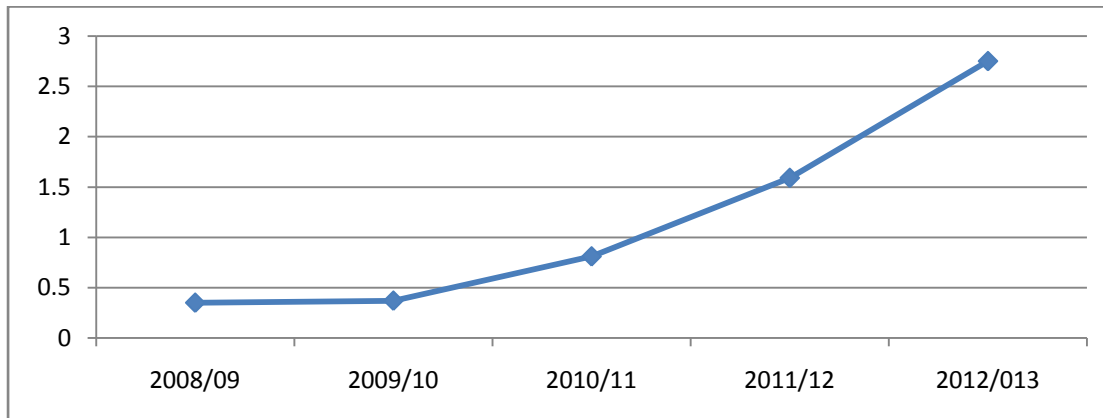


Table 4.4 and Figure 4.4 shows that the NPA to total assets ratio of KBL. This ratio is increasing each year than previous year during the study period. The ratio is 0.35% in the fiscal year 2008/09 after that it is increases each year and finally reaches to 2.75% at the end of fiscal year 2012/013. The average NPA to total assets ratio is 1.17%,

standard deviation is 1.02% and coefficient of variation is 86.58% during the five year study period.

4.1.2 Nepal Investment Bank Limited (NIBL)

Table: 4.5

Total Assets, Total Deposits, Total Lending and Total NPA of NIBL

(Rs. In Millions)

Fiscal Year	Total Asset	Total Deposit	Total Lending	Total NPA
2008/09	53011	46698	36827	213
2009/10	57305	50095	40319	254
2010/11	58356	50138	41095	395
2011/12	65756	57010	41636	1425
2012/13	73152	62428	46400	913
Mean	61516	53274	41255	640
SD	7960	6343	3432	520
CV	13	12	8	81

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.5

Total Assets, Total Deposits, Total Lending of NIBL

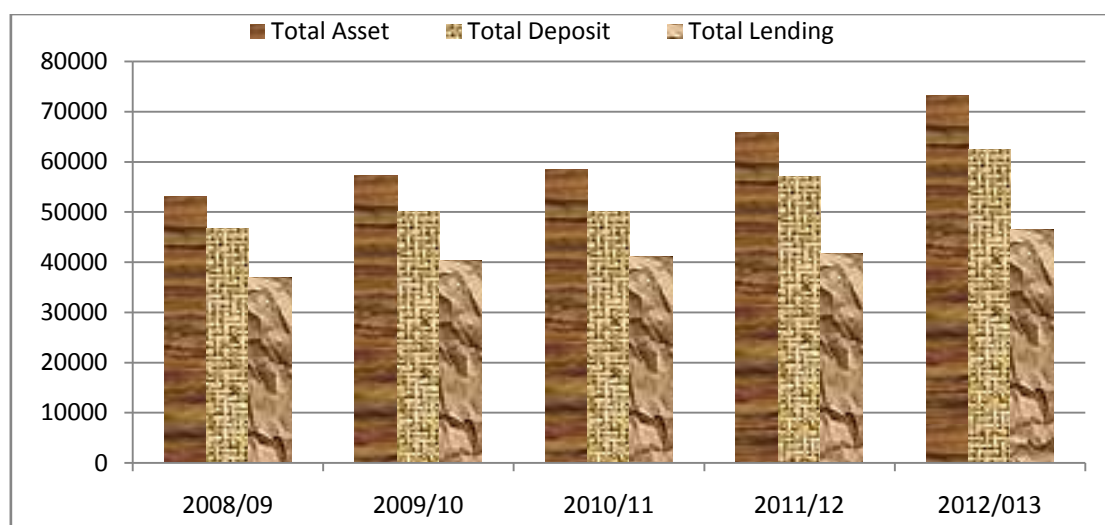


Table 4.5 and Figure 4.5 shows that the total assets, deposit, lending and NPA of NIBL. During the study period of five fiscal years total assets are increasing each fiscal year than previous year. The average total asset of five fiscal years is Rs.61516 million, standard deviation is Rs. 7960 million and coefficient of variation is 13%. Total deposit is increasing each year than previous year, average deposit is Rs. 53274 million, standard deviation is Rs. 6343 million and coefficient of variation is 12%. Total lending is increasing each year than previous year. The average lending is Rs. 41255, standard deviation is Rs. 3432 million and coefficient of variation is 8%. Similarly, NPA of bank is increasing each year than previous year except the fiscal year 2012/013 during the study period. The average NPA is Rs. 640 million, standard deviation is Rs. 520 million and coefficient of variation is 81% during the five year study period.

