

CHAPTER-ONE

INTRODUCTION

1.1 General Background

Nepal, a landlocked country with a total area of 147,181sq.km. and around 26.49 million population lies in between two large countries, China in the North and India in the South, East & West. China and India are linked geographically, culturally, economically and socially with Nepal. Nepal is a landlocked and mountainous country. Nepal is divided into three regions on the basis of its physical and geographical feature. Himalayan region which covers 15% of area with 7.39% of total population, Hilly region which covers 68% of area with 44.5% of total population and Terai region which covers 17% of area with 44.3% of total population. Due to the internal conflict & security and physical infrastructure like transportation, education, communication, market, health, electricity as well as agricultural land, the population of Himalayan and Hilly region is in decreasing trend and Terai region is in increasing trend. Out of the total population, 86% people represents about 22.78 million stay in rural area and only 14% people representing about 3.71 million stay in urban area. Nepal is a developing country contributing only 0.02% to the world GDP. The per capita income is about US \$ 280.

Nepal is an agricultural country where more than 80% population depends upon agriculture. Only 20% people out of total population are engaged in industrial and other sector. The agriculture in Nepal has been a source of livelihood for majority of the people and serves as the backbone of Nepalese economy. The contribution of agriculture sector to GDP stood at 40% where as that of non-agriculture sector stood at 60%. The recently conducted national living standard and consumption pattern survey 2004 revealed in its preliminary findings that the population below the poverty line in Nepal has declined to 30.84%. The survey also finds that the remittance from foreign migrant labour has been the major contributor for the

improvement of the poverty level. The main occupation of the rural people is still agriculture. But the overall performance of agriculture sector has not remained strong. Likewise the agricultural sector is still not commercialized due to the geographical condition of the country and lack of essential infrastructure like road, electricity, communication facilities, market, irrigation etc.

Poverty has been the critical issue facing Nepal since long time before. Improvement of the quality of the life of the rural people has been a matter of great concern for the government. As poverty is the root causes of many problems currently faced by Nepal like population growth, environmental degradation and social anomalies, the government has been giving a very high priority to its alleviation.

The growth of GDP at constant (1994/95) price fluctuated over the past five year from the peak of 6.1% recorded in the FY 2007/08 to lowest level of 3.4% in the FY 2006/07. The economy rebounded by 4.4% in FY 2009/10 and was stagnant at 4.6% in the FY 2010/11. Overall performance of the economy in the FY 2010/11 decelerated to 3.5% growth. Growth rate of GDP hardly cover the growth rate of population in Nepal (NRB, Macro Economic Indicators, 2011).

For the development of any country, the financial sector of that country is responsible and must be strong. The financial sector is important and is a vast field, which includes banks, finance companies, co-operatives, insurance companies, stock exchange, foreign exchange market, mutual fund, employee provident fund etc. These institutions collect idle and scattered money from the general public and organization and finally invest in different needy enterprises that consequently help in increasing employment opportunities, reducing poverty and thereby developing the society and the nation as a whole.

Nepal has been facing the problem of accelerating the pace of economic development. Economic development of the any country depends upon the uplift meant of the people through increasing their productivity thereby raising their

incomes, which ultimately help them to cross the poverty line. In this respect the role of commercial banks in the country becomes vital. The commercial banking system in Nepal is still in its infant stage as compared to other developed countries. However their important role in the economic development of the country has been fully realized and these banks are being oriented in their activities to make best suited for the overall economic development of the country.

1.1.1 Credit Management

Credit creation or lending is the main business of every commercial bank. In the field of banking transaction, the term credit is referred to the loan. Credit is defined as the amount of money lent by the creditor (Bank) to the borrower (Customers) either on the basis of security or without security. The main function of commercial banks is granting of credit. Credit is regarded as the income generating source especially in commercial banks. It is also known as the heart of commercial banks in the sense that, it occupies the large volume of transaction; it covers the main part of investment; it is the main factor and source for creating profitability. The credit affects the overall economy of the country. In today's context, it also effects on national economy to some extent. If the bank provides credit facility to individual person, it will help for growth of individual status. Similarly, it provides to trade& industry, the government will get tax from them and help to increase national economy. It is proved from very beginning that credit is the shareholder's wealth maximization derivative. However, other factors can also affect profitability and wealth maximization but the most effective factor is regarded as credit. The credit is the most challenging job because it is backbone of commercial banks. Without good and proper management of credit, the bank couldn't survive in the competition for long time. Thus, effective management of credit should seriously be considered. Management is the system, which helps to complete the every job effectively and systematically. The credit management is also the system, which helps to manage credit effectively. In other words, credit

management refers management of credit exposures arising from loans, corporate bonds and credit derivatives. Credit exposures are the main source of investment in commercial banks and return on such investment is supposed to be main source of income. Thus credit management is defined as the function of analyse credit risks, supply credit to customer as prescribed by the NRB directives, regular follow up, regular monitoring and recovery the loan after maturity period.

Credit management strongly recommends analysing and managing the credit risk. Credit risk is defined as the possibility that a borrower will fail to meet its obligations in accordance with the agreed terms. Credit risk is not restricted to lending activities only but includes off balance sheet and inters bank exposures. It is the most dominant risk present in the banking industry and profitability of the bank is more dependent on the proper management of credit risk. The goal of the credit risk management is to maximize a bank's risk adjusted rate of return by maintaining the credit risk exposure within the acceptable parameters.

The credit policy of a bank provides the framework to determine whether or not to extend credit and how much credit to extend. The credit policy decision of a bank has two broad dimensions; credit standards and credit analysis. The bank has to establish and use standards in making credit decision, develop appropriate sources of credit information and method of credit analysis.

Indeed, making loans is the principal function of banks to fund consumption and investment spending by business, individuals and government offices. The fact how well a bank performs its lending functions has a great deal to do with the economic health of the country. Bank loans support the growth of new businesses and job, and promote economic vitality. More risk in banking tends to be concentrated in the loan portfolio when serious financial trouble, its problems usually spring from loans. Generally loan problems emerge from the following reasons:-

- i. Loans have become uncollectible due to lack of efficient management
- ii. Illegal manipulation of loans
- iii. Misguided lending policies
- iv. Unexpected economic downturn

Credit Management is especially focused on the management of loan disbursement and collection procedure, handling and monitoring. All the activities followed by a bank for the disbursement & collection of loan are known as credit management. So, we can say that loan management is a backbone of any bank. If a bank do loan management properly & accordingly, bank can earn more profit. Every bank's success or failure heavily depends on effective loan management.

On the other side deposit collection is the most essential part of any financial institution for sustainable existence. However, it is from public or loan received from any other parties, deposit is ultimate source to flow the lending smoothly. As being the financial intermediaries they absorb the deposit from surplus sector of economy and invest it to the deficit or demand sector.

1.1.2 Commercial Banks and the Economy

Bank is a financial institution, which is established by law, who collects the fund from several ways and disburses the loan for needy bodies. In other words Bank plays an intermediaries role between the savers and users. They supply the financial needs of modern business by various means. They collect the deposits from the public individual as well as institutions on the condition that they are repayable on demand. Their business is confined to financing the short term needs of trade and industry such as working capital. They grant loans in the form of cash credit and overdrafts. Apart from that financing they also render service like collection of the bills and cheque, safe keeping of valuable ornaments, financial advising to their customers (Vaidya, 2001).

In every country of the world and more so far for developing countries like Nepal,

fast economic development is one of the most important aspects of the development activities. However, it is obvious that unless the development of the most important sectors like agriculture, industry, trade and commerce are achieved, overall economic development is impossible. For overall development, the regular supply of financial resources is a pre-requisite. Finance as fuel for providing energy to move the vehicle of economic development and financial institution naturally serve as reservoir for supplying and controlling the stream of that fuel i.e. commercial banks and finance companies which are the financial institutions, play the vital role for the development of agriculture, industry, trade, commerce and overall economic development of the country. The main objectives of the commercial banks are to mobilize the idle resources in productive uses though 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 finance for the various economic activities in the country.

Nepal has started the process of financial reform and economic liberalization since the late 1980s. As a part of overall liberalization, the government has implemented several policy reforms in the financial sector. The board thrust of financial sector reforms are: to allow market forces to play a greater role in the financial system to enhance private sector participation in the development process of the financial system; to develop a capital market; and to increase competition and thereby efficiency of the sector.

Following a number of reforms in the financial sector over the past two and half decades, the banking sector has become autonomous to a great extent. As results many new joint venture banks and financial companies have been established. Progress has been made to enhance the role of market forces and to create competition in the banking sector. Thus, Nepal has entered in a new era of banking business. Consequently, by the end of 2011 altogether 298 banks and non-

bankfinancial institutions licensed by NRB are in operation. Out of them, 32 are in "A" class commercial banks⁸⁹ in "B" class development banks, 75 in "C" class finance companies, 22 in "D" class micro- credit development banks, 16 in saving and credit co-operatives, and 38 in NGOs. Besides, 2,350 saving and credit co-operatives in the micro finance area are registered with the Department of co-operatives. After the liberalization, the financial sector has been kept more open and liberal to private sector. As a result of this out of 32 commercial banks, 29 are in the private sector including 5 private sector banks have also in foreign stake.

The table 1.1 shows the total capital fund, deposits, investment and loan and advances of the financial sector of Nepal during the five years of period.

Table 1.1
Indicators of Financial Sector

Heads						(Rs. In Million)
	2007	2008	2009	2010	2011	Growth % in 2011 above 2010
Capital Fund	6,901.70	25,778.00	50,265.60	75,485.90	103,407.50	36.99
Deposits	391,152.60	508,905	668,679.50	785,238.00	869,951.40	10.79
Investment	101,888.20	120,335.60	70,346.50	84,641.50	107,562.40	27.07
Loans and Advances	291,605.80	391,537.70	499,892.60	609,921.90	698,779.00	14.56
Total Assets/Liabilities	582,477.30	706,324.00	967,605.30	1,007,969.10	1,144,717.70	13.57

Source: Banking and Financial Statistics, 2011(www.nrb.org.np)

1.2 Brief Profile of Sanima Bank Limited (SBL)

Talking about the credit management of Banks in Nepal, we would like to be concentrated towards Sanima Bank Limited (SBL). SBL was established in 2004 as Sanima Bikas Bank Limited, under the Development Bank Act, 2052 (1995) and Company Act, 2053, (1996). It started functioning as “A” Commercial Bank after it got operating license from Nepal Rastra Bank on Feb 15, 2012. Its head office is at Naxal, Narayanchaur, Kathmandu with altogether 22 branches. Now it is operated under Bank and Financial Act, 2063. The bank was established by the dynamic and enterprising Non-

Residential Nepalese (NRN) with a vision to mobilize required resources for the national development process.

The Bank has been in forefront in the country for mobilizing its resources in financing hydro power projects. The bank was established to provide banking and financial solutions in a simplified way with customer focus while adding value to stakeholder's interest. The capital structure and share holding pattern of the Sanima Bank is as follows:

Capital Structure:

Authorized Capital: NPR 2,100,000,000.00

Issued Capital: NPR 2,016,000,000.00

Paid-up Capital: NPR 2,016,000,000.00

Share Holding Pattern:

Promoter's: 70%

General Public: 30%

The bank is committed to do following works to achieve its objectives:

- To provide loan on Sector of agriculture, Industry, Trade, SMEs, Micro Credits, Housing and Land Development and Service Business Sector by utilizing available resources and skills.
- To operate special program by selecting poor and backward populated socially for upgrading their life style.
- To provide banking service and help them for select and implement of right projects for rural semi-rural and urban sector of its geographical people according to development bank concept.
- To develop and implement alternative scheme for mobilization of internal resources as well as external resources.
- To provide certain level of loan against group liabilities to less income generated people and scheduled group for their suitable projects.

Salient Features of the Bank

- Debit Card and ATM Facility

- Any branch banking facility
- Maximum benefit and security to depositors.
- Loan facility to entrepreneurs on easy process and low cost interest.
- Special program to use the technology and human resources.
- Easy and quick computerized banking services.
- Money Transfer facilities.
- Remittance

1.3 Statement of the Problem

Nepalese people depend on non-institutional money lenders such as local lenders called Mahajans, Landlords and Merchants at high interest rate because of lack of enough financial institution. Although some financial institutions are operating but still their operating system and loan lending process are complex and rigid. Most of the financial institutions are operating only in Kathmandu. Why do not they want to go to remote area? Financial institutions are one of the apex entities of economy in any nation promoting different business activities such as trade, industry and commerce.

The performances of the many government banks of the Nepal are not so satisfactory. Nepal Bank Limited and Rastriya Baniya Bank used to have operating loss some years before. One of the reasons for that is an ineffective credit management. A bank can't run properly without managing its liquidity position. The liquidity position depends on the management of loan and their capacity to borne all expenses. Without effective and proper loan or credit management, no banks can accomplish its predetermined goals and objectives. Hence, it is the life-blood of any financial institution.

Many are ignorant about loan disbursement and loan repayment pattern of financial institutions, which plays the dominant role in conducting proper credit management.

This research is concerned on the following issues:-

- Is the credit management of Sanima Bank Limited efficient or not?
- Is Sanima Bank Limited performing well in terms of liquidity, profitability, sector-wise loan and non-performing loan?
- What are the views of the employees of Sanima Bank Limited with regard to the credit management?

1.4 Objectives of the Study

This study has tried to meet the following specific objectives.

- a) To assess the credit practices, efficiency and current credit position of Sanima Bank Limited.
- b) To evaluate the performances of Sanima Bank Limited in terms of liquidity, profitability, sector-wise loan and non-performing loan etc.
- c) To know the views of employees of Sanima Bank Limited with regard to the credit management.

1.5 Significance of the Study:

Credit Management has become as integral part of almost ever banking operation. It is indisputable that the loans and advances are major sources of generating profit in case of financial institution. There is need of additional capital investment to score higher rate of economic growth. Domestic saving and foreign capital (grants and loans) are two principal sources of capital available for investment. Domestic saving is the most crucial and viable source of capital in our country.

Banks also attracts domestic savings under different attractive deposit schemes from savings and grant loans and advances to business sector in long term, mid-term and short term to accelerate economic activities. In the context of Nepal, there is not sufficient research work in credit management. There is enough research work on the performance of commercial banks but this specific function does not seem to be given importance before.

Hence, fund collected by bank should be cautiously allocated under loans and advance. This undertaken venture is pivotal factor to know the true affairs and positions of financial institutions in regard to management of disbursed loans and advances. This will also be a guideline for improving their performance to achieve their objectives. This study also helps to identify the hidden weaknesses regarding loan management of financial institution.

The study of Credit Management of financial institutions will be beneficial to the followings:

a) To the shareholders:

Shareholders are true owners of the company. This study will be useful for them for acquiring the answer regarding- how the funds are utilized as loans and advances? To what extent they are gaining? And is the productivity of their limited resource satisfactory?

b) To the Management:

This study will be helpful to compare and examine own with others regarding performance viz success or failure, effectiveness and so forth.

c) To the Stakeholders:

Customers (depositor and debtors), creditors, competitors, investors, financing agencies, stock exchange, personnel can get information about the performance of financial institution's loans and advances with the help of this analysis. They can make yes or no decision regarding the investment.

d) To the Policy Makers:

Officers of government, ministry, central bank and security exchange and tax can formulate appropriate policy regarding bank with the help of this study.

1.6 Limitations of the Study

The study relates only with the Sanima Bank Limited regarding the loan disbursement, repayment and outstanding in detailed form. Then data have been availed so, the selected sample bank has been continuously studied as described in the proposal.

No study can be free from limitation. This study has some limitations. This task is assigned for the partial fulfilment of MBS course of T.U. It is better that it would be useful for other aspects for any stakeholders. The main limitations of this study are as follows:

- a) This study has focused only on credit management.
- b) The study is based on SBL as a representative of commercial banks.
- c) This study is based on the analysis of 5 years data from FY 2006/07 to FY 2010/11.
- d) Data used in the study are both primary and secondary. Primary data has been collected through the structured questionnaire.

- e) Limited tools and techniques have been used because of lack of sufficient resources.