Table: 4.6
NPA to Total Lending Ratio of NIBL

(Rs. In Millions)

Fiscal Year	Total NPA	Total Lending	Ratio (%)
2008/09	213	36827	0.58
2009/010	254	40319	0.63
2010/011	395	41095	0.96
2011/012	1425	41636	3.42
2012/013	913	46400	1.97
Mean			1.51
SD			1.21
CV			79.72

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.6

NPA to Total Lending Ratio of NIBL

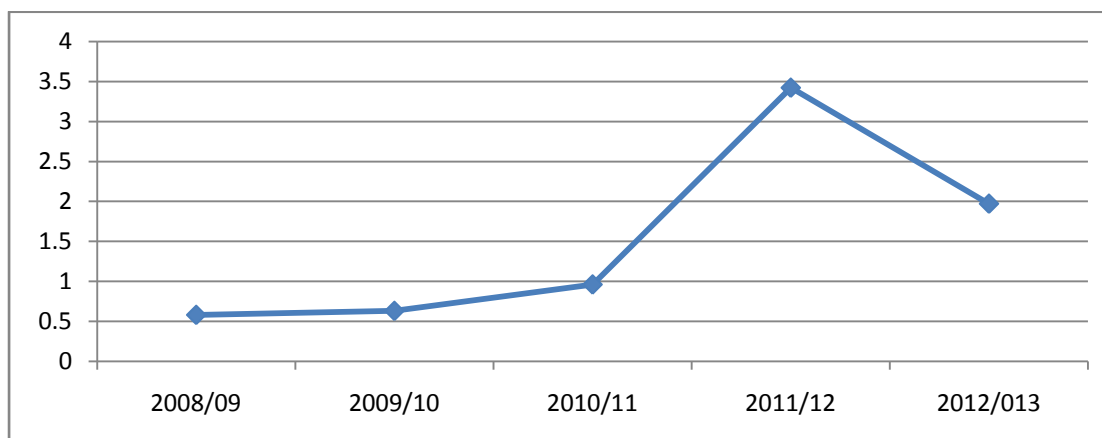


Table 4.6 and Figure 4.6 shows that the NPA to total lending ratio of NIBL. This ratio is increasing each year than previous year except the fiscal year 2012/013. The ratio is 0.58% in the fiscal year 2008/09 after that it is increases each year and reaches to 3.42% at the end of fiscal year 2011/012 and finally decreases to 1.97% at the end of fiscal year 2012/013. The average NPA to total lending ratio is 1.51%, standard deviation is 1.21% and coefficient of variation is 79.72% during the five year study period.

Table: 4.7

NPA to Total Deposit Ratio of NIBL

(Rs. In Millions)

Fiscal Year	Total NPA	Total Deposit	Ratio (%)
2008/09	213	46698	0.46
2009/010	254	50095	0.51
2010/011	395	50138	0.79
2011/012	1425	57010	2.50
2012/013	913	62428	1.46
Mean			1.14
SD			0.86
CV			75.09

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.7

NPA to Total Deposit Ratio of NIBL

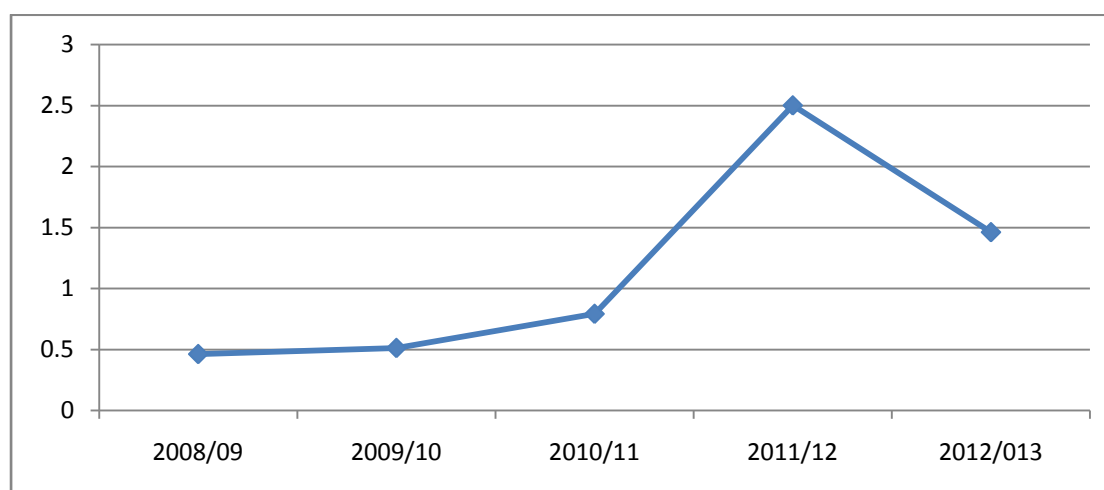


Table 4.7 and Figure 4.7 shows that the NPA to total deposit ratio of KBL. This ratio is increasing each year than previous year except the fiscal year 2012/013. The ratio is 0.46% in the fiscal year 2008/09 after that it is increases each year and reaches to 2.50% at the end of fiscal year 2011/012 and finally decreases to 1.46% at the end of fiscal year 2012/013. The average NPA to total deposit ratio is 1.14%, standard deviation is 0.86% and coefficient of variation is 75.09% during the five year study period.

Table: 4.8

NPA to Total Assets Ratio of NIBL

(Rs. In Millions)

Fiscal Year	Total NPA	Total Assets	Ratio (%)
2008/09	213	53011	0.40
2009/010	254	57305	0.44
2010/011	395	58356	0.68
2011/012	1425	65756	2.17
2012/013	913	73152	1.25
Mean			0.99
SD			0.74
CV			75.02

Source: Annual reports from the fiscal year 2008/09 to 2012/013

Figure: 4.8

NPA to Total Assets Ratio of NIBL

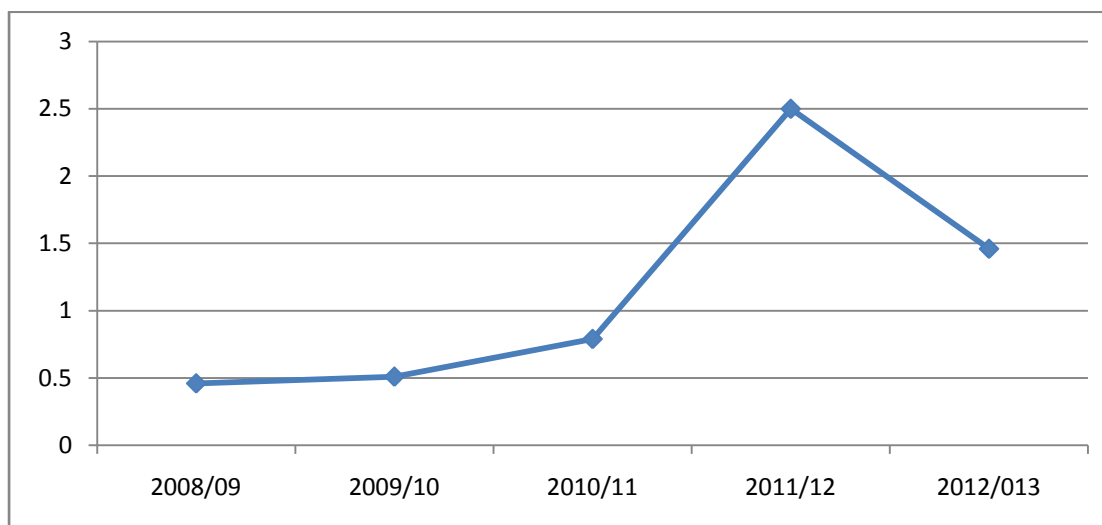


Table 4.8 and Figure 4.8 shows that the NPA to total assets ratio of NIBL. This ratio is increasing each year than previous year except the fiscal year 2012/013. The ratio is 0.40% in the fiscal year 2008/09 after that it is increases each year and reaches to 2.17% at the end of fiscal year 2011/012 and finally decreases to 1.25% at the end of fiscal year 2012/013. The average NPA to total assets ratio is 0.99%, standard deviation is 0.74% and coefficient of variation is 75.02% during the five year study period.

4.2 Comparative Analysis

Table: 4.9

Comparisons of NPA of Sample Banks

(Rs. In Millions)

Variables	KBL	NIBL
Average	296	640
Standard Deviation	300	520
Coefficient of Variation	101%	81%

Source: Table 4.1 & 4.5

Comparing to NIBL with the average value of Rs. 640 million the KBL is better with the average value of Rs.296 million. The Standard Deviations of KBL & NIBL are Rs.

300 & 520 million respectively, it means NIBL has more variability in compare to KBL. The CV of NPA of KBL & NIBL are 101%, and 81% respectively which indicate that KBL is more variable than NIBL.

Table: 4.10
Comparisons of NPA to Total Lending Ratio of Sample Banks

Variables	KBL	NIBL
Average	1.67	1.51
Standard Deviation	1.50	1.21
Coefficient of Variation	89.51	79.72

Source: Table 4.2 & 4.6

Comparing to KBL with the average value of 1.67% the NIBL is better with the average value of 1.51%. The Standard Deviations of KBL & NIBL are 1.50% & 1.21% respectively, it means KBL has more variability in compare to NIBL. The CV of NPA to total lending ratio of KBL & NIBL are 89.59%, and 79.72% respectively which indicate that NIBL is more variable than KBL.

Table: 4.11
Analysis of NPA to Total Deposit Ratio

Variables	KBL	NIBL
Average	1.34	1.14
Standard Deviation	1.12	0.86
Coefficient of Variation	83.64	75.09

Source: Table 4.3 & 4.7

Comparing to KBL with the average value of 1.34% the NIBL is better with the average value of 1.14%. The Standard Deviations of KBL & NIBL are 1.12% & 0.86% respectively, it means KBL has more variability in compare to NIBL. The CV of NPA to total deposit ratio of KBL & NIBL are 83.64%, and 75.09% respectively which indicate that KBL is more variable than NIBL.