1.7 Organization of the Study

The study has been organized into five chapters as mentioned below:

- **Introduction** will be presented in the first chapter. It would be divided into nine sub topics. They are general background, credit management, commercial bank and the economy, brief profile of Sanima Bank Limited (SBL), statement of the problem, objectives of the study, significance of the study, limitations of the study and organization of the study.
- **Review of Literature** will be presented in the second chapter which will be further divided into three sub topics. They are conceptual review, review of legislative provision and review of past thesis. Conceptual framework relating to credit/loan as well as Journals, Books, legislative provision and unpublished dissertations related to the study will be reviewed under this topic.
- **Research Methodology** will be comprised of research design, nature and source of data, population and sample, data collection procedure, method of data analysis, data processing procedure, and technique of financial analysis.
- **Data Presentation and Analysis** will be presented in fourth chapter. Data would be obtained from primary and secondary sources. Analysis of primary and secondary data and findings will be explained. It is the main concentration area for the study to get outcome of the research.

Summary, Conclusion and Recommendations will be presented in the fifth chapter. This chapter is the most core and result pointed part of the thesis. Bibliography and necessary annexes will also be presented after the fifth chapter.

CHAPTER-TWO

REVIEW OF LITERATURE

The review of literature is a critical aspect of planning of the study. The main purpose of literature review is to find out what works have been done in the area of the research problem under this study and what has not been done in the field of the research study being undertaken for review study. The researcher uses different books, reports, journals and research studies published by various institutions, unpublished dissertations submitted by master level students. And the same have been reviewed. It is divided into three sub topics:-

- i. Conceptual Review
- ii. Review of Legislative Provision
- iii. Review of Past Thesis

2.1 Conceptual Review

Financial institutions occupy the paramount role in development of the country. These institutions not only mobilize savings but also promote investments in the different enterprises of the national economy that spontaneously assist in alleviating poverty, uplifting employment opportunities and in developing the society and country as whole. Thus, the development of financial institution (commercial bank, finance company, insurance company) is regarded as one of the crucial yardstick for measuring the level of economic development. Nepal, one of the poorest countries in the world is in need of additional capital investment to proper the rate of economic growth. Domestic & foreign capital (grants and loans) are two major chunks of capital available for investment and earlier is crux and stable source of capital to gear sustainable development of nation.

Credit administration involves the creation and management of risk assets. The process of lending takes into consideration the people and the system required for

the evaluation & approval of loan requests, negotiation of terms, documentation, disbursement, administration of outstanding loans and workouts. Knowledge of the process and awareness of its strength and weakness are important in setting objectives and goals for lending activities and for allocating available funds to various lending functions such as commercial, instalment and mortgage portfolio (Johnson, 1990).

2.1.1 Definition of Credit/Loan

In banking business credit and loan can be known as same meaning. Webster's dictionary defines loan as “something lent a sum of money lent often for a specified period and repayable with interest”. (Agnes, 2000) financial institutions lend money out of deposits, they have received. They must increase money by advancing loan since they have to pay interest on deposits. It is apt to provoke "Deposits are the children of loans and loans are the children of deposits."

According to Oxford Learners Dictionary, the meaning of credit can be seen as follows:

“An arrangement that you make, with a shop / store for example, to pay later for something you buy.”

“Money that you borrow from a bank; a loan.”

“The status of being trusted to pay back money to somebody who lends it to you.”

Now according to above definition it can be said that credit is synonyms of loan and advances. So in this study credit is defined as loan and advance as well as loan only in somewhere.

Banks do not keep 100%reserves against deposit for meeting the demands of depositors. As all depositors do not need money at the same time, banks with a small reserve satisfy their demand whenever and wherever demonstrated and grants Loan and advances as credit from excess reserve of deposit.

Credit is financial assets resulting from the delivery of cash or other assets by a

lender to a borrower in return for an obligation to repay on specified date or demand along with the interest. It usually comprises:

- i. Consumer loan, overdraft & credit card loan.
- ii. Residential Mortgages.
- iii. Non-personal loan, such as commercial loans to business, financial institution, government and their agencies.
- iv. Direct finance leasing.
- v. Other financial arrangement that are in substance loans.

As gist it is apt to quote, "Performing loans have multiple benefits to the society while non-performing loan evades even existing capital"

2.1.2 Types of Loan

Types of loan are also known as disbursement procedures and falls under lending procedures and disbursements procedures.

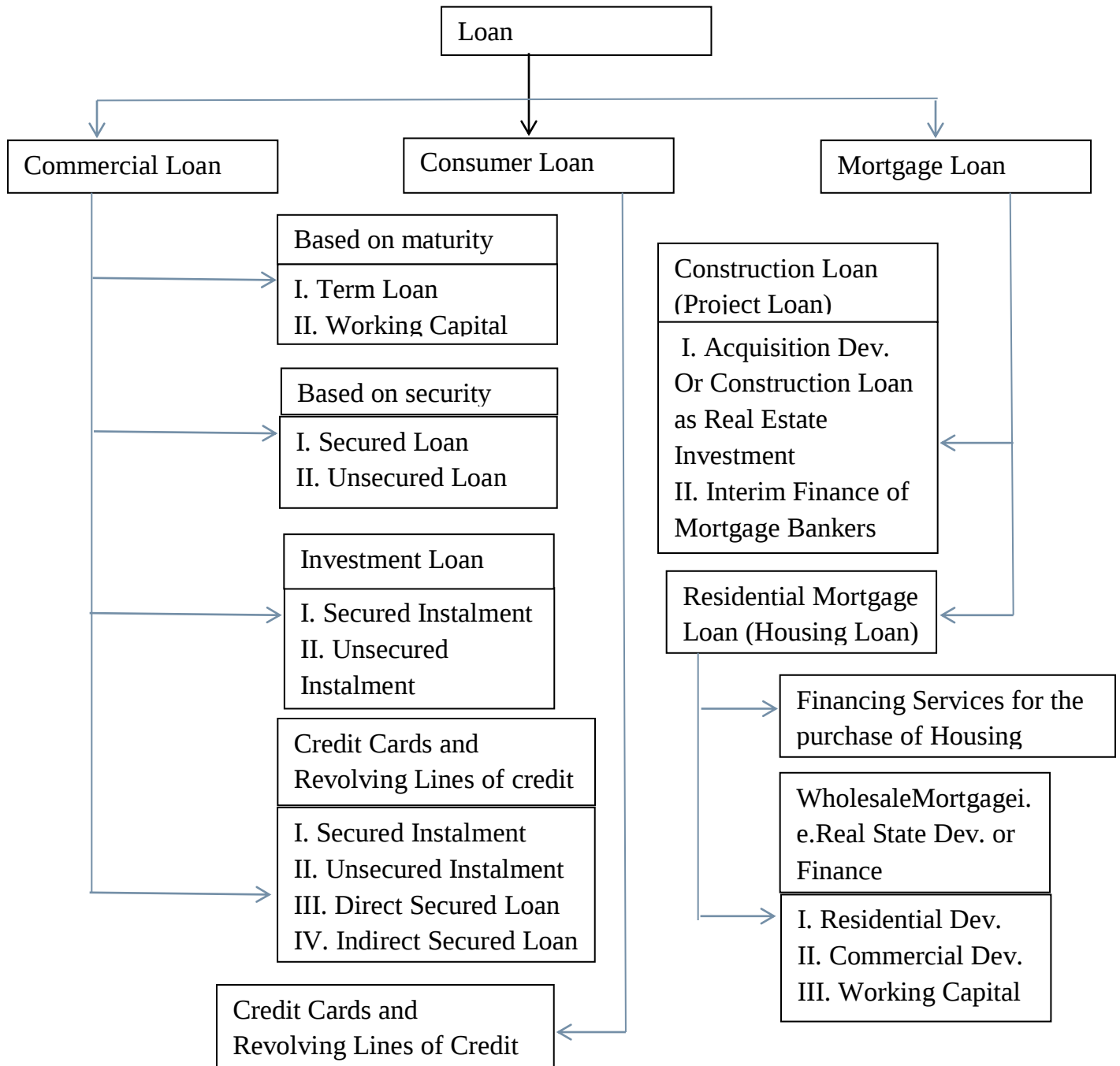
- i. Overdraft
- ii. Cash credit
- iii. Bills discounting (Munjal,1997)

Likewise, Johnson & Johnson has depicted the types of loan as follows:-

- i. Commercial loan
- ii. Consumer loan
- iii. Mortgage loan (Johnson,1940)

Johnson has classified loan as follows:

Figure 2.1
Loan Classification Chart



Source: Johnson Et. Al "Commercial Bank Management" [New corrle :- the Dryden Press, 1940 ehs: 8, 10 11]

Whereas SBL provides the following Loan Scheme (6th Annual Report, p 11):

At SBL the researcher knowhow hard it is to build and run a business. They believe that helping local businesses grow is a key part of their banks responsibility. Their theme is as – “We are here to be your partner. We believe that when we help you succeed then we do too”. SBL wants borrower’s business to succeed. Loan products of SBL are designed to minimize borrowing costs. SBL offers varieties of loan options with competitive rates, personal service and fast approval.

Agriculture: Under the Agriculture sector they provide loan for cereal crops production, cash crops production, seed production, fisheries, cattle farming, poultry farming, forestry, herbal production, farm mechanization & irrigation etc.

Industry: Under the Industry sector the bank provides loans for production industry, energy industry, agriculture & forestry industry, minerals industry, tourism industry, export promotion industry & export promotional areas, service industry, construction industry, cold storage and other industries.

Trade & Commerce: Under the Trade & Commerce sector, trading loan such as Trade Revolving Loan i.e. Overdraft type trading loan, Trade Working Capital Loan and trade other loan i.e. retail trade in any sector of trade and commerce are provided.

Service: Under the Service sector the banks facilitates the loan for tourism, health, information technology, communication, transportation, education, games & entertainment, foreign employment business, environment conservation projects, hire purchase and other service business.

Housing & Land Development: Under the Housing & Land Development sector loans for land development and purchase, construction of residential houses, construction of business house, shopping complex & others are provided.

Vehicles and Equipment: They provide loans for the purchase of vehicles and equipment. They finance up to 80 % of the value of the vehicles and the equipment.

Loan against FDR and Government bonds: The depositors can draw 90% amount of their fixed deposit up to their deposit's maturity time giving plus 2% interest.

SMEs: Under this sector they provide loan to small & medium size industries, trading enterprises for working & fixed capital.

Micro Credit: Under this sector they provide loan below Rs. 50,000.00 for deprived groups.

Though the bank has above lending options, it has classified loan and advances as term, working capital/short term, overdraft, real estate, home equity, lines of credit, hire purchase/leasing and other loan etc. As there is no uniform standard among intellectuals and organizations for classifying loan, sincere and authentic effort is being made for categorizing and dealing about loan.

i. Term loan

It refers to money lent in lump sum to the borrowers. It is principal form at medium term debt financing having maturities of 1 to 8 years, term loans are as usually repaid in level amounts over the period of the loan, either a large final 'Balloon Payment' or just a single 'Bullet Payment' at maturity.

Banks can accommodate repayment patterns of the anticipated cash flow of the borrowing firms. The rate of interest on it is sometimes fixed not only for the life of loan but also as per piece rate. The conditions of a term loan are likely these of most unsecured funds.

Barely and Myess (1996) urge that bank loans with maturities including 1 year period is called term loan. The firm agrees to pay interest based on the bank's prime rate and to repay principal in the regular instalments. Special patterns of

principal payments over time can be negotiated to meet the firm's special need. It is made to support equipment purchases and more permanent funding needs. In receipt term loans occupy the open part of the bank's loan portfolio but traditionally short term loans were emphasized.

ii. Overdraft

Overdraft connotes the excess amount withdrawn over their deposits. The situation of overdraft evolves when bank honours the cheques to an agreed limit. It is a kind of working capital (i.e. fulfilment of short term needs of businessman) loan and allowed only in current accounts. Hence, it is an agreement by which the bank allows the customer to draw over and above the current account balance. The account balance fluctuates frequently since withdrawal and repayment of money took place. Interest on overdraft is charged on debit balance on daily basis.

iii. Cash Credit

It is the commonest form of lending by the firm (Bank). The loan is not given directly in cash but deposit account is being opened on the name of loan taker and the amount credited to that account. In this way, every bank loan creates deposit. It may be operated within the stipulated limit and required time by the borrower. It is provided against the pledge or hypothecation of stock in trade, land building, goods & machinery.

iv. Working Capital Loan

Working capital denotes the difference between current Assets & current liabilities. It is granted to the customers to meet their working capital gap for supporting production process. A natural process develops where funds moving through the cycle are generated to repay a working capital loan. Working capital can be categorized into fixed (permanent) working capital and variable (Temporary) working capital. Short term loan meets the fixed working capital needs whereas overdraft fulfils the variable working capital demands.

v.Fixed Deposit Receipt Loan

The depositors keep fixed deposits for a specified period. The deposit interest rate depend upon maturity period. Generally account holder cannot withdraw from this account. But the depositor can get loan against the collateral of such deposits if he needs money before the maturity date. In general financial institutions allow up to 90% of the FDR face value which can be taken against pledge of original FDR for a period not exceeding FDR maturity.

vi.Project Loan

Project loan is granted to the customers as per project viability. The borrowers have to invest certain proportion to the project from their equity and the rest will be financed on project loan. The so called "Debt-equity Ratio" of the project is 60:40.

"Construction loans are short term loans made to developers for the purpose of completing proposed projects maturities on construction loans range from 12 months to as long as 4 to 5 years, depending upon the size of the specific project (Johnson, 1940). The basic guiding principal involved in disbursement policy is to advance funds corresponding to the completion of the project.

Hence, what percent of the loan will be disbursed or which stage of completion must be spelled in disbursement policy. Term loan & working capital loan needed for project fall under it.

vii.Priority or Deprived Sector Loan

As per directive issued for financial institution by Nepal Rastra Bank, commercial and development and finance companies respectively viz. 'A', 'B' & 'C' class are required to extend advances to the priority & deprived sector. Provision of priority sector loan has been fully phased out and 3% of the total loan must be flown forwards to deprived sector. Institutional support to Agriculture Development

Bank and Rural Development Bank are also considered under this category. Deprived sector lending includes:

- Advance to poor/ downtrodden/ weak/ deprived people up to Rs. 60000 in generating income on employment
- Distributional credit to Rural Development Bank and to Micro credit institutions.
- Loans to NGOs, who are premised to carry out banking transaction of lending up to Rs. 60000.

viii.Hire Purchase Financing (Instalment Loan)

Hire purchase loans are characterized by periodic repayment of principal and interest over the maturity of the loan. Hirer agrees to take the goods on hire a stated rental including the repayment of principal as well as interest with an option to purchase. It can be extended on secured or unsecured basis having maturities of five years or longer.

Majority of instalment loans are made on fixed rates with the interest rate remaining constant over the life of the loan. A recent survey of commercial banks indicates those banks are planning to offer instalment loans on a variable rate basis. It can be secure and insecure as well as direct and indirect instalment loan.

ix.Off Balance Sheet Transaction

In fact, bank guarantee & letter of credit refer to 'Off Balance Sheet' transactions of financial institution. It is also known as contingent liability. Contingent liability pinpoints the liability, which may or may not arise during the happening of certain event. Footnotes are kept as reference to them instead of recording in the books of accounts.

It is non-funded based remunerative facilities but more risky than the funded until adequate collateral are taken. Let's take two varieties to describe separately.

x.Bank Guarantee

It is definite and irrevocable undertaking by a bank (guarantor) on behalf of its customer (debtor) to make payment up to the specified sum of money to the beneficiary (creditor) on demand in case of default by its customer.

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

xi.Letter of Credit (L/C)

It is issued on behalf of the customer (buyer/ importer) in favour of the importer for the import of goods & services stating to pay certain sum of money on the submission of certain document complying the stipulated terms and conditions as per the agreement of L/C.

It is also known as importers letter of credit since the bank of importer opens it. However, the same import L/C is known as export L/C to importer's bank and exporter himself. This classifies the fact that importer and exporter do not open separate L/C for the trade of same commodities.