Table: 4.12
Analysis of NPA to Total Assets Ratio

(Ratio In %)

Variables	KBL	NIBL
Average	1.17	0.99
Standard Deviation	1.02	0.74
Coefficient of Variation	86.58	75.02

Source: Table 4.4 & 4.8

Comparing to KBL with the average value of 1.17% the NIBL is better with the average value of 0.99%. The Standard Deviations of KBL & NIBL are 1.02% & 0.74% respectively, it means KBL has more variability in compare to NIBL. The CV of NPA to total assets ratio of KBL & NIBL are 86.58% and 75.02% respectively which indicate that KBL is more variable than NIBL.

4.3 Correlation Analysis

Correlation Analysis generally used to describe the degree to which one variable is related to another, in statistics is used in order to depict the co-variance between two or more variables. It helps to determine whether:

- A positive or negative relation exists
- The relation is significant or insignificant
- Establishes cause and effect relation if any.

The statistical tool, “correlation analysis” is preferred in this study to identify the relationship between NPA & NPAT, NPA & Loan & Advance, NPA & Total Deposit and NPA & Total Assets whether the relationship is significant or not.

4.3.1 Relationship between NPA & Net Profit

Coefficient of correlation measures the degree of relationship between total nonperforming assets (NPA) and Net Profit (NPAT) of sample banks. Let, NPA is independent variable (X) and NPAT is dependent variable (Y).

Table: 4.13

Correlation between NPA & Net Profit of Sample Banks

Banks	Coefficient of Correlation (r)	Coefficient of Determination (r ²)	't' Value		Result
			Tabulated	Calculated	
KBL	-0.7899	0.6239	3.182	2.231	Insignificant
NIBL	0.2168	0.0470	3.182	0.384	Insignificant

Source: Annex VI & VII

From the table 4.13, the values of coefficient of correlation (r) between total NPA and net profit is -0.7899 of KBL which shows that there is a negative correlation between NPA and NPAT of KBL but the value of correlation is 0.2168 of NIBL which shows the positive relationship between NPA & NPAT of NIBL. The value of coefficient of determination (r²) is 0.6239 of KBL & 0.0470 of NIBL which shows that 62.39% of the total variation in dependent variable (NPAT) is explained by independent variable (NPA) of KBL and 4.7% of the total variation in dependent variable (NPAT) is explained by independent variable (NPA) of NIBL. The calculated 't' value is less than the tabulated value of both sample banks, therefore it reveals that the relationship between NPA and NPAT is insignificant.

4.3.2 Relationship between NPA & Total Lending

Coefficient of correlation measures the degree of relationship between total nonperforming assets (NPA) and Total Lending (TL) of sample banks. Let, NPA is independent variable (X) and TL is dependent variable (Y).

Table: 4.14

Correlation between NPA & Total Lending of Sample Banks

Banks	Coefficient of Correlation (r)	Coefficient of Determination (r ²)	't' Value		Result
			Tabulated	Calculated	
KBL	0.9742	0.9491	3.182	7.479	Significant
NIBL	0.5594	0.3130	3.182	1.169	Insignificant

Source: Annex VIII & IX

From the table 4.14, the values of coefficient of correlation (r) between total NPA and total lending of KBL is 0.9742 & NIBL is 0.5594 which shows that there is a positive correlation between NPA and total lending of both sample banks. The value of coefficient of determination (r²) is 0.9491 of KBL & 0.3130 of NIBL which shows that 94.91% of the total variation in dependent variable (TL) is explained by independent variable (NPA) of KBL and 31.30% of the total variation in dependent variable (TL) is explained by independent variable (NPA) of NIBL. The calculated 't' value of KBL is greater than the tabulated value i.e. $7.479 > 3.182$, therefore it reveals that the relationship between NPA and TL is significant but The calculated 't' value of NIBL is less than the tabulated value i.e. $1.169 < 3.182$, therefore it reveals that the relationship between NPA and TL is insignificant.

4.3.3 Relationship between NPA & Total Deposit

Coefficient of correlation measures the degree of relationship between total nonperforming assets (NPA) and Total Deposit (TD) of sample banks. Let, NPA is independent variable (X) and TD is dependent variable (Y).

Table: 4.15

Correlation between NPA & Total Deposit of Sample Banks

Banks	Coefficient of Correlation (r)	Coefficient of Determination (r ²)	't' Value		Result
			Tabulated	Calculated	
KBL	0.9732	0.9471	3.182	7.3288	Significant
NIBL	0.7756	0.6051	3.182	2.128	Insignificant

Source: Annex X & XI

From the table 4.16, the values of coefficient of correlation (r) between total NPA and total deposit of KBL is 0.9732 & NIBL is 0.7756 which shows that there is a positive correlation between NPA and total deposit of both sample banks. The value of coefficient of determination (r²) is 0.9471 of KBL & 0.6051 of NIBL which shows that 94.71% of the total variation in dependent variable (TD) is explained by independent variable (NPA) of KBL and 60.51% of the total variation in dependent variable (TD) is explained by independent variable (NPA) of NIBL. The calculated 't' value of KBL is greater than the tabulated value i.e. $7.3288 > 3.182$, therefore it reveals that the relationship between NPA and TD is significant but The calculated 't' value of NIBL is less than the tabulated value i.e. $2.128 < 3.182$, therefore it reveals that the relationship between NPA and TD is insignificant.

4.3.4 Relationship between NPA & Total Assets

Coefficient of correlation measures the degree of relationship between total nonperforming assets (NPA) and Total Assets (TA) of sample banks. Let, NPA is independent variable (X) and TA is dependent variable (Y).

Table: 4.16

Correlation between NPA & Total Assets of Sample Banks

Banks	Coefficient of Correlation (r)	Coefficient of Determination (r ²)	't' Value		Result
			Tabulated	Calculated	
KBL	0.9703	0.9414	3.182	6.9425	Significant
NIBL	0.7570	0.5731	3.182	2.007	Insignificant

Source: Annex XII & XIII

From the table 4.17, the values of coefficient of correlation (r) between total NPA and total assets of KBL is 0.9703 & NIBL is 0.7570 which shows that there is a positive correlation between NPA and total assets of both sample banks. The value of coefficient of determination (r²) is 0.9414 of KBL & 0.5731 of NIBL which shows that 94.14% of the total variation in dependent variable (TA) is explained by independent variable (NPA) of KBL and 57.31% of the total variation in dependent variable (TA) is explained by independent variable (NPA) of NIBL. The calculated 't' value of KBL is greater than the tabulated value i.e. $6.9425 > 3.182$, therefore it reveals that the relationship between NPA and TA is significant but The calculated 't' value of NIBL is less than the tabulated value i.e. $2.007 < 3.182$, therefore it reveals that the relationship between NPA and TA is insignificant.

4.4 Major Findings of the Study

- NPA of KBL is increasing each year than previous year during the study period the average NPA is Rs. 296 million, standard deviation is Rs. 300 million and coefficient of variation is 101%.
- NPA of NIBL is increasing each year than previous year except the fiscal year 2012/013 during the study period. The average NPA is Rs. 640 million, standard deviation is Rs. 520 million and coefficient of variation is 81%.
- In case of Nonperforming assets, KBL is better than NIBL with the average value of Rs.296 million but the KBL is more variable than NIBL. The CV of

NPA of KBL & NIBL are 101%, and 81% respectively which indicate that KBL is more variable than NIBL.

- Comparing to KBL with the average value of 1.67% the NIBL is better with the average value of 1.51% in case of NPA to total lending ratios. The CV of NPA to total lending ratio of KBL & NIBL are 89.59%, and 79.72% respectively which indicate that NIBL is more variable than KBL.
- NPA to total deposit ratio of NIBL is better with the average value of 1.14% than KBL with the average value of 1.34%. The CV of NPA to total deposit ratio of KBL & NIBL are 83.64%, and 75.09% respectively which indicate that KBL is more variable than NIBL.
- NPA to total assets ratio of NIBL is better with the average value of 0.99% than KBL with the average value of 1.17%. The CV of NPA to total assets ratio of KBL & NIBL are 86.58% and 75.02% respectively which indicate that KBL is more variable than NIBL.
- The values of coefficient of correlation (r) between total NPA and total lending of KBL is 0.9742 & NIBL is 0.5594. There is significant relationship between NPA and TL of KBL and insignificant relationship between NPA and TL of NIBL.
- The values of coefficient of correlation (r) between total NPA and total deposit of KBL is 0.9732 & NIBL is 0.7756. There is significant relationship between NPA and TD of KBL and insignificant relationship between NPA and TD of NIBL.
- The value of coefficient of correlation (r) between total NPA and total assets of KBL is 0.9703 & NIBL is 0.7570. There is significant relationship between NPA and TA of KBL and insignificant relationship between NPA and TA of NIBL.
- The value of coefficient of correlation (r) between total NPA and net profit of KBL is -0.7899 & NIBL is 0.2168. There is insignificant relationship between NPA and NPAT of both sample banks.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

In the last chapter of this study is summary, conclusion and recommendation have discussed and explored the facts and matters required for various parts of the study. Through the analytical chapter by using some important financial as well as statistical tools, makes a comparative analysis of various aspects of nonperforming assets of concern commercial banks.

Having completed the basic analysis required for the study, the researcher must point out the mistakes and error and also correct them by giving suitable suggestions for further improvement. Therefore, this summarized and recommended tasks of the researcher of the study would be meaningful to the top management of the bank to initiate the action and achieve the desired result.

5.1 Summary

A commercial bank means the bank, which deals with exchanging currency, accepting deposits, giving loans doing other various commercial transactions. Therefore, the major function of commercial bank is to accept deposits and provide loans. There is not so long history of commercial bank in Nepal. Nepal Bank Limited established in 1994 B. S. was the first commercial bank of the Nepal. But now there are thirty two commercial banks all over the country and they have been expanding their services by establishing branches in every corner of the country.

The assets of commercial bank indicate the manner in which the funds entrusted to the bank are employed. The successful working of the bank depends on ability of the management to distribute the fund among the various kind of investment known as assets outstanding loan advance of the bank. These assets constitute primary source of income to the bank. As being a business unit a bank aims at making huge profit since loan and advances are more profitable than any other assets of the bank, it is willing to lend as much as its fund as possible. But the bank has to be careful about the

repayment of loan and interest giving loan. If the bank is too timid, it may fail to obtain the adequate return on the fund, which is confined to it for use.