As an inference, the categorization of loan is exhibited as given below.

xii.Bridge-Gap Loan

The approving institution cannot disburse the facility (of loan) due to incompleteness of legal and other formalities though term loan is approved to some customers and bridge gap loan can be asked in such situation.

xiii.Housing Loan (Real Estate Loan)

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

xiv. Consortium loan

No single financial institution grant loan to the project due to single borrower limit or other reason and two or more such institutions may consent to grant credit facility to the project among them. Financiers have equal (or likely) charge on the projects assets and mortgage. The bank also purchases cheques of approved customers. It is deemed as being liquid investment as it possess certainly to get back fund invested on its maturity.

xv. Single payment loan

Occasionally retail customers need to borrow larger amounts of funds for a short term and then repay in a single payment. As it is a special purpose loan, it requires special handling than typical retail loan. Commercial loan department processes this type of loan in most of the banks. The differentiating features of this type of loan are that the funds are needed for a short period of time and a source of funds will be available to retire the loan. Loan provided against the certificates of deposit is its example. It is usually not a major component of a bank's consumer loan portfolio.

xvi. Credit cards and revolving lines of credit

Banks are increasingly utilizing charge cards and revolving lines of credit to make unsecured consumer loan. Revolving credit line lowers the cost of making loan since operating and processing cost are reduced. Due to standardization, centralized department processes revolving credits resulting reduction on administrative cost. Continued borrowing arrangement enhances cost advantage. "Once the credit line is established, the customer can borrow and repay according to his needs and the bank loan approve the fund to the customer on lower cost" (Anderson, 1940).

Charge cards & credit lines tied to demand deposit accounts are the two most common revolving credit agreements. It can be further divided into credit cards,

automatic overdraft lines and larger credit lines.

2.1.3 Objectives of the Sound Credit Policy

The purpose of a written loan policy are (i) to ensure compliance by lending personnel with the banks policies and objectives regarding the portfolio of loan and (ii) to provide personnel with a framework of standards within which they can operate.

Senior loan administrator getting supports from subordinates and associates should formulate loan policy. For establishing this policy, it is necessary to get approval about this form board of directors after discussion. Performing loans extend multiple benefits to the society where as non-performing loan (i.e. given to unviable projects) erodes even existing scare capital.

i.To have Performing Assets

Performing assets repay principal and interest to the bank from its generated cash flow. The objective of sound loan policy is to keep financial health of the bank meeting interest of depositors and shareholder as well.

ii.To Contribute Economic Development

Sound loan policy says that loans are granted to productive sector (or viable project) which provides multiple benefit to the society such as direct & indirect employment generation, capital creation, tax paid to the government and uplift of living standard.

iii.To Provide Guidance to Lending Officials

There should be no discrimination while dealing with borrower by one officer or another and by one branch or another. Individual loan officers make inconsistent judgment from each other and also with organizational goal in the absence of credit policy.

iv.To Set a Yard Sticks for Control

Periodic follow-up is essential for proper implementation of any credit policy. A sound credit policy aids in identifying the deviation between actual and standard performance along with corrective actions to be taken.

2.1.4 The Elements to be dealt in Credit Policy

The well set up credit policy normally throws light on the following components.

i.Credit Volume

The policy consists of the credit deposit ratio the bank has to maintain since volatility of deposits and borrowings affect loan volume. High volatility of deposits and borrowing will result low loan volume and vice versa. Single borrower limit granted by bank should not exceed the one set by regulatory authority. Under funded credit and non-funded credit banks grants maximum up to 25% and 50% of its core Capital respectively according to directive no. 3 issued by NRB to licensed banks and financial institution.

ii.Credit Mix

Financial institutions do not put their old funds only to one sector even though this sector is doing well. Investment in only one sector may cause bankruptcy of the lenders. Even if two individual borrowers of different sector have the same level of risk, the portfolio risk is minimized due to diversification. The ceiling (i.e. maximum amount of loan wanted to be granted) is fixed in relation to core capital of the bank keeping within the periphery of NRB directives.

There must be clear specification regarding the mix of short term and long term loan deposit mix and interest rate movement of bank affects the mix of short term and long term.

iii.Pricing

The bank however do not take the risk beyond a certain level. Irrespective of how

high the lending rate is prime lending rate is fixed as a practice. Based on the risks, percentage is added in the prime lending rate. The rate follows the same direction of risk i.e. higher the risk, higher the rate and vice versa. Fixed or mixed or floating rate of interest along with compensating balance is to be kept.

In essence, pricing should be fixed in a manner that results profit. Profitability in loan is determined as given below,

$$P=I-O-C-D$$

Where,

P = Profitability

I = Interest inclusive other charge if any

O = Operating expenses

C = cost of Fund

D = Expected Default Loss

iv.Lending Authority

Either centralized or decentralized approach can be adopted by lending authority. A certain limit is given to branch nothing under lateral approach. The proposal should be submitted to head office beyond branch limit. The board of director is the ultimate lending authority having cap like single borrower prescribed by NRB. Some banks fix limit to the official based on their level under both the approaches. In some organizations the lending authority is tied up with the knowledge and expertise rather than with the level.

v.Securities

Liked and disliked securities of bank must be stated in credit policy. Some banks accept bullions & personal guarantee as securities (collateral), whereas others go more forward than that and demand collateral like land, building etc., likewise, the policy should cover the selection of valuator. Guiding factor for selecting

collateral are marketability, liquidity, transferability and convenience.

vi. Risk analysis

Criteria to be met by borrower for getting loan should be clearly described. Proper demarcation about liquidity, leverage, efficiency and profitability ratios must be established such that selection of borrowers can be done consistently.

vii. Loan Administration and Control Mechanism

"The administration of loan portfolio may be divided into the general management objectives of planning, organizing and controlling lending activities" (Johnson, 1940).

Planning should entail consideration of risk and return of loans that meet profit objectives and allocation of loan assets among consumer, commercial, mortgage. Organizing refers to the passing of planned goals and objectives into actions through definition of policies as well as establishment of support function and dissemination of services whereas controlling covers making and monitoring loans to keep on performance standard and to attain profit objectives and goals. "In certain countries there is 'four eyes' concept." A single person cannot do anything. There should be involvement of at least two officials or two departments (Dahal, 2002). Instance of separate department for separate functions like credit approval, documentation, and disbursement and so on facilities in finding mistakes of one department by others. It assists in keeping non-performing assets (NPA) or low level.

The banks need to take various securities so that in case of default of loan such securities can be disposed to recovery of loans.

viii. Loan Classification and Provisions

Loans show their signal (as good or bad) with the passage of time and they should be classified and provided accordingly. Net loan (i.e. total loan loss provision) should be shown instead of showing gross loan in the financial statement. In credit

policy the following things should be dealt.

- Statement of policy objectives
- Organization of the lending function
- Credit standard
- Handling of problem loan
- Credit review and raising process
- Legal consideration
- Delegation of authority
- Types of credit expansions
- Pricing
- Market area

2.1.5 Lending Criteria

For every disbursement of credit, well defined and approved procedure must be followed, such well established criteria for disbursing loan and advance is the most essential for the survival and succession of the commercial bank. These criteria are known as 5 C's, of credit needs to be evaluated, which are as follows (Garg, 2063).

i.Character

How honest and trustworthy is the borrower. Does the borrower intention to pay? There may be borrowers who have enough resources and cash flow to repay the loan but the intention is missing. This is critical since after all it is the character of the person which prompts him to repay his due as per commitment in time. To assess the character of the borrower requires strong inter person skills to talk to the borrower and understand his mental state, make market check on his past actions with other lenders/ business dealing, business experience, lifestyle etc.

ii.Capacity

Capacity refers to the borrower's ability to generate sufficient cash flow from

normal operations to meet future obligations. To the lender, this represents the primary source of repayment for a loan and is the most critical of the five Cs of credit. It needs to be analysed whether the business has the resources (funds, income and revenue) to repay the debt. The business should be sound enough to generate profit which is sufficient for not only repayment of bank loans but also provides reasonable return for the promoters. The earning capacity of the business should be assessed on a conservative basis taking into account the various risk elements relating to the business and its external environment.

iii.Collateral

This is the second way out in case the cash flow of the business is not adequate to service the debt and loans have defaulted. With a secured loan, you pledge something that you own as collateral. It might be personal assets like certificates of deposits or stocks, or business assets like real estate, inventory, equipment or accounts receivable. What could you offer as security for the loan? Is the collateral going to increase or decrease in value? Can the collateral being offered be registered? Can the security be sold, moved or relocated, with or without the knowledge of the lender? A lender considers the ratio of the value of collateral, against the amount of loan. Collateral is considered a secondary or even tertiary source of repayment for a loan.

iv.Capital

It represents the funds retained in the borrowing entity to provide a cushion against unexpected losses. A strong equity position will provide financial resiliency to help a firm weather periods of operational adversity. Minimal or non-existence equity makes a business susceptible to miscalculation and thereby increases the risk of default. A strong equity position also ensures that the owners will remain committed to the business. Capital is often looked at as the amount of money that you have invested into your own business. A financial lender or an investor may be curious as to why you are seeking financial assistance before

using your own assets. Many lenders or investors also want to know if you plan on using your own money to help your business succeed when needed.

v.Conditions

It refers to the national and local economy, the industry and the bank itself. This is often difficult to quantify since it encompasses the entire spectrum of internal or external environment affecting the business. This includes general economic measures, interest rates, the local economy, industry risk analysis, the financial institutions current level of losses and problem credits. Financial lenders and investors are more likely to lend or invest money in a business that will succeed in today's market. Businesses with a poor financial outlook in the next five to ten years are not likely to receive financial backing.

2.1.6 Principle of Lending

There are different principles of lending established for the sustainability of the banks and financial institutions and assurance of return. Banking companies have to examine the loan demand proposal presented to them on the basis of these principles; if such proposal comply with these principles, then only loan should be sanctioned. These principles can be listed as follows (Regmi, 2007).

A. Principle of Liquidity

Liquidity is always required for any banking company to meet the cash withdrawal of the depositors. It is the fund of depositors upon which banking business is dependent. So to maintain the continue faith of depositors every banking company needs to maintain a certain level of liquidity. Presently, the rate of liquidity is 12 percent of its total risk weighted assets for the banking companies having license of the class A, B, C and 8 percent of its total risk weighted assets for the banking companies having license of D class is determined by NRB directive no 1. In addition to this every banking company has to keep certain percent of amount of the total deposit and liabilities to NRB to maintain liquidity. For the banking

companies having class A license - 5 percent of the total deposit, for the banking companies having class B & C license - 2 percent of total deposit and liabilities is determined as compulsory reserve ratio (CRR) by directive no 13 of NRB.

B. Principle of Security

Security of the loan is another necessary aspects needed to be thought seriously. For the security of loan banks have ensure the timely return of the interest and principal. The nature of the collateral, background of the customer, his capacity to pay, guarantee, etc. are some important aspects in this regard. So before making the decision of lending, every banking company has to think seriously in these matters. For the security of the loan banking companies are getting different types of security from the debtor or guarantor. These, mortgage, hypothecation, pledge, assignment/ Power of Attorney Guarantee (Personal/ corporate, lien, movable/fixed) are some ways by which banking companies make their loan secure for repayment.

C. Principle of Diversity

Concentrated lending can create the problem in banking companies once respective sector fails to perform properly. The Principle of diversity says do not keep the all eggs in the same basket. So before making decision of lending, banking companies have to think that the concentration in lending should be avoided and diversity should be maintained. To reduce the concentration risk of banking companies and promote diversity the NRB directive no. 3 make limitation. The maximum limitation of concentration in single customer, firm, company or group is 25 percent of the primary capital in fund based lending and 50 percent in non-fund based lending for the banking companies having license of class A, B & C. Likewise, for the companies having class D license the limitation of 40 thousand for the micro business and 1 lakh for the micro industry not exceeding 25 percent of total lending for a single or group of customers is determined.

D. Principle of Stability

While investing in the security or providing loan on the security, banking companies need to check the price stability of such securities because at the time of crisis banks can make money by selling these securities. If the price rate of such securities is stable and strong, bank's investment will remain secure, otherwise it can be risky.

E. Principle of Profitability

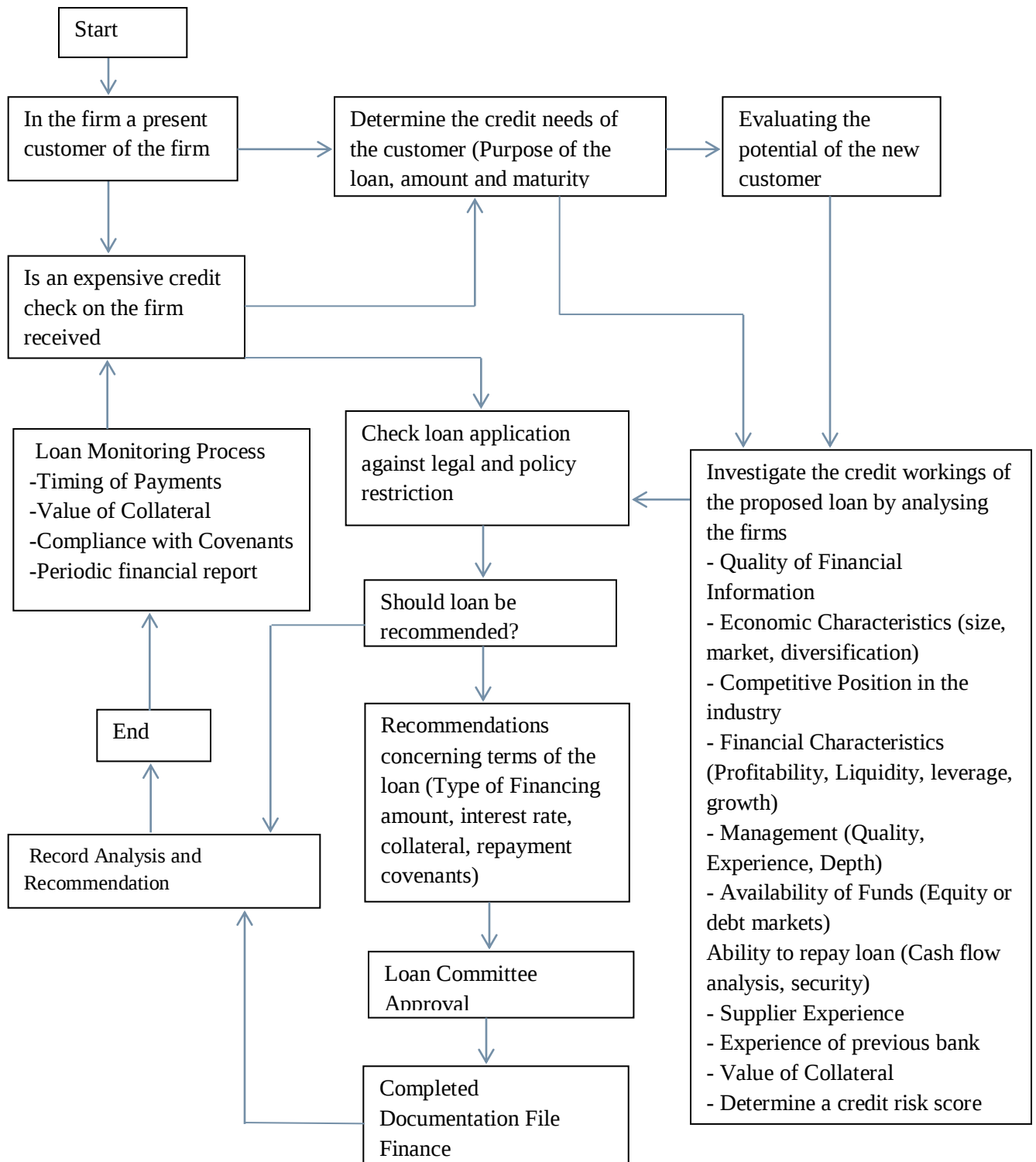
The main objective of the banking companies is to make profit and lending is the main source of profit for every banking company. So every banking company needs to lend their money in profitable way. When the customer for the loan presents the proposal, the bank has to examine the profitability of such proposal.

2.1.7 Business Loan Decision Making Process

When loan officers, credit analysers, and loan review committees evaluate a commercial loan application, they combine financial projections with qualitative information. The loan granting decision is based on the analysis of a firm's historical and proforma financial information and on the interpretation of qualitative information concerning its product markets and industry characteristics, plus the overall performance of management.

In practice, the evaluation of a loan application is based on the information presented in financial statements plus any qualitative information, such as the quality of management, the ability to repay the loan, and the availability and value of collateral. Frequently the qualitative information is of greater value in the lending decision than the financial statement analysis. Generally, business loan decision making process is as follows:

Figure 2.2
Loan Decision Making Process



Source:(Show and Gentry), vol. 17, number 3, Autumn 1988 (Page 47).