Similarly, if the bank is too liberal, it may easily impair its profits by bad debts. Therefore, bank should not forget the reality that most of the bank failures in the world are due to shrinkage in the value of the loan and advances. Despite of being loan and advances more profitable than other assets, it creates risk of non repayment for the bank. Such risk is known as credit risk or default risk. Therefore, like other assets, the loan and advances are classified into performing and non performing assets on the basis of overdue aging schedule. If the dues in the form of principal and the interest are not paid, by borrower within a maturity period, that amount of principal and interest is called non performing loan or assets. It means NPA could wreak branch profitability both through loss of interest income and need to write off the principal loan amount.

Performing assets have multiple benefits to the company as well as to the society while non performing assets erode even existing capital of the bank. Escalating level of NPAs has been becoming great problem in banking business in the world. In this context, Nepal cannot be run off from this situation. The level of NPA in Nepalese banking system is very alarming. It is well known fact that the bank and financial institution in Nepal have been facing the problem of swelling nonperforming assets and the issue of becoming more and more unmanageable day by day. It is well known from different financial reports, newspapers and news that the total NPA in Nepalese banking system is about 32 Billion while it is very worse in case of two largest commercial banks RBB and NBL. (Nepal Rastra Bank, Banking and financial statistics, 2006: 06)

Therefore, this study is concerned to find out the level of NPA and its effects on the returns on assets and the other factors of the Nepalese commercial bank. This study especially focuses on two commercial banks of Nepal, viz. Investment Bank and Kumari Bank only, out of the 32 commercial banks operating in the banking industry of Nepal. Finally, summary and conclusion and various suggestions were described in this chapter. It drew the conclusion from the findings of the study and explained the

summary of research paper. Besides, it also provides various suggestions to give further improvement.

5.2 Conclusion

Nepalese banking industry is faced with variety of serious challenges, the prominent being the management of large volume of non-performing loans and the development of corporate values and ethics among the stake holders in the banking industry. There is already a stiff competition between the market players and the possibility of entry of new players is going to further add to the pressure. So in such a scenario, stakeholders including NRB have to be vigilant that banks do not compromise on the prudent risk management practices in order to survive the competition, which might ultimately lead to the bank failure. At the same time, NRB has to keep tight vigil in the banking industry so as to be take corrective measures in creating and maintaining a stable and a sound banking industry.

- Among the two sample banks taken under study, KBL has the lowest amount of NPA which is in increasing trend in the 5 year study period and NIBL's NPA is also in the increasing trend.
- The NPA to total lending ratio is in increasing trend during the study period of both sample banks.
- The total asset, total deposit, total lending of NIBL is in the increases than previous year and NIBL has also increases except the fiscal year 2010/11.
- Comparatively, during the five year study period NIBL is better than KBL in case of NPA to total lending ratio, NPA to total deposit ratio & NPA to total assets ratio.
- The correlation analysis shows that there is negative and insignificant relation between NPA and net profit of KBL and positive & insignificant relation between NPA and net profit of NIBL.

- The relationship between other variables like NPA & total deposit, NPA & total lending and NPA & total assets of KBL is positive & Significant but NIBL has negative & insignificant.

5.3 Recommendations

High level of nonperforming assets not only decreases the profitability of the banks but also entire financial as well as operational health of the country. If the NPA were not controlled immediately, it would be proved as a curse for the banks in near future. Therefore, following are some of the recommendations, which will help to reduce the level of NPA of the Nepalese commercial banks.

- Corporate structure of bank plays key role in the effective loan management. Being loan a risky asset, efforts should be made to have proper control in every steps of loan management. The banks should establish separate department for credit appraisal, documentation, disbursement, inspection and recovery of loan which have possibility of finding mistakes of one department by the others, so that the effectiveness can be achieved.
- Loan must be given if the banker is satisfied that the borrower can repay money from the cash flow generated from operating activities. However, the banks want to ensure that their loan is repaid even in case of failure of business. To prevent banks from such happenings, the bank take collateral is disposed for the recovery of loan. Therefore the bank should take proper valuation of collateral so that the bank at least will be able to recover its principal and interest amount in case of failure of the borrower to repay the loan.
- Lack of proper financial analysis of the borrower by the banks, is one of the major cause behind increasing NPA of Nepalese commercial banks. Therefore, proper financial analysis should be performed before giving loan to the borrower.
- Those banks, which have high level of NPA, should take necessary action towards recovering their bad loan as possible. In case of doubtful to repay the

loan by the borrower, the bank should dispose of the collateral taken from them and recover the principal and the interest amount thereof.

- Diversification of the loan should be managed by the individual banks. In the context of Nepal it is provided to the borrower so often go to the bank not in the new sector. Default by older borrower can be found, which should be avoided.
- Control mechanism of the bank should be managed properly. Black listed customers should not be given the new loan, as it would lead to the same situation to the bank.
- Political influences in the loan disbursement should be avoided as it may lead to worse condition to the bank as it may increase the non performing loan of the bank.
- Every commercial bank should maintain loan loss provision as per NRBs directives regarding nonperforming assets.
- Further studies can be conducted by using others organization as sample, by using other sophisticated tools and techniques, by using other aspects as well.