2.1.8 Credit (Loan) Disbursement Procedure of SBL

The credit (loan) disbursement process may vary according to size and types of the loans. However, there is certain lending process followed by SBL. The principal lending process has the following steps in general (SBL, Credit Manual, 2006).

a. Application form for requesting Credit Limits

To avail various lines of credit facilities, the client has to duly fill-up bank's prescribed form requesting credit limits which shall contains name of person company, full address, legal entity, promoters/ shareholders/ proprietor's name and their background, associated concerns if any, capital, details of securities, sister concern etc.

b. Discussion with the client

After obtaining application form for requesting credit limits, the bank makes discussion with client regarding credit needs, experience, business projection, nature of business, sales turnover, security details, market share of business, financial statement.

c. Site visit

The credit officer of bank usually makes a site visit to assess the customer's location and the condition of the property. The site visit helps to verify the accuracy of the information provided by the applicant. It also reveals the degree of customer's sincerity and character.

d. Reference Check

The credit officer of bank may contact other creditors, who have already enjoyed the credit facility, to find out the applicant's behaviour, character, experience, status of business, purpose of loan, past record etc., according to necessity.

e. Documentations

If the bank is satisfied with client regarding business, financial statement,

collateral security, then asked to submit several crucial documents (citizenship certificate, scheme of the institution or the business, certificate of registered institution, certificate of income tax registration, financial statement, memorandum & article etc.) in order to fully evaluate the loan request, including complete financial statement. In case of corporate borrower, the board of director's resolution authorizing the negotiation of a loan with the bank must be submitted.

f. Obtaining Credit Information Report (CIB)

When a credit proposal is received, the credit worthiness and the transactions record of the client with other banks are to be ascertained. For this, credit inquiry to Credit Information Bureau and other banks is to be sent. While sending the enquiry, following information is given.

- i. Name of the Client
- ii. Registration No
- iii. Registered Address
- iv. Requested Limit
- v. Name of sister concern

Father's and grand father's name of proprietor, promoters, directors etc., if there are no adverse remarks in the replies obtained from CIB and other bank, then the loan proposal can be initiated.

g. Processing of Proposal

To process a loan proposal, following information are required;

- i. Background of the client and involved person
- ii. Nature and types of business
- iii. Sister Concern and their nature of business. Financial position of the business/person. Liabilities of the client with other banks and financial institutions. Types of facilities requested with limits and period of time.

- iv. Justification as to why facilities are required.
- v. How the facilities will be repaid or settled.
- vi. Types of securities to secure the requested facilities. Inspection report of project and proposed collateral. With the above reports and the information the credit proposal is processed

h. Property Valuation

If the project and collateral are satisfactory and acceptable, then the bank sends approved valuator of the bank for valuation of the property (Land and building).

i. Loan Sanctions

Upon proper scrutiny of the loan appraisal, the sanctioning authority approves the proposal and prepares a loan sanction letter. The sanction letter spells out the details of the loan, the amount and its purpose, the manner of disbursement, the securities to be pledged against the loan, the repayment schedule and other terms & condition of financing.

Upon receipt of the approval from sanctioning authority at the branch, the credit committee of branch issues a credit facility offer letter to the borrower. This letter spell out the details of loan, the amount and its purpose, details of interest rate, service charges, the manner of disbursement the securities to be pledged against the loan and other terms and condition to be implemented by the bank and borrower. If the borrower is satisfied with the credit facility offer letter, the borrower signs in the offer letter and the agreements are made.

2.1.9 Management for Loan Recovery (Recovery Management)

Bank desires the proper utilization of loan by the debtors. Indeed, recovery of loan denotes sequences lay down to get back amount with all due interest including remedial and punitive action to be taken if necessary.

i. Audit of Credit

Credit audit refers to keeping eyes on the granted loan decide how properly this utilized. It is done until the loan is recovered. It is done from time to time to know plight of debtors, proper use of the loan and profit loss position. It comprises

- Verification of loan documents.
- Field visit
- Forms of credit to be prepared
- It may be different forms such as:
 - Internal credit audit
 - External credit audit
 - Credit audit by control bank

ii. Recovery of Interest on Loan

The borrower should pay interest and principal on time as per the deed of the loan and time assigned by the bank. Otherwise, according to the rule of the bank, it charges the interest on interest if borrower does not pay loan in fixed time.

iii. Loan Recovery Process

Bank recovers the granted loan as per the terms and conditions stated in the deed of loan. Loan should be repaid either on instalment basis or lump-sum basis as per the deed of loan. Loan recovery period can be extended making new agreement if borrower's situation goes beyond his control.

iv. Handover of Securities

Bank needs to return movable or immovable properties taken as securities from borrower or security received from third persons as guarantee.

v. Process of Recovering Date-expired Loan

The bank recovers principal and interest of unrecovered loan as per Bank and Financial Institution Act 2063. After recovering the loan accordingly the

remaining cash from sale of property (security) should be returned to the borrower. Good, acceptable, low qualities, doubtful and bad are the classification of loan prescribed by NRB.

vi. Maintenance of Data

A report must be prepared containing clear cut information about loan from release date to recovery data. This works as guideline to current and future management.

2.2 Review of Legislative Provision

NRB Act, 2058 and bank and Financial Institution Act, 2068 have reviewed in this segment. After February 4, 2004 the ordinance relating bank and financial institutions has been promulgated. The ordinance is popularly called an umbrella act as it reveals and replaces all exiting Acts relating to commercial banks, NIDC, other Development banks and finance companies and brings all such institutions under the purview of a single act. Same ordinance was made act by the parliament in 2063 as BAFIA, 2063. It was supposed to be complied since 2063-4-13. The act is divided into 12 chapters and contains altogether 94 sections. Provision regarding Credit disbursement and its recovery procedures are mentioned in chapter 8 that re-establishes the NRB's authority to regulate lending and minimize the chances of loan going to an unscrupulous or diversion of funds.

The NRB issued Directives annually to guide the banking activities. Every bank should follow NRB rules and regulations, otherwise he should pay fine. NRB Directives stated about loans and advances in Directives no. 2. The main provisions established by NRB in the form of prudential norms in above relevant area are briefly discussed here under.

1. Provision for Minimum Capital Fund

License financial institution should keep minimum capital fund for total risk weighted assets after 2005 is as follows:

Table 2.1
Provision for Minimum Capital Fund

Institution	Minimum Capital Fund to Total Risk Weighted Assets	
	Core Capital	Capital Fund
For “A”	6%	10%
For “B”& “C”	5.5%	11%
For “D”	4.0%	8.0 %

Source: NRB Directives, 2068

Note: It is 5.5% of core capital and 11% of capital fund for A,B and C class financial institution up to full comply of Basel II guideline.

2. Provision for credit in the Deprived Sector

Banks should lend 3 percent of total loan and advances to deprive sector as per directives. This provision was imposed to commercial banks only in past but extended it to development banks, “B” class financial institution, also since fiscal year 2064/65 according to monetary policy 2064-65 published by regulatory body, Nepal Rastra Bank.

3. Provision of Credit to the Priority Sector

NRB requires commercial banks, development banks and finance companies to extend certain percent of total loan and advances to the priority sector/deprived sector. Commercial banks credit to the deprived sector is also a part of priority sector credit. As per the NRB Directive, 2068 percentage of loans and advances required to be flowed in the deprived sector are as follows:-

Class	Percentage
Commercial Bank ("A" Class)	3%
Development Bank ("B" Class)	2.5%
Finance Companies	2%

As per the NRB Directive, 2068 following sectors fall under the deprived sector:-

- i. Credit to those who have low income level.
- ii. Credit granted form Micro-Hydro power project, solar home system, solar cooker, solar dryer, solar pump, biogas, wind energy, water mill and improved cook stoves.
- iii. Credit granted for foreign employment and self-employment.
- iv. Loan disbursed to women oriented micro-enterprises.
- v. Loan flowed to "D" class licensed organization.

4. Provision for the Investment in Productive Sector

Nepal being a developing country needs to develop infrastructure and other primary sectors like agriculture industry, etc. For this NRB has directed commercial banks to extend at least 40% of their total credit to the productive sector. Loan to the priority sector, agriculture sector and industrial sector have to be included in productive sector investment.

5. Provision for the Single Borrower Credit Limit

i. For "A" "B" "C" Class Licensed Institution

Licensed institution may extend to a single borrower or group or related borrowers the amount of fund based loans and advances up to 25 percent of the core capital fund and non-fund based (off balance sheet facilities like letter of credit, guarantees, acceptances, commitments) up to 50% of its core capital fund. Fixation of limit on credit and facilities to single borrower shall be made on the basis of core capital fund as per the latest quarterly balance sheet certified by the internal auditor of concerned institution. The fund based loan and non-fund based facilities are separate and accordingly the single borrower limit shall not be calculated by aggregating the both. According to monetary policy 2064-65, the amount and percentage limit can be addition for hydropower projects.

ii) For "D" Class Licensed Institution

Credit to the deprived and low income people may be extended a maximum of up to Rs.40,000 per group member/individual for operation of micro business and not more than Rs.100,000 per each micro enterprise to be provided on a gradual basis to the group member for operation of micro enterprise against acceptable collateral. It will have increased up to Rs. 60,000 and Rs. 150,000 respectively (Monetary Policy, 2064-65, Nepal Rastra Bank, p. 12, section 84). However, the institution shall extend such-enterprise credit up to 25 percent of the total loans and advances.

6. Cash Reserve Requirement

Banks are required to keep adequate liquidity to meet the depositor's demand for cash at any time and to inject the confidence of the depositor's thoughts regarding the safety of deposited fund. To serve for the public welfare NRB has directed to licensed banks and financial institutions to maintain 5% minimum cash reserve upon their total deposit.

7. Loan Classification and Loan Loss Provision

To improve the quality of assets of banks, NRB has directed the banks to classify their outstanding loan and advances, investment and other assets into four categories on the basis of time.

a)Pass b) Substandard c) Doubtful d) Loss Loans and advances falling in the category of pass classified as performing loan. Loans and advances falling in the category of Substandard, Doubtful and Loss are classified as nonperforming loan.

The loan loss provision on the basis of the outstanding loans and advances and bills purchase classified as per this directive should as follows:

Table 2.2
Classification of Loan and Required Provisioning

Classification of Loan	Criteria	Loan Loss Provision
Pass	Due upto 3 months	1%
Sub Standard	Due upto 3-6 months	25%
Doubtful	Due upto 6-12 months	50%
Bad	Due upto 12 months	100%

Source: NRB Directives, 2011

The researcher reviewed the conceptual framework, related studies and legal as well as regulatory guidelines. In this chapter the researcher has organized the literature as related with the credit management. The term ‘credit’ in banking sector also known as loan too. So, the researcher suppose these two terms in the same sense. Hence, the review of literature has been trying to stopping and ahead the research methodology will have presented under the research framework.

2.3 Review of Journal/Articles

In book entitled "**Management Techniques of Bank Lending**" has explained about credit management has two main objectives. One is credit planning and control at the macro level. And another is allocation, follow up and control of credit to individual customers at the micro-level (Chatterjee, 1999).

The book named "**Banking management**" says that in banking sector or transaction an unavailability of loan management and it's methodology is regarded very important under this management many subject matters are considered and thought for example there are subject matters like the policy of loan flow, the documents of loan flow, loan administration audit of loan, renewal of loan, the condition of loan flow, the provision of security, the provision of the payment of capital and it's interest and other such procedures. This management plays a great role in healthy competitive activities. (Bhandari, 2003) yet another dubbed as: loan and advances dominate the asset side of the 'Balance sheet' at any bank. Similarly earnings from such loans and advance occupy a major space in income statement of the bank. Lending cab be said to be the visor of bank. However, it is very

important to be denuded that most of the bank failures in the world are due to shrinkage in the value of loan and advances. Hence, risk of non-payment of loan is known as credit risk or default risk (Dahal,2002).

Similarly, in another book the concerned matters are being presented as loan administration involve the earning and management of risk assets. The process of lending takes into consideration of the people and system required for the evaluation and appeal of loan requests negotiation of terms, documentation, disbursement, administration of considering loans and workout, knowledge of the process and awareness of its strength and weakness are important in setting objectives and goals for lending activities and for allowing available funds to various lending functions such as environmental, instalment and mortgage portfolio (Johnson, 1940).

Crosse(1963) has mentioned in his book "**Management Policies for commercial Banks**", that lending is essence of commercial banking, consequently the formulation and implementation of sound lending policies are among the most important responsibilities of bank directors and management .Well conceived lending policies and careful lending practices are essential if a bank is to perform its credit creating function effectively and minimize the risk inherent in any extension of credit. Before formulating a lending policy, many factors have to be taken into consideration because banks are not the real owners of deposits but rather the custodians of money.

Klisse (1978) gives his view in his book '**Money and Banking** 'that in an economy that depends more and more on credit, banks find themselves lending for a variety of purposes, sometimes directly, sometimes through other agencies. This wider use of loan is not due merely to a change in attitude of the banks. It reflects also more fundamental changes such as shifts in the public's consumption patterns and in financial investment policies.

Reed, Cotter, Gill and Smith (2005) in their book entitled '**Commercial banking**'

focus on the importance of loan in banking sector. As per their view, loans are the most important asset held by banks and bank lending provides the bulk of bank income. Lending is not only important to the banks only, it is equally important to the community the banks serve. That's why loan policies must be worked out carefully after considering many factors.

Gitman and Joehnk (1972) in their book "**Fundamentals of investing**" compare the bank investment with a vehicle. He says that it is such vehicle into which funds can be placed with the expectation that will preserve or increase in value and generates positive results. A banker seeks optimum combination of earning, liquidity and safety while formulating investment policy.

Singh and Singh (1963) put forth their view in the book written by them entitled "**Financial Analysis for Credit Management in Banks**" that the investment (credit) policies of banks are conditioned to great extent by the national policy framework; every banker has to apply his own judgment for arriving at a credit decision, keeping his banker's credit policy also in mind.

As inference from all these above stated authors it can be said that loan management refers to systematic identification of needy one or required party (loan taker), verifying their documents, pre and post site visit, disbursement of loan keeping collateral as cushion for giver and post disbursement inspection cum sound recovery of granted loan as far as practicable.

Srinivasan and Kim(1988) have explained an expert credit granting system prototype in designing expert financial systems:

A Case Study of Corporate Credit Management

Credit granting process in the participating corporation considered of two distinct phases (1) a customer evaluation phase, where the customer's credit worthiness is evaluated based on a variety of criteria; and ii) a credit limit determination phase, where the conclusions of the analysis are transformed into a credit limit or the

customer. System design was therefore, split into two phase, (i) development of an appropriate data base and knowledge base to support the customer evaluation process and (ii) development of an appropriate model to support the credit limit determination phase.

This paper has assumed to describe an expert credit granting prototype designed for a fortune 500 corporation. The focus has been on the conceptual process undertaken for designing the prototype. The model base and rules that comprise the prototype are combination of normative prescriptions and managerial preferences presented in a user-friendly environment issues that need conscious recognition in implementing such expert systems in corporate finance were also brought forth. The progress in computer and information technologies has provided financial researcher an opportunity to affect a transfer of the expertise contained in normative model to practicing managers through the medium of intelligent computer systems. This is a modest attempt to provide a conceptual foundation to this notion and illustrate its feasibility.

Shaw and Gentry (1987)haveshown**Managing and Recommending Business Loan Evaluation (Marble)** system. MARBLE is a generalized expert system that minimizes the lending expertise of several banking and finance professionals. The objectives of MARBLE are to help lending officer, credit analysis, and loan review committees to improve the evaluation of loan applicants and to learn how expert system operate. Based on the knowledge base and the information provided on the loan applicant, MARBLE synthesizes the information and estimates the likelihood that the loan will be repaid. Knowing that the conclusion recommended by MARBLE reflects the judgments of lending experts, management can use it to assist in the lending decision. The MARBLE system has the capability of learning from decision examples. Examples were used to show the value of inductive inference in the knowledge acquisition process. This learning capability makes it possible to build an intelligent decision support system. An empirical study shows

encouraging result for incorporating inductive learning in MARBLE for loan evaluation.

Duchassi, Shawk, and Seagle(1988)have showed Commercial Loan Analysis Support System (CLASS) in their article "**Aknowledge-Engineered system for commercial loan decisions**".This article describe an expert system, commercial loan analysis support system (CLASS) is an expert system designed to evaluate a company's financial posture, recommend commercial loan decision and pertinent components, and document the loan analysis. Like a loan officer, CLASS constitutently synthetics a large number of detailed facts into a loan recommendation. CLASS has been designed to seek our any potential weakness in the prospective borrower and conduct an extensive detailed analysis of each weakness. Weaknesses may be over analysed but none will be overlooked. This approach is consistent with the general notion in commercial lending that one is primarily concerned with weaknesses instead of strong points which are taken for granted. In addition to the limited validation conducted by the expert a more comprehensive validation can be implemented in two ways. First, the system can be empirically tasted with a large sample of historical loan decisions. Second field tested can be conducted in which loan officer use CLASS while making actual loan decisions. Their judgments can be compared to those of CLASS at each step in the analysis. By building CLASS, it was demonstrated that financial knowledge can be represented and applied to a complex financial problem. It is hoped that the approached described will pave the way for building expert systems that address other important financial problems.

2.4 Review of Past Theses

Rajkar (2011)hadanalysed the loan management of Himalayan Bank Ltd. and Everest Bank Ltd.The main purpose of the study was to analyse the efficiency of the selected banks in terms of loan management and also to analyse the non-performing loan in terms of growth rate of loan outstanding, loan recovery, loan

investment and provisions made. Out of the total commercial banks of Nepal, the researcher had selected Everest Bank Limited and Himalayan Bank Limited for the study. Various tools were used to analyse the study like ratio analysis, statistical tools (mean, standard deviation etc.).

From the study it was found that the average loan investment to total loan outstanding of Everest Bank Limited was better than that of Himalayan Bank Limited. It was also observed that the loan recovery of Everest Bank Limited was better than Himalayan Bank Limited. Everest Bank Limited had less non-performing loan than that of Himalayan Bank Limited.

Satyal (2010) studied the credit practices of NABIL Bank Ltd., SCB Nepal Ltd. and Himalayan Bank Ltd. The major objective of the study was to measure the credit performances in quality, efficiency and its contribution in total income and also to determine the liquidity position, the impact of deposit in liquidity and its effect on credit practices. Nabil Bank Ltd., SCB Nepal Ltd. and Himalayan Bank Ltd. were selected as sample for the study among the total commercial banks of Nepal. Portfolio analysis, ratio analysis and comparative analysis were used to analyse the study.

After the study it was found that NABIL Bank Ltd. has deployed the highest proportion of its total deposits in earning activities than SCB Nepal Ltd. and Himalayan Bank Ltd. SCB Nepal Ltd has highest contribution in the service sector whereas Himalayan Bank Ltd. has higher contribution in the industrial sector. All banks have disbursed low amount of loan in the agriculture sector.

Neupane (2009) had conducted study on credit policy analysis of commercial Bank with special reference to Everest Bank Limited with the main objective of identifying the credit management position of Everest Bank Limited as well as to analyse the various financial ratios and trend of deposit utilization and loans of Everest Bank Limited. Out of the total commercial banks of Nepal, Everest Bank Limited was chosen as sample for the study purpose. Ratio analysis and other

statistical tools like mean and standard deviation were used to analyse the study.

After the detailed study it was found that the debt to assets ratio of EBL is excessively high, in other words they have excessively geared capital structure. Return on loan and advances, credit and advance to fixed deposit and Cash and bank balance to current deposit are in fluctuating trend. Non-performing assets to total assets of EBL is in declining trend.

Basnet (2009) conducted the study on credit management of Rastriya Banijya Bank Limited. The main purpose of the study was to analyse the position of loan and advances and recovery status of the Rastriya Banijya Bank Limited and also to identify the strength and weaknesses of the credit administration of the bank. The researcher has selected Rastriya Banijya Bank Limited among all the commercial banks of Nepal for the study purpose. Different tool and techniques were used by the researcher to analyse the data namely: financial tools (ratio and analyses) and statistical tools (mean standard deviation, correlation and coefficient of determination etc.)

After the thorough study it was found that loan and advances of the bank is in increasing trend. At the same time non-performing loan of the bank is also in increasing trend. But the lending procedures of the bank are also improving.

Adhikari (2008) has studied credit management of Siddhartha Vikas Bank Limited. The main objective of the study was to evaluate the performance of SVBL in terms of liquidity, profitability, sector wise loan and non-performing loan and analyse the trends of deposit collection and credit lending. Among the total development banks of Nepal, Siddhartha Vikas Bank Limited was selected as sample. Trend analysis, ratio and analysis and correlation analysis were used to analyse the study.

After the analysis, it was found that the relationship between deposit collection and loan disbursement is highly positive and both deposit collection and loan

disbursement is in increasing trend. Liquidity and profitability position of the bank is in satisfactory level.

Shrestha (2008) had conducted the study on credit management of Nepal Bangladesh Bank Ltd. The main purpose of the study was to examine the lending practices and resource utilization of Nepal Bangladesh Bank. Also to examine the lending efficiency of NB Bank and its impact on the profitability. Out of the various commercial banks of Nepal, Nepal Bangladesh Bank Ltd. was selected for the study. Financial tools and statistical tools were used to analyse the study.

It was found that, NB Bank had more non-performing assets than performing assets and it is in increasing trend. As a result of increment in non-performing loan, loan loss provision had also increased. The loan loss provision had severely affected the profitability of the bank. NB Bank had also kept more liquid fund idle.

Thapa (2008) analysed the credit management and practices of Rastriya Banijya Bank Ltd. The main objective of the study was to assess the credit practices, efficiency and current credit position of Rastriya Banijya Bank Ltd. and to analyse the ratio of credit invested in different sectors and securities. Out of the total commercial banks of Nepal, Rastriya Banijya Bank Ltd. was selected for the study purpose. Various financial tools and statistical tools (mean, standard deviation and correlation) were used to analyse the findings of the study.

It was found that the bank was running with operating loss in the first two years of the study period but in the last four years the bank has been able to earn operating profit due to the decrease in non-performing loan and loan loss provision and increase in the interest income.

Sejuwal (2007) conducted comparative study on credit management of commercial banks; with reference to NABIL and SCBNL. The main purpose of the study were to assess the credit practice and credit efficiency of the selected commercial banks as well as to explore the relationship between loan and advances, non-performing

loan and net profit of the selected commercial banks. Out of the total commercial banks in Nepal only 2 commercial banks were selected i.e. Nabil Bank Ltd. And Standard Chartered Bank Nepal Ltd was selected as sample. Ratio and analysis, correlation analysis and probable error were used to analyse the study.

It was found that NABIL has been strong enough than SCBNL in terms of deposit mobilization as loan. As well as NABIL has been able to earn more interest income than SCBNL but in terms of non-performing loans and loan loss provision SCBNL sounds better than NABIL.

The research relating to the topic credit management is not a new thing in the financial as well research work. Various researches can be found relating to credit management, lending management, loan management, credit analysis and credit appraisal etc. as well. The related research works have been reviewed in the above section of the current chapter of this research work.

Though it's not a new and different topic but it is the first study regarding the data based on the sample bank like Sanima Bank Limited. There is no study conducted in past regarding the credit management selecting the sample bank. To meet this gap, the present study has been conducted.

2.5 Research Gap

The purpose of this research is to develop some expertise in one's area, to see what new contribution can be made and receive some idea, knowledge and suggestion in relation to credit management of Sanima Bank Limited. Thus, the previous studies cannot be ignored because they provide the foundation to the present study. In other words, there has to be continuity in research. This continuity in research is ensured by linking the present study with past research studies. Here, it is clear that new research cannot be found on the same topic i.e. Credit Management of Sanima Bank Limited. Therefore, to fulfil this gap the research is selected.

To complete this research work many books, journals, articles and various published and unpublished dissertations are followed as guideline to make the research easier and smooth. In this regard, here we are going to analyse the different procedure of credit management, which is considered only on Sanima Bank Limited. The main research problem is to analyse whether the Sanima Bank has right level of liquidity as well as is able to utilize its resources effectively or not. To achieve this main objective various financial and statistical tools are used. Similarly, t-test is done to test whether the relationship between the variables is significant or insignificant.

Credit Management is the major function of the commercial bank which is carried out on the basis of NRB Directives and policies of the concerned bank. The directives of NRB change over time and commercial banks also should adopt the policies with the changing pace of time. So, the up to date study over the change of time frame is major concern for the researcher and concerned organization. The study covers the most recent financial data, NRB circulars and guidelines.

CHAPTER-THREE

RESEARCH METHODOLOGY

In order to accomplish the targeted objective of the study, a definite course of research methodology has been followed. A systematic methodology is considered as inevitable for true, fair, better and superior consequences. In fact, research is a scientific inquiry about certain phenomenon or object.

Research methodology refers to the various sequential steps to be adopted by a researcher in studying a problem with a certain objective in view. It is a way to solve the research problem systematically. It may be understood as a science of studying how research is done scientifically. It includes the various steps that are generally adopted by a researcher in studying his research problem along with logic behind them. (Kothari, 2001). The basic objective of this study is to examine and to analyse the credit management (credit disbursement and recovery) of SBL dividing study period (from 2006/07 to 2010/2011) and to provide recommendation for their financial improvement.

Research design, nature and sources of data, sample and method of data analysis are incorporated under this chapter.

Here, research methodology comprises analytical and descriptive research design. The main objective of this study is to see trend relationship between the figure of loan disbursement and collection and to explain the causes of delayed payment from borrowers followed by recommendations.

3.1 Research Design

Kerlinger (1986) describes a research designs as follows: Research design is the plan, structure and strategy of investigation conceived so as to obtain answers to research questions and to control variance. The crux of this research is to analyse the soundness of SBL in relation to loan disbursement, capital adequacy, deposits,

profitability and liquidity.

Research design is the task of defining the research problem. In other words, "A research design is the arrangement of conditions and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure" (Selltin, 1967). The research design is thus an integrated form that guides the researcher in planning and exercising the research works, both exploratory (descriptive) cum analytic along with historical types are adopted as procedure under research design. Statistical analysis is also used herein. Descriptive Analysis design will be adopted in fulfilling the objectives of this study. It is tough to study the principle causes arising from borrower's side and quantify them in relation to the weak repayment performance of SBL.

Statistical tools analysis throws light on the trend situation of loan disbursement and recovery (collection) from FY 2006/07 to FY 2010/11 as far as possible.

Karl Pearson's coefficient of correlation is used to analyse the relationship between the different variables and t-test is used to test the hypothesis between the variables. Average, percentage, graph, chart and diagram will be used herein.

3.2 Nature and Sources of Data

Both primary and secondary sources data have been collected in order to achieve the real and actual results.

i. Primary Sources of Data

Primary data relevant to study have been gathered through questionnaire and observation of institution itself.

Fifteen personnel, of SBL head office and branch had been selected for the sources of primary data. Questionnaire was distributed to the concerned and their responses have been collected for study.

ii. Secondary Sources of Data

Secondary sources of data are the information received from books, journals, newspaper, reports and dissertations etc. the major sources of secondary data are as follows:

- i. Economic survey of Nepal Government, Ministry of Finance.
- ii. NRB directives
- iii. Annual general report of SBL
- iv. National newspaper, journals and magazines.
- v. Websites

3.3 Population and Sample

At present, there are altogether 32 commercial banks on operation in Nepal. Credit management of SanimaBankLimited has been focused. Hence, loan disbursement and recovery of SBL from FY 2006/07 to FY 2010/11, five years are taken as sample for the study, since it is time consuming and cumbersome to census the whole population. All commercial bank data published by Nepal Rastra Bank for the study period is taken as population of the study.

3.4 Respondent Profile

The study is also based on primary data information collected through developing a scheduled questionnaire and distributing these to employees of SBL (Managers, finance chief).

Beside this, junior employees have also been observed and their responses have been drawn regarding the relevant questionnaires.

3.5 Method of Data Analysis

Any analytical tools can be used in solving the problem of this study. For the purpose of the study, all collected primary as well as secondary data are arranged, scanned, tabulated under various heads and then after descriptive cum statistical

analysis have been carried out to enlighten the study.

"Financial analysis is the starting point of making plans before using any sophisticated forecasting and budgeting procedures" (Pandey,1999). Hence ratio analysis is used under financial analysis to attain the result after tabulating the data. Mean, standard deviation, correlation, coefficient of variation, hypothesis are calculated under statistical analysis.

3.5.1 Financial Tools

A ratio is a quotient of two mathematical expressions. Establishment of quantitative relation of data by the financial statement is called ratio analysis. "To evaluate the financial condition and performance of company the financial analysis need ascertain statistical. The yardstick frequently used is a ratio on index relating two pieces of financial data to each other" (Van Horne, 2004). "A single ratio in itself does not indicate favourable or unfavourable conditions. It should be compared with some standard (Pandey, 1999).

The analysis of finance of ratios involves two types of comparison. First, the analysis can compare a present ratio with peer and expected future ratios for the company. The second method of composition involved comparing the ratios of one firm with two of similar firms or with industry average at the same point in time. Such a comparison gives insight into the relative financial condition and performance over time (Van Horne, 2004).

A. Liquidity Ratios

Liquidity ratios are used to judge a firm's ability to meet short term obligations. From them much insight can be obtained into the present cash solvency of company and its ability to remain solvent in the event of adherent. Essentially, we wish to compare short term obligations with the short term resources avoidable to meet these obligations. The following liquidity ratios have been calculated in order to exhibit the liquidity position of the Sanima Bank Limited.

i. NRB Balance to Total Deposit

It provides about the short-term solvency of the firms. It establishes the relationship between NRB Balance and total deposits of which is expressed as:

$$\text{NRB Balance to Total Deposits} = \frac{\text{NRB Balance}}{\text{Total Deposit}}$$

NRB Balances are those assets which can be converted into cash immediately. Likewise, total deposits denote the total deposit collected during the year it may be either saving, current or fixed deposits.

ii. Cash Balance to Total Deposit

This ratio measures the relationship between the cash balance and the total deposits. This ratio exhibits whether the bank has maintained sufficient amount of cash or not to pay out its liabilities in its day to day operations. It is expressed as:

$$\text{Cash Balance to Total Deposit} = \frac{\text{Total Cash Balance}}{\text{Total Deposit}}$$

iii. Cash and Bank Balance to Total Deposit Ratio

This ratio points the banks capacity to cover their deposit like current, call saving and margin.

A higher ratio is preferred since bank is able to cover deposits. It can be expressed as:

$$\text{Cash and Bank Balance to Total Deposit Ratio} = \frac{\text{Total Cash and Bank Balance}}{\text{Total Deposit}}$$

iii) Total Liquid Fund to Total Deposits Ratio

This ratio highlights the percentage of total liquid funds in total deposits. A higher ratio means greater liquid funds are in total deposits and lower ratio means lower liquid funds are in total deposit. It is calculated as:

$$\text{Total Liquid Fund to Total Deposit} = \frac{\text{Total Liquid Fund}}{\text{Total Deposit}}$$

B. Assets Management Ratio

The assets management ratio measures the proportion of various assets and liabilities in balance sheet. Every commercial bank should manage its assets and liabilities properly to earn high profit. Assets management ratio measures its efficiency in multiplying various liabilities in performing assets. Following are the various assets management ratio which measure the lending strength and effective use of assets.

i. Total Assets to Total Liabilities Ratio

The total assets of the bank should play vital role in profit generating through lending activities. The ratio measures the bank ability to multiply its liability into assets. It is always recommended to have higher ratio of total assets to total liabilities ratio since it signifies overall increases of credit. The higher ratio indicates the higher productivity.

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

ii. Loan and Advances to Total Assets Ratio

Loan and advances is an important part of total assets. The total working fund play active role to generate reasonable profit through fund mobilization. So bank should carefully mobilize the total assets. The ratio of loan & advances to total assets ratio measures the volume of loan & advances in the structure of total assets. A high ratio indicates better mobilization of funds as loan and advances and vice-versa.

$$\text{Loan and Advances to Total Assets Ratio} = \frac{\text{Total Loan and Advances}}{\text{Total Assets}}$$

iii. Loan and Advances to Total Deposit Ratio

The main source of bank to provide credit facility to its customers is its deposit. The bank utilizes the deposit for profit generation purpose. Loan and advance to

deposit ratio shows whether the banks are to successful to utilize the total deposit. Generally a high ratio reflects the higher efficiency to utilize total deposit and vice versa. The ratio can be calculated by using following formula.