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APPENDICES

Appendix I

Major Variables of KBL

Rs. In Million

Fiscal Year	Total Asset	Total Deposit	Total Lending	Total NPA
2008/09	18538	15710	14593	64
2009/010	20522	17432	14765	75
2010/011	20491	16986	14626	167
2011/012	25131	21985	17614	399
2012/013	28222	25318	19369	776

Appendix II

Major Variables of NIBL

Rs. In Million

Fiscal Year	Total Asset	Total Deposit	Total Lending	Total NPA
2008/09	53011	46698	36827	213
2009/010	57305	50095	40319	254
2010/011	58356	50138	41095	395
2011/012	65756	57010	41636	1425
2012/013	73152	62428	46400	913

Appendix III

Calculation of Total NPA to Total Lending Ratios of Sample Banks

Rs. In Millions

Year	KBL		NIBL		KBL	NIBL
	Total NPA	Total Lending	Total NPA	Total Lending	NPA/TL	NPA/TL
2008/09	64	14593	213	36827	0.44	0.58
2009/10	75	14765	254	40319	0.51	0.63
2010/11	167	14626	395	41095	1.14	0.96
2011/12	399	17614	1425	41636	2.27	3.42
2012/013	776	19369	913	46400	4.00	1.97

Appendix IV

Calculation of Total NPA to Total Deposit Ratios of Sample Banks

Rs. In Millions

Year	KBL		NIBL		KBL	NIBL
	Total NPA	Total Deposit	Total NPA	Total Deposit	NPA/TD	NPA/TD
2008/09	64	15710	213	46698	0.41	0.46
2009/10	75	17432	254	50095	0.43	0.51
2010/11	167	16986	395	50138	0.98	0.79
2011/12	399	21985	1425	57010	1.81	2.50
2012/013	776	25318	913	62428	3.07	1.46

Appendix V

Calculation of Total NPA to Total Assets Ratios of Sample Banks

Rs. In Millions

Year	KBL		NIBL		KBL	NIBL
	Total NPA	Total Assets	Total NPA	Total Assets	NPA/TA	NPA/TA
2008/09	64	18538	213	53011	0.35	0.40
2009/10	75	20522	254	57305	0.37	0.44
2010/11	167	20491	395	58356	0.81	0.68
2011/12	399	25131	1425	65756	1.59	2.17
2012/013	776	28222	913	73152	2.75	1.25

Appendix VI

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Net Profit of KBL

Rs. In Millions

Year	NPA (X)	NPAT (Y)	X ²	Y ²	XY
2008/09	64	404	4096	163216	25856
2009/010	75	503	5625	253009	37725
2010/011	167	394	27889	155236	65798
2011/012	399	276	159201	76176	110124
2012/013	776	291	602176	84681	225816
N = 5	∑ X = 1481	∑ Y = 1868	∑ X² = 798987	∑ Y² = 732318	∑ XY = 465319

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 296.20$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 300.13$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 101.33$$

Net Profit after Tax,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 373.60$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 92.78$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 24.83$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2 \times n \sum Y^2 - (\sum Y)^2}} = -0.7899$$

$$r^2 = 0.6239$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 2.231$$

Appendix VII

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Net Profit of NIBL

Rs. In Millions

Year	NPA (X)	NPAT(Y)	X ²	Y ²	XY
2008/09	213	901	45369	811801	191913
2009/010	254	1266	64516	1602756	321564
2010/011	395	1177	156025	1385329	464915
2011/012	1425	1039	2030625	1079521	1480575
2012/013	913	1915	833569	3667225	1748395
N = 5	∑ X = 3200	∑ Y = 6298	∑ X² = 3130104	∑ Y² = 8546632	∑ XY = 4207362

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 640$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 520.12$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 81.27$$

Net Profit after Tax,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 1259.60$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 391.69$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 31.10$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2 \times n \sum Y^2 - (\sum Y)^2}} = 0.2168$$

$$r^2 = 0.0470$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 0.384$$

Appendix VIII

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Total Lending of KBL

Rs. In Millions					
Year	NPA (X)	TL (Y)	X ²	Y ²	XY
2008/09	64	14593	4096	212955649	933952
2009/010	75	14765	5625	218005225	1107375
2010/011	167	14626	27889	213919876	2442542
2011/012	399	17614	159201	310252996	7027986
2012/013	776	19369	602176	375158161	15030344
N = 5	∑ X = 1481	∑ Y = 80967	∑ X² = 798987	∑ Y² = 1330291907	∑ XY = 26542199

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 296.20$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 300.13$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 101.33$$

Total Lending,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 16193.40$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 2188.66$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 13.52$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2 \times n \sum Y^2 - (\sum Y)^2}} = 0.9742$$

$$r^2 = 0.9491$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 7.479$$

Appendix IX

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Total Lending of NIBL

Rs. In Millions

Year	NPA (X)	TL (Y)	X ²	Y ²	XY
2008/09	213	36827	45369	1356227929	7844151
2009/010	254	40319	64516	1625621761	10241026
2010/011	395	41095	156025	1688799025	16232525
2011/012	1425	41636	2030625	1733556496	59331300
2012/013	913	46400	833569	2152960000	42363200
N = 5	∑ X = 3200	∑ Y = 206277	∑ X² = 3130104	∑ Y² = 8557165211	∑ XY = 136012202