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

C. Profitability Ratio

Profit is the ultimate goal of every business enterprises, which is essential for the survival of banks, so it is regarded as the engine that drives the banking business and indicates economic progress. It is the major of tangible expression of performance toward achievement of entity objectives and goals. The profitability ratio measures the profitability condition of the bank. Profitability ratios are calculated to measure the management's ability regarding how well they have utilized their funds. Lending is one of the major functions of commercial bank, so following are the various types of ratio which show the contribution of loan and advances to generating in profit and help to decide investor whether to invest in particular firm or not.

i. Interest Income to Total Income Ratio

This ratio measures the volume of interest income to total income. The high ratio indicates the high contribution made by lending investing activities.

$$\text{Interest Income to Total Income Ratio} = \frac{\text{Interest Income}}{\text{Total Income}}$$

ii. Interest Income to Interest Expenses Ratio

Interest income to interest expenses ratio measure the gap between interest rates offered and interest rate charged. The ratio can be calculated as follows.

$$\text{Interest Income to Interest Expenses Ratio} = \frac{\text{Interest Income}}{\text{Interest Expenses}}$$

iii. Return on Loan and Advances Ratio

This ratio measures the earning capacity of the commercial banks through its fund mobilization in forms of loan and advances. Higher ratio indicated greater success to mobilize fund as loan and advances and vice versa. Mostly loan & advances includes cash credits, overdrafts, bills purchased and discounted. The ratio can be calculated as follows.

$$\text{Return on Loan and Advances Ratio} = \frac{\text{Net Profit}}{\text{Total Loan and Advances}}$$

D. Lending Efficiency Ratio

i. Performing Loans to Total Loans and Advances

Performing loans to total loans & advances ratio shows the proportion of performing loans in the total loan portfolio. As per the NRB directives performing loans are those loans that repay principle and interest timely to the bank from the cash flow it generates. It is calculated by:

$$\text{Performing Loans to Loan and Advances} = \frac{\text{Performing Loans}}{\text{Total Loan and Advances}}$$

ii. Loan Loss Provision to Total Loan and Advances Ratio

Loan loss provision to total loan & advances describes the quality assets that a bank holding. The provision for loan loss reflects the increasing probability of non-performing loan. The provision of loan loss mean the net profit of the banks will come down by such amount. Increase in loan loss provision decrease in profit result to decrease in dividends but its positive impact is that strengthens financial condition of the bank by controlling the credit risk and reduced the risk related deposits.

$$\text{Loan Loss Provision to Loan and Advances} = \frac{\text{Loan Loss Provision}}{\text{Total Loan and Advances}}$$

The low ratio indicates the good quality of assets in total volume of loan and advances. High ratio shows the more risky assets in total volume of loan and advances.

iii. Non-Performing Loan to Total Loan and Advances

NPL to total loans and advances ratio determines the proportion of non-performing loans in the total loan portfolio. Higher ratio implies the bad quality of assets of banks in the form of loan & advances. Hence lower NPL to total credit ratio is preferred. As per international standard only 5% NPL is allowed but in the context of Nepal 10% NPL is acceptable. It is calculated as follows:

$$\text{Non - Performing Loan to Loan and Advances} = \frac{\text{Non - Performing Loan}}{\text{Total Loan and Advances}}$$

iv. Sector Wise Loan and Advances Ratio

This ratio measures the portfolio behaviour of the credit disbursement to different sectors. Commercial banks disbursed loans and advances to various sectors of the economy and have types of borrowers.

$$\text{Sector - wise Loan and Advances} = \frac{\text{Loan in different Sectors}}{\text{Total Loan and Advances}}$$

v. Security-wise Loan and Advances Ratio

Every commercial bank has provided the loan and advances in terms of different security to its customers. The ratio measures the portfolio behaviour of the credit disbursement to different securities. The ratio can be calculated by:

$$\text{Security - wise Loan and Advances} = \frac{\text{Loan against different security}}{\text{Total Loan and Advances}}$$

3.5.2 Statistical Tools

i. Arithmetic Mean (Average)

Averages are statistical constants which enable us to comprehend in a single effort

the significant of the whole (Gupta, 2000). Arithmetic mean represents the entire data by a single value. It provides the gist and gives the bird's eye view of the huge mass of unwieldy numerical data. It is calculated as:

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

Where,

$\bar{X}$ = Mean value or Arithmetic Mean

N = Number of observations

$\sum X$ = Sum of observations

ii) Standard Deviation (S.D.)

It is defined as the positive square root of the arithmetic mean of the squares of the deviations of the given observations from their arithmetic mean. It is used as absolute measure of dispersion of variability. It is calculated as:

$$S.D. = \sqrt{\frac{\sum (X - \bar{X})^2}{n}}$$

Where,

S.D. = Standard Deviation

$\sum (X - \bar{X})^2$ = Sum of Squares of deviation

n = Number of Observations

A small S.D. pin points a high degree of uniformity or homogeneity of the data while a large S.D. provokes just adverse.

iii) Co-efficient of Variation (C.V.)

"Co-efficient of variation is the percentage variation in mean, standard deviation

being considered as the total variation in the mean"(Gupta,1998). The C.V. is the relative measure based on S.D. and defined as the ratio of the S.D. to the mean expressed in percent. It is calculated as:

$$C.V. = \frac{S.D.}{\bar{X}}$$

Where,

C.V. =Coefficient of Variation

S.D. = Standard Deviation

$\bar{X}$ = Mean

It is independent of the unit. Hence, two distributions can be compared with the help of C.V. for knowing their variability. A series with smaller C.V. is said to be less variable or more consistent or more homogenous or more uniform or more stable than the other and vice versa.

iv) Correlation (r)

Correlation may be defined as the degree of linear relationship existing between two or more variables. These variables are said to be correlated when the change in the value of one results change in another variable. Correlation may be

- i. Simple or partial or multiple correlations.
- ii. Positive or negative or zero correlation
- iii. Linear or nonlinear correlation.
- iv. Perfect or non-perfect or zero correlation

In the words of Tippet (1927), "The effect of correlation is to reduce the range of uncertainty of our prediction." It is calculated as:

$$r_{xy} = \frac{N\sum XY - \sum X \cdot \sum Y}{\sqrt{N\sum X^2 - (\sum X)^2} * \sqrt{N\sum Y^2 - (\sum Y)^2}}$$

Where,

r_{xy} =Correlation between X and Y

$N\sum XY$ = Product of number of observations

$\sum X \sum Y$ = Product of sum X and Y

v) Coefficient of Determination (r^2)

It explains the variation derived in depended variable due to the any one specific variable it denotes the fact that the independent variable is good predictor of the behaviour of the dependent variable. It is square of correlation coefficient.

vi) T-test

T-test is the statistical examination of two population means. A two-sample t-test examines whether two samples are different and is commonly used when the variances of two normal distributions are unknown and when an experiment uses a small sample size. The t-test looks at the t-statistic, t-distribution and degrees of freedom to determine a p value (probability) that can be used to determine whether the population means differ. The t-test is one of a number of hypothesis tests, which is calculated as:

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

Where,

r = correlation coefficient

n = no. of observations

If the calculated t value exceeds the tabulated value we say that the means are significantly different at that level of probability and vice-versa.

vii) Trend Analysis

When a series of data pertaining to series of containing periods is studied, its characteristics and its future direction are best estimated by the time series. Time

series analyses a series of data keeping in mind the various short term and long term fluctuations.

The least square method to trend analysis has been used to measure the trend behaviours of the bank. The method is widely used in practices. The straight line trend of series of data is represented by the following formula.

$$Y = a + b x$$

Here, y is used to disunite the trend values to distinguish them from the actual y values, a is the y intercept or the computed trend figure of the y variable when $x = 0$, b represents the slope of the trend line of the amount of change in y variable that is associated with a change of one unit in x variable, the x variable in times series analyses represents times.

While analysing the time series, the propensity of growth and growth rate have been examined based the value of trend value of least square method. The growth rate has been measured from 2007 to 2011 to reveal the real status of the study period.

CHAPTER-FOUR

DATA PRESENTATION AND ANALYSIS

In this chapter the relevant information available has been used by analysing the loan management of SBL for the fulfilment of the research objectives. The data of five years (2006/07-2010/11) has been presented for the purpose of study. This study is based on both primary and secondary data. Sources of secondary data are the annual reports of the bank, NRB publications, books, journals, published or unpublished reports etc. Primary data has been collected through direct interview with the staffs of the bank.

For the purpose of analysis, data has been presented in the form of tables and figures. Data presentation and analysis is done to fulfil the objectives of the study. The objectives of the study are to analyse the trend of every year's deposit collection and loan investment, to measure total amount disbursed, out of total deposit collected to measure performance of bank in terms of profitability, liquidity, NPL, to study the attitudes of employees of SBL in regard to the performance of the bank.

4.1 Analysis of Secondary Data

4.1.1 Liquidity Ratios

A commercial bank must maintain its satisfactory liquidity position to satisfy the credit needs of the community, to meet demands for deposit withdrawal, pay maturity obligation in time and convert non cash assets into cash to satisfy immediate needs without loss to the bank. To measure the liquidity position of the bank, the following ratio has been calculated.

4.1.1.1 NRB Balance to Total Deposit Ratio

Table 4.1
NRB Balance to Total Deposit Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.03	0.05	0.12	0.01	0.05	0.05	0.08	1.52

Source: Appendix II (a)

The above table shows that the NRB balances of SBL during the study period. The highest NRB balance to total deposit ratio was 0.12, while the lowest ratio was 0.01 times in FY 2008/09 and 2009/10 respectively. The mean of the current ratio was 0.05, while standard deviation and coefficient of variation were 0.08 & 1.52.

4.1.1.2 Cash Balance to Total Deposit Ratio

Table 4.2
Cash Balance to Total Deposit Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.01	0.02	0.02	0.01	0.02	0.02	0.008	0.44

Source: Appendix II (b)

The above table shows that the Cash balances of SBL during the study period. The highest cash balance to total deposit ratio was 0.02, while the lowest ratio was 0.01 times in FY 2010/11 and 2009/10 respectively. The mean of the current ratio was 0.02, while standard deviation and coefficient of variation were 0.008 & 0.44.

4.1.1.3 Liquid Fund to Total Deposit Ratio

This ratio indicates the ability of bank to discharge its liquidity risks. Liquid fund are those assets, which can be converted into cash within a short period without any decline in their volume

Table 4.3
Liquid Fund to Current Liability Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.04	0.07	0.14	0.04	0.08	0.08	0.04	0.54

Source: Appendix II (c)

The above table shows the liquid funds of SBL during the study period. The highest liquid funds to total deposit ratio was 0.14, while the lowest ratio was 0.04 times in FY 2008/09 and 2009/10 respectively. The mean of the current ratio was 0.14, while standard deviation and coefficient of variation were 0.08 & 0.60.

4.1.2 Profitability Ratios

Profitability ratios are very helpful to measure the overall efficiency in operation of financial institutions. In the context of banks, bank can't survive without profit. The profit is the major indicators of efficient operation of bank. The bank acquires profit by providing different services to its customers or providing loan and making various kinds of investment opportunities. Profitability ratios measure the efficiency of bank. A higher profit ratio shows the higher efficiency of bank and vice versa.

4.1.2.1 Interest Income to Total Income Ratio

This ratio measures the volume of interest income to total income of bank. The higher ratio indicates the higher contribution made by lending and investing activities.

Table 4.4
Interest Income to Total Income Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.92	0.96	0.90	0.94	0.96	0.94	0.02	0.03

Source: Appendix II (g)

From the above table.4.7, it can be said that interest income to total income ratio of the bank was in fluctuating trend during the study period. The highest ratio was 0.96 in the FY 2007/08 and FY 2010/11 and the lowest ratio was 0.90 in the FY 2008/09, where the mean ratio was 0.94 and CV was 0.03.

4.1.2.2 Interest Income to Interest Expenses Ratio

Interest income to interest expenses ratio is the gap between interest rates offered and

interest rate charged. Higher ratio indicates the higher capacity of bank to earned profit and vice versa.

Table 4.5
Interest Income to Interest Expenses Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	2.33	1.87	1.52	1.54	1.52	1.76	0.35	0.20

Source: Appendix II (h)

The above table 4.8 shows that SBL had high degree of gap between interest offered and interest charged. As per the table, the bank charged high interest rate to borrowers and offering low interest rate to its depositors. According to the table the interest income to interest expenses ratio ranged from 2.33 highest ratios to 1.52 lowest ratios during the study period. The ratio was in decreasing trend. It increased up to 1.52 in the FY 2008/09 and FY 2010/11 and mean ratio was 1.76 which showed the least profitable situation at the latest year. CV ratio was 0.20.

4.1.2.3 Return to Loan and Advances Ratio

This ratio measures the earning capacity of commercial bank through its fund mobilization as loan and advances.

Table 4.6
Return to Loan and Advances Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.006	0.008	0.014	0.017	0.024	0.014	0.007	0.54

Source: Appendix II (i)

The table 4.9 shows that return on loan and advances was in increasing trend. The highest ratio was 0.024 in the FY 2010/11 and lowest ratio was 0.006 in the FY 2006/07. The mean ratio is also 0.014, which shows the bank has earned the reasonable profit throughout the study period.

4.1.2 Assets Management Ratios

This ratio measures the efficiency of a commercial bank in its fund mobilization. A

commercial bank must be able to manage its assets properly to earn high profit maintaining the appropriate level of liquidity. Assets management ratio measures the efficiency of the bank to manage its assets in profitable way satisfactorily.

4.1.3.1 Total Assets to Total Liabilities Ratio

The total assets of the bank should pay active role in profit generating through lending activities. This ratio measures the bank ability to multiply its liability into assets. It is always recommended to have higher ratio of total assets to total liabilities. The higher ratio indicates the higher productivity and vice versa.

Table 4.7
Total Assets to Total Liabilities Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	1.16	1.13	1.17	1.14	1.29	1.18	0.07	0.06

Source: Appendix II (d)

It can be said that, the total assets to total liabilities ratio is in fluctuating trend. The ratio was 1.16 in the FY 2006/07, which decreased to 1.13 in the FY 2007/08. Likewise it reached to 1.29 in FY 2010/11. The mean ratio was 1.18 when SD and CV were 0.07 & 0.06 respectively.

4.1.3.2 Loan and Advances to Total Assets Ratio

Loan and advances of commercial bank represents the major portion in the volume of total working fund. This ratio measures the volume of loan and advances in the structure of total assets. The high degree of this ratio indicates the good performance of the bank in mobilizing its funds by way of lending function. Granting of loan and advances always carries a certain degree of risk. Thus this asset of banking business is regarded as risky assets. This ratio measures the management attitude towards risk assets. The low ratio is an indication of low productivity and high degree of safety in liquidity and vice versa.

Table 4.8
Loan and Advances to Total Assets Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.59	0.65	0.68	0.70	0.68	0.66	0.04	0.06

Source: Appendix II (e)

It can be said that the ratios were in fluctuating trend. First it increased, and then decreased. The highest ratio was 0.70 in the FY 2009/10 and lowest ratio was 0.59 in FY 2006/07. The mean ratio was 0.66 whereas SD & CV were 0.04 and 0.06 respectively. The table shows the assets management in terms of loans and advances which is in better form throughout the study period.

4.1.3.3 Total loans & advances to Total Deposit Ratio

This ratio measures the extent to which the bank is successful to manage its total deposit on loan and advances for the purpose of income generation. A high ratio indicates the better mobilization of collected deposit and vice versa. But it should be noted that too high ratio might not be better from liquidity point of view.

Table 4.9
Total Loans & Advances to Total Deposit Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.82	0.87	0.90	0.88	1	0.89	0.07	0.08

Source: Appendix II (f)

As per the above table it can be found that the ratio of loan & advances to total deposit ratio of bank was in increasing trend. The highest ratio in the FY 2010/11 was 1 and lowest ratio was 0.82 in the FY 2006/07.

Credit deposit ratio should be around 70% as standard. From this point of view the loan and advances to total deposit ratio of the bank slightly high in the first in the five years of study period.

4.1.4 Lending Efficiency Ratio

Lending efficiency, quality of lending and its effect measured in this topic. The

efficiency of a bank depends upon to a large extent on the efficiency with which its assets are managed and utilized. This ratio is concerned with measuring the efficiency of bank. The following are the various type of lending efficiency ratio.

4.1.4.1 Loan Loss Provision to Total Loan and Advances Ratio

Loan loss provision to total loan and advance describes the quality of assets that a bank holding. The provision for loan loss reflects the increasing probability of non-performing loan. Provision for loan loss mean the profit of the banks will come down by such amount. Increase in loan loss provision decrease in profit result to decrease in dividends but its positive impact is that strengthens financial conditions of the banks by controlling the credit risk and reduced the risks related to deposits. The low ratio indicates the good quality of assets in total volume of loan and advances and high ratio indicates more risky assets in total volume of loan.

Table 4.10
Loan Loss Provision to Total Loan and Advances Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0.01	0.014	0.011	0.011	0.01	0.011	0.002	0.15

Source: Appendix II (j)

The above table 4.10 shows the ratio of loan loss provision to loan and advances which is in fluctuating trend during the five years of the study period. The figure shows that the bank suffered least proportion of non- performing assets during the study period. The highest ratio was 0.014 in the FY 2007/08 and lowest ratio was 0.01 in the FY 2006/07 and 2010/11. The mean ratio and CV of the study period were 0.011 and 0.15, which shows more consistent nature of the data.

4.1.4.2 NPA Loans to Total Loans and Advances Ratio

Nepal Rastra Bank, issues different directives from time to time to enhance the strength of bank. As per the NRB directive no 2 related to loan classification and loan loss provisioning on the credit, the bank and financial institutions should

classify their loan and advances in four different categories. The loan falling under sub-standard, doubtful and loss categories is termed as Non- performing loan.

Table 4.11
NPA Loans to Total Loans and Advances Ratio

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	0	0.015	0.0017	0.0008	0.000045	0.0036	0.007	1.832

Source: Appendix II (k)

The table 4.11 shows the ratio of Non-performing loans to total loans and advances which is in decreasing trend throughout the study period, which reveals the good efficiency of the loan management. The highest ratio is 0.015 in the FY 2007/08 and 0 is the lowest ratio in the FY 2006/07. The mean ratio is 0.0036, which shows low ratio of non-performing loan to total loan and advances. The CV during the study period is 1.832.

4.1.4.3 Performing Loan to Total Loan and Advances

The credits which are not crossed the time schedule of repayment and are within 3 months delay of maturity date fall under the classification topic “Pass Credit”. It is also known as performing loan. The performing loan is major current assets of bank.

Table 4.12
Performing Loan to Total Loan and Advances

Year	2006/07	2007/08	2008/09	2009/10	2010/11	Mean	S.D	C.V
Ratio	1	0.98	0.99	0.99	0.99	0.99	0.007	0.007

Source: Appendix II (l)

The table 4.12 shows the proportion of performing loan which is the major component of every bank to total loan and advances. As per the table, the ratio is increasing during study period. It increased up to 0.99 in the FY.2010/11. The ratios lie between lowest 0.98 to highest 1. The average ratio of performing loan was 0.99 during the study period.

4.1.5 Sector wise Loan Classification of Sanima Bank Limited

Credit is an act of lending and borrowing of money. It is a sum of money delivery by bank or one party and receipt by customer or another party on agreement expresses or implied to repay with or without interest. Loan and advances includes credit against different sector like; agriculture, mines, production, service, consumable loan etc. Total credit is the amount that is led by the bank by accepting the security of debtors. It is depend upon the interest rate structure. The SBL has provided loan and advances to its customer on the basis of different sector determined by Nepal Rastra Bank. The major loan portfolios are; agriculture, production, construction, consumable loan etc. The outstanding of loan and advances which are provided by the bank on the basis of different sector are as follows:

Table 4.13
Sector-wise Loan Classification of SBL

(Rs. In Million)

Sector	2006/07	%	2007/08	%	2008/09	%	2009/10	%	2010/11	%	Total
Agriculture & Forest Related	0.80	0.05	1.10	0.04	2.00	0.05	0.06	0.00	0.76	0.01	4.72
Fishery	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Mining	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Manufacturing	118.50	7.89	282.30	11.14	327.80	8.12	502.12	10.56	1019.89	15.85	2250.61
Construction	157.70	10.50	352.40	13.91	633.10	15.68	861.85	18.13	1047.08	16.27	3052.13
Electricity, Gas, Water	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	351.61	5.46	351.61
Metal Products, Machinery and Electronic Equipment & Assemblage	0.00	0.00	1.70	0.07	7.20	0.18	8.83	0.19	90.57	1.41	108.30
Transport, Communication & Public Utilities	228.70	15.23	243.30	9.60	327.60	8.11	204.48	4.30	706.92	10.98	1711.00
Wholesaler and Retailer	208.70	13.90	294.60	11.63	490.70	12.15	847.76	17.84	934.59	14.52	2776.35
Finance, Insurance & Real Estate	29.10	1.94	206.70	8.16	1176.80	29.14	899.93	18.93	750.09	11.65	3062.62
Hotel & Restaurant	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	72.13	1.12	72.13
Other Services	84.00	5.59	123.30	4.87	215.60	5.34	339.56	7.14	367.74	5.71	1130.20
Consumption Loans	370.00	24.64	484.90	19.14	570.50	14.13	497.74	10.47	452.65	7.03	2375.79
Local Government	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Others	304.40	20.27	543.10	21.44	287.30	7.11	590.43	12.42	642.17	9.98	2367.40
Total	1501.90	100.00	2533.40	100.00	4038.60	100.00	4752.76	100.00	6436.18	100.00	19262.84

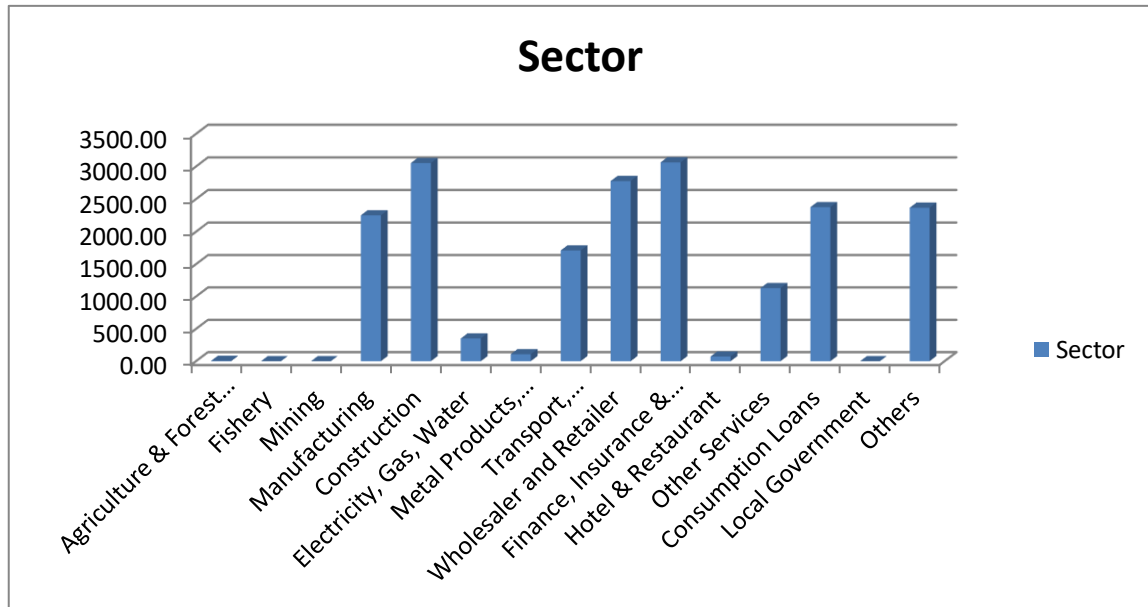
Source: Banking and Financial Statistics, 2011

The above table 4.13 exhibits the loan outstanding and proportion of loan on different sector for five consecutive years. The proportions of sector wise loan ranged from 29% highest to 0% lowest during in the study periods. According to the above table the total loan flows was Rs. 1501.90, 2533.40, 4038.60, 4752.76 and 6436.18 million in the FY 2006/07 to 2010/11 respectively. As per the table, different sectors have occupied the highest percentage during the five years of study period. The highest percentage of loan was provided to consumption loan during FY 2006/07, to others in FY 2007/08, to finance, insurance and real sector in FY 2008/09 and 2009/10 and to construction sector in FY 2010/11. The highest percentage of loan was provided to finance insurance and real sector i.e. Rs. 1176.80 million out of Rs. 4038.60 million, which covered 29.14% in the FY 2008/09.

Similarly, the lowest percentage of total loan is occupied by different sectors like fishery, mining and local government, which is near to zero. Likewise, the construction loans and wholesaler and retailer loan are the major sector, which ranked 2nd and 3rd respectively in terms of proportion during the study period. As per the above table, it can be concluded that the amount of loan offered to agriculture sector was in decreasing trend where as other sectors are in fluctuating trend from the FY 2006/07 to FY 2010/11.

The table 4.13 also shows the average loan of SBL in the five years period on different sector. According to the table highest loan was flowed in the finance, insurance and real sector i.e. Rs. 3062.60 million in five years period. Likewise it seems that the lowest average loan was disbursed to the fishing, mining and local government sector in the five years period which was equal to zero. The total loan & advances made by the bank on different sector in five consecutive years can be shown from the following figure;

Figure 4.1
Sector-wise Loan Classification of SBL



Source: Table 4.13

The above diagram shows proportion of outstanding loans of SBL on different sectors. The figure 4.1 demonstrates the fact that finance, insurance and real sector and construction sector occupied highest part of figure, then after wholesaler and retailer, consumption loan and others sector loan respectively. Likewise from the above figure, it is clear that the mining, fishing and local government sector has not covered the any part of the total loan outstanding.

4.1.6 Security wise Loan Classification

Commercial bank's main function is to collect money as a deposit from different client and borrow loan from other bank, government and NRB. This collected money is reinvested as a loan and advances to client. Bank creates profit from difference of interest rates between borrowing and lending money. Credit is an important function of bank with a lot of risk. Money being invested at right business organization, profitable organization is necessary to earn profit. If bank invested huge amount at wrong place due to miss calculation, it is reason of loss. Banks survives with profit depend upon the right lending. The bank has provided

loan and advances to its customer on the basis of different acceptable securities. The major securities are; movable/ immovable securities (including gold & silver, land & buildings, hypothecation, pledge) government guarantee, government bond, receipt of fixed deposit, counter guarantee, personnel guarantee etc. The outstanding of loans and advances which were provided by the bank on the basis of different sectors are as follows.

Table 4.14
Security wise Loan Classification of SBL

(Rs. In Million)

Description	2006/07		2007/08		2008/09		2009/10		2010/11	
	Amt	%	Amt	%	Amt	%	Amt	%	Amt	%
Movable/Immovable Assets	1,141	76	2,072	82	3,497	87	4,538	88	6,016	93
Guarantee of Local Licensed Institutions	-		-		-		-		-	
Government Guarantee	-		-		-		-		-	
Internationally Rated Bank Guarantee	-		-		-		-		-	
Export Documents	-		-		-		-		-	
Own Fixed Deposit Receipt	361	24	461	18	540	13	390	8	137	2
Fixed Deposit Receipt of Other Licensed Institutions	-		-		-		-		-	
Government Bonds	-		-		-		-		-	
Counter Guarantee	-		-		-		-		-	
Personal Guarantee	-		-		-		4	0.07	3	0.05
Other Securities	-		-		-		214	4	280	4
Unsecured	-		-		-		-		-	
Total	1502	100	2533	100	4037	100	5,146	100	6,436	100

Source: Annual Reports of SBL

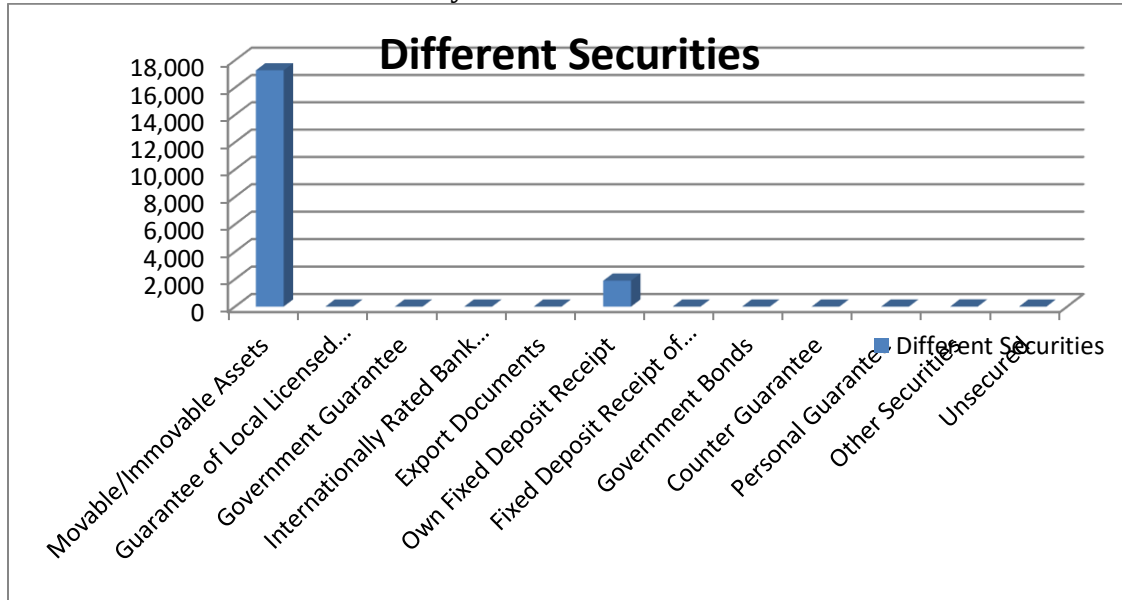
The above table 4.14 shows the loans outstanding amount and proportion of different securities in five consecutive years. According to the above table, it can be found that the SBL is providing loan and advances to its customers on the basis of different securities like movable & immovable security, guarantee of local institutions, government guarantee, receipts of fixed deposit, government bond, personnel guarantee etc. The ratio of security wise loan and advances ranged from 93% highest to 2% lowest during the study period. The moveable/immovable

security including gold & silver, land & building, plant & machinery, vehicle, hypothecation, pledge etc occupied the highest ratio of total loan and advances in all fiscal years. The amount of Rs. 1141 million was provided on the basis of moveable/immoveable security in the FY 2006/07, which covered the 76% of total loans and advances. The percentage of loan under such security is 82% in the FY 2007/08. Similarly the ratio of this security to total loan and advances were increasing trend, which were 87%, 88% and 93% in the FY 2008/09 to 2010/11 respectively.

Likewise, the lowest loan granted against personal guarantee during the study period. The amount of loan on such type of security was zero in FY 2006/07, 2007/08 and 2008/09. It was only Rs 4 million in the FY 2009/10, which covered only 0.07 % of total loan and advances. Similarly, it was reduced to Rs. 3 million in the FY 2010/11 covering only 0.05% of total, which was the lowest ratio.

The ratios of loan against the own fixed deposit receipts are increasing up to the FY 2008/09. The amount of loan against the own fixed deposit receipts is Rs. 361 million in the FY 2006/07, covering 24% of total loan. After, it increased to Rs. 461 and Rs. 540 million in FY 2007/08 and 2008/09 respectively. Then it is decreasing in last two years. The ratio of loan against own fixed deposit receipt are 8% and 2% in FY 2009/10 to 2010/11 respectively. As per the above table, it can be concluded that the amount of loan providing against moveable/immoveable securities were in increasing trend whereas loan against own fixed deposit receipt are in fluctuating trend and loan against personal guarantee and other securities are increasing. The total loan and advances made by the bank on different securities in five consecutive years can be shown from the following figure:

Figure 4.2
Security Wise Loan Classification



Source: Table 4.14

The figure 4.2 shows proportion of outstanding loans under different securities. The figure demonstrates the fact that movable and immovable security (including gold & silver, land & buildings, hypothecation, pledge) occupied highest part of total loan and advances during the study period, then after loan against own fixed deposit receipt and other securities respectively. Likewise from the above figure, it is clear that the guarantee of local licensed institutions, government guarantee, export documents, government bonds and personnel guarantee does not cover the part of the total loan outstanding.