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 640$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 520.12$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 81.27$$

Total Lending,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 41255.4$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 3432.38$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 8.32$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2 \times n \sum Y^2 - (\sum Y)^2}} = 0.5594$$

$$r^2 = 0.3130$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 1.169$$

Appendix X

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Total Deposit of KBL

Rs. In Millions

Year	NPA(X)	TD (Y)	X ²	Y ²	XY
2008/09	64	15710	4096	246804100	1005440
2009/010	75	17432	5625	303874624	1307400
2010/011	167	16986	27889	288524196	2836662
2011/012	399	21985	159201	483340225	8772015
2012/013	776	25318	602176	641001124	19646768
N = 5	Σ X = 1481	Σ Y = 97431	Σ X² = 798987	Σ Y² = 1963544269	Σ XY = 33568285

NPA,

$$\text{Mean } (\bar{X}) = \frac{\Sigma X}{N} = 296.20$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\Sigma X^2 - \frac{(\Sigma X)^2}{n} \right]} = 300.13$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 101.33$$

Total Deposit,

$$\text{Mean } (\bar{Y}) = \frac{\Sigma Y}{N} = 19486.20$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\Sigma Y^2 - \frac{(\Sigma Y)^2}{n} \right]} = 4030.64$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 20.68$$

$$\text{Correlation } (r_{xy}) = \frac{n \Sigma XY - \Sigma X \Sigma Y}{\sqrt{n \Sigma X^2 - (\Sigma X)^2 \times n \Sigma Y^2 - (\Sigma Y)^2}} = 0.9732$$

$$r^2 = 0.9471$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 7.3288$$

Appendix XI

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Total Deposit of NIBL

Rs. In Millions

Year	NPA (X)	TD (Y)	X ²	Y ²	XY
2008/09	213	46698	45369	2180703204	9946674
2009/010	254	50095	64516	2509509025	12724130
2010/011	395	50138	156025	2513819044	19804510
2011/012	1425	57010	2030625	3250140100	81239250
2012/013	913	62428	833569	3897255184	56996764
N = 5	Σ X = 3200	Σ Y = 266369	Σ X² = 3130104	Σ Y² = 14351426557	Σ XY = 180711328

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 640$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 520.12$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 81.27$$

Total Deposit,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 53273.80$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 6364.06$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 11.91$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2 \times n \sum Y^2 - (\sum Y)^2}} = 0.7756$$

$$r^2 = 0.6015$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 2.128$$

Appendix XII

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Total Assets of KBL

Rs. In Millions

Year	NPA (X)	TA (Y)	X ²	Y ²	XY
2008/09	64	18538	4096	343657444	1186432
2009/010	75	20522	5625	421152484	1539150
2010/011	167	20491	27889	419881081	3421997
2011/012	399	25131	159201	631567161	10027269
2012/013	776	28222	602176	796481284	21900272
N = 5	∑ X = 1481	∑ Y = 112904	∑ X² = 798987	∑ Y² = 2612739454	∑ XY = 38075120

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 296.20$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 300.13$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 101.33$$

Total Assets,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 22580.80$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 3977.34$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 17.61$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \times \sqrt{n \sum Y^2 - (\sum Y)^2}} = 0.9703$$

$$r^2 = 0.9414$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 6.9425$$

Appendix XIII

Calculation for Mean Value, Standard Deviation, Coefficient of Variation & Correlation between NPA & Total Assets of NIBL

Rs. In Millions

Year	NPA (X)	TA (Y)	X ²	Y ²	XY
2008/09	213	53011	45369	2810166121	11291343
2009/010	254	57305	64516	3283863025	14555470
2010/011	395	58356	156025	3405422736	23050620
2011/012	1425	65756	2030625	4323851536	93702300
2012/013	913	73152	833569	5351215104	66787776
N = 5	∑ X = 3200	∑ Y = 307580	∑ X² = 3130104	∑ Y² = 19174518522	∑ XY = 209387509

NPA,

$$\text{Mean } (\bar{X}) = \frac{\sum X}{N} = 640$$

$$\text{Standard Deviation } (\delta_X) = \sqrt{\frac{1}{n-1} \left[\sum X^2 - \frac{(\sum X)^2}{n} \right]} = 520.12$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{X}} = 81.27$$

Total Assets,

$$\text{Mean } (\bar{Y}) = \frac{\sum Y}{N} = 61516$$

$$\text{Standard Deviation } (\delta_Y) = \sqrt{\frac{1}{n-1} \left[\sum Y^2 - \frac{(\sum Y)^2}{n} \right]} = 7959.70$$

$$\text{Coefficient of Variation (CV)} = \frac{\delta}{\bar{Y}} = 12.94$$

$$\text{Correlation } (r_{xy}) = \frac{n \sum XY - \sum X \sum Y}{\sqrt{n \sum X^2 - (\sum X)^2} \times \sqrt{n \sum Y^2 - (\sum Y)^2}} = 0.7570$$

$$r^2 = 0.5731$$

$$\text{T-value, (t)} = \frac{r}{\sqrt{1-r^2}} \times \sqrt{n-2} = 2.007$$