4.1.7 Loan and Advances (Credit) to Total Deposit Ratio

Loan and advances (Credit) and deposits are the major functions of commercial banks. The relationship between these functions shows the efficiency, ability and idle resources of commercial banks. The ratio of loan and advances to total deposits i.e. (CD) ratio shows the effective utilization of collected resources from the public for the profit generating purpose. Higher ratio reflects higher efficiency of bank to utilize the collected resources and vice – versa. The following table

4.15 shows that how much the bank is successful in mobilizing the collected resources i.e. deposits collected from public in terms of loan & advances for the 6 years this research period.

Table 4.15
Comparative analysis of Loan and Advances to Total Deposit
(Rs. In Million)

Periods	Loan and Advances		Deposit Collection		CD Ratio
	Amount	%	Amount	%	
2006/07	1,487	7.65	1,823	8.58	81.57
2007/08	2,498	12.85	2,881	13.56	86.70
2008/09	3,992	20.54	4,418	20.80	90.37
2006/10	5,092	26.19	5,760	27.12	88.40
2010/11	6,371	32.77	6,357	29.93	100.23
Total	19,440.19	100	21238.37	100	
Mean	3,888		4,248		
S.D.	1,957		1,904		
C.V	0.5		0.44		

Source: Annual Reports of SBL

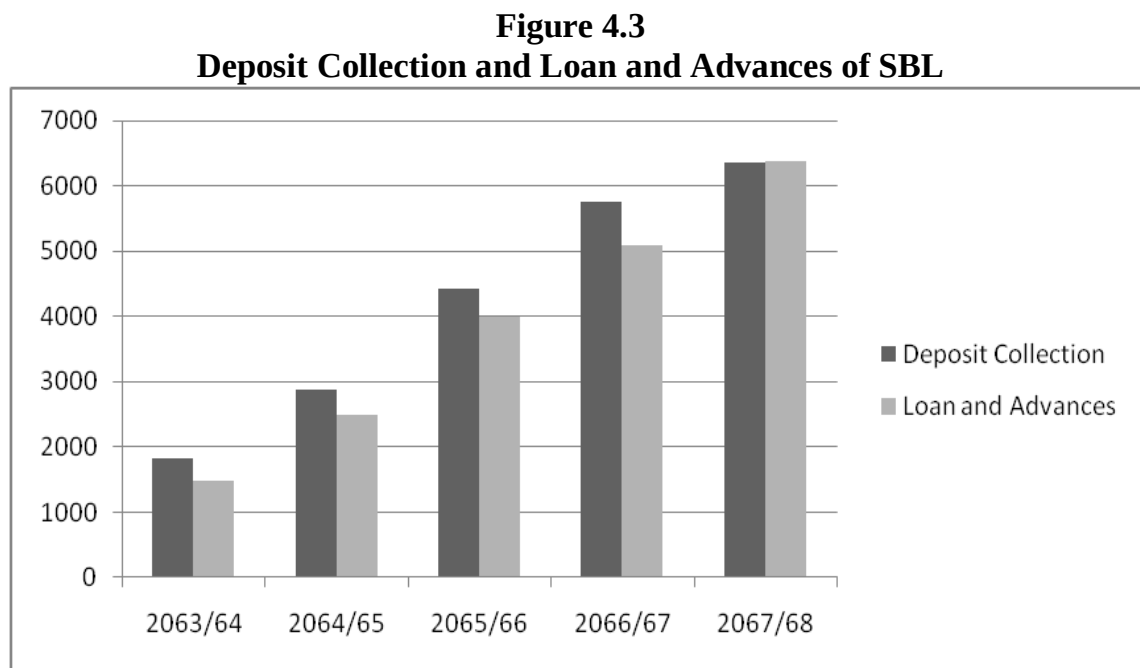
The above Table 4.16 shows that the SBL had the highest Credit Deposit (CD) ratio of 100.23 percent in the F.Y.2010/11 and the lowest ratio of 81.57 percent in the FY 2006/07 which revealed that the bank was able to utilize the maximum collected resources of Rs. 6371 million in the FY 2010/11 and minimum of Rs. 1847 million in the FY 2006/07. On the average of 5 years of research period, the mean CD ratio was 89.45 percent. Similarly, the mean of total deposit and loan and advances for the 5 years of period was Rs. 4248 million and Rs. 3888 million respectively and the coefficient of variation (CV) was 0.44 percent and 0.5 percent respectively. The higher the value of CV, the less will be uniformity and the smaller the value of CV, the more will be the uniformity.

Since the CV of total loan and advances was more in comparison with total

deposits, it has less uniformity & consistency with respect to total deposits.

The total deposit in the FY 2006/07 was Rs. 1823 million which was the smallest amount of deposit during the study period. From the FY 2007/08 it took its speed in increasing trend with the maximum deposit of Rs. 6357 million in the FY 2010/11. On the average of 5 years of study period, the bank became able to utilize the maximum percent of its collected resources in loan and advances. Since the bank has to bear high cost on its liquidity fund, the bank has managed to utilize the deposit fully by investing them in proper and safe way, so that the recovery can be done continuously without any additional new NPA or overdue loan in coming future.

The comparison between the deposit collected by the bank and loan & advances made by the bank for the 5 years from FY 2006/07 to FY 2010/11 can be shown from the following Figure:



Source: Table 4.15

From the above figure, it can be found that the bank does not have huge idle fund collected from the public during the study period. Since the bank has to pay

interest regularly and also has to bear other costs, it has invested in proper and safe way and earned more profit in order to strengthen the bank internally to compete with other joint venture banks.

4.1.8 Analyzing Loan Classification and Loan Loss Provision

Providing the loan to customer is an important & risk able function of every bank and financial institutions. The growth and advancement of financial institutions must depend upon the quality and quantity of the loan. Then the bank should be managed credit administration properly. Loan classification and loan loss provision is a system for managing credit risk.

Nepal Rastra Bank, which is the central bank of Nepal issues different directives from time to time to enhance the strength of bank. As per the NRB directive no 2 related to loan classification and loan loss provisioning on the credit, the bank and financial institutions should classify their loan and advances in four different categories and has to make provision for such classified loan are as follows:

<u>Category of Loan</u>	<u>Rate of provisioning</u>
Pass	1 percent
Sub-standard	25percent
Doubtful	50 percent
Loss (bad)	100 percent

Pass loan is called performing loan and others; sub-standard, doubtful & loss loans are called non-performing loans. The loan classification and loan loss provisioning of Sanima Bank for the 5 consecutive years are given below:

Table 4.16
Loan Classification of Loan as per Quality

(In Million)

Periods	Pass		Sub-Standard		Doubtful		Bad		Total Overdue	Total
	Amt	%	Amt	%	Amt	%	Amt	%		
2006/07	1501.92	100	0	0	0	0	0	0	0	1501.92
2007/08	2495.05	97.02	34.05	1.32	4.28	0.17	0.00	0	38.33	2533.38
2008/09	4029.92	99.65	3.30	0.08	0.00	0.00	3.77	0.09	7.07	4036.99
2009/10	5141.49	99.83	0.72	0.01	2.97	0.06	0.67	0.01	4.36	5145.85
2010/11	6435.90	99.99	0	0	0	0	0.29	0.004	0.29	6436.18

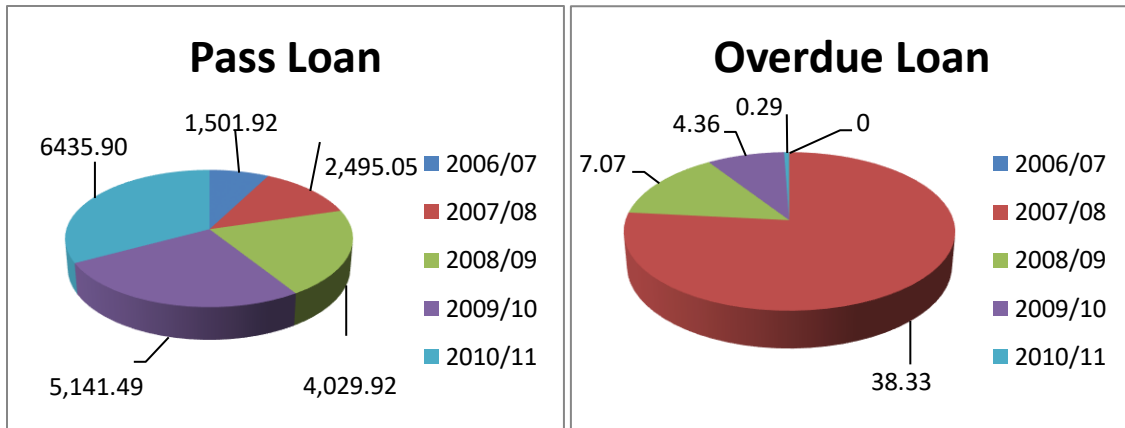
Source: Annual Reports of SBL

The above Table 4.17 exhibits the loan classification under the quality for five consecutive years. The amounts of pass loan ranged from Rs.1501 million to Rs. 6435 million during the study periods. From the table it is clear that the pass or performing loan of bank was in increasing trend from the FY 2006/07 to 2010/11. The amounts of pass loan were Rs. 2495, 4029 & 5141 million, in the FY 2007/08, 2008/09 and 2009/10 respectively. The proportion of pass loan out of total loan and advances were 100%, 97.02%, 99.65%, 99.83% and 99.99% in the five consecutive FY respectively. From the above table, it can be concluded that the proportion of pass loan which is the main source of income, have been increased throughout the study period.

The loans, which are due from the last 3 to 6 months, are categorized in sub-standard loan. The table shows that the amount of sub-standard loan ranged from 0.72 million to 34.05 million during the research period with in decreasing trend. The ratios of such loans lie between 1.32% to 0.01%. Likewise, the percentages of doubtful loan were 0.17% and 0.06% during FY 2007/08 and 2009/10 respectively. The loans, which are due from last one year, come under the category of loss. The ratios of loss loan were 0.09%, 0.01 and 0.004% during FY 2008/09, 2009/10 and 2010/11 respectively. According to the table, the sub-standard loan, doubtful loan and bad loan covers minor proportion of the total loan and

advances. There are different reasons contributing for the decrease in the level of NPL in SBL. Proper guiding rules, accountability and responsibility, good monitoring, proper lending system and good governance are some reasons for this.

Figure 4.4
Pass and Overdue Loan and Advances



Source: Table 4.16

The diagram 4.4 shows the classification of loan and advances into pass category and overdue category. From the above figure, it is cleared that the pass loan was in increasing trend throughout the study period. But the portion of pass category loan was increasing in the last four fiscal years study period. Likewise the overdue category loan was in decreasing trend throughout the five years of the study period.

Table 4.17
Loan Loss Provision as per the classification of Loan and Advances

(Rs. In Million)

Periods	Pass		Sub-Standard		Doubtful		Bad		Total	Upto Last Year	Cur. Year Change	Profit/Loss
	Amt.	%	Amt.	%	Amt.	%	Amt.	%				
2006/07	15.02	100.00	0.00	0.00	0.00	0.00	0.00	0.00	15.02	10.01	5.01	9
2007/08	24.95	70.08	8.51	23.91	2.14	6.01	0.00	0.00	35.60	15.02	20.58	19
2008/09	40.30	89.76	0.82	1.84	0.00	0.00	3.77	8.40	44.90	35.60	9.30	58
2009/10	51.41	95.66	0.18	0.33	1.49	2.76	0.67	1.25	53.75	44.90	8.85	86
2010/11	64.57	99.56	0.00	0.00	0.00	0.00	0.29	0.44	64.86	53.75	11.11	155

Source: Annual Reports of SBL

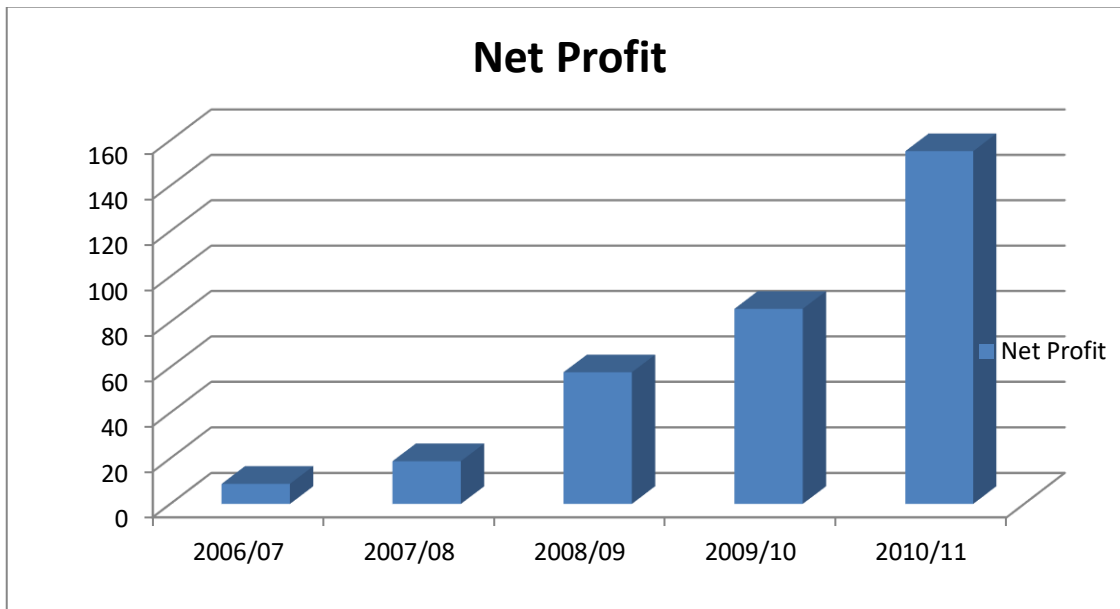
The above Table 4.18 shows the amount and percentage of loan loss provision maintained by SBL in different fiscal years. The percentage of provision on pass loan during the study period was found as 100%, 70.08%, 89.76%, 95.66% and 99.56% respectively. As per the NRB directives, the provision should have 1% of pass loan.

Similarly, as per the NRB directives, the provision should have 25%, 50% and 100% of sub-standard, doubtful and bad loan respectively. The loan falling under sub- standard, doubtful and loss categories is termed as Non-performing, which was in decreasing trend during the study period. The above table indicates that the percentage of provision for Non-performing is very low which exhibits the loan efficiency of the bank. The percentages of provision for sub-standard loan ranged from lowest 0.33% to highest 23.91%, for doubtful loan ranged from 2.76% to 6.01 % and for loss loan ranged from 0.44% to 8.40% in five consecutive years.

The amount of total loan loss provisions were Rs.15.02 million, Rs.35.60 million, Rs.44.90 million, Rs.53.75 million and Rs. 64.86 million in the five fiscal years respectively, which showed that the amount of total loan loss provision was in increasing trend from the FY 2006/07 to 2010/11.

There is adverse relationship between loan loss provision and profitability of bank. If amount of loan loss provision increases, there will decrease in amount of profit and vice versa. According to the above table, it found that the SBL had earned reasonable amount of profit, since there is minimal amount of loan loss provision as compared to the total loan and advances. Likewise the bank has been able to earn profit of Rs. 9, 19, 58, 86 and 155 million respectively during the consecutive fiscal years, whereas the amount of loan loss was very minimal as compared to the total loan and advances. It is cleared that the loan loss provision directly affects to Net profit.

Figure 4.5
Net Profit of the Bank



Source: Table 4.17

The figure 4.5 shows the Net profit position of bank during the study period of five consecutive years. As per the figure, the net profit of bank was minimal in the first two fiscal years. The SBL's profit position is in increasing trend from the FY 2006/07 to FY 2010/11. It can be found that the bank has been able to earn accumulated profit of Rs. 155 million in the last fiscal years.

4.1.9 Performing and Non-performing Loan & Advances of SBL

Pass loans are those loans that repay principle and interest timely to the bank from the cash flow it generates. As per NRB directives the loans classified as pass category is termed as per performing loan. Performing loans to total loans and advances ratio determines the proportion of performing loans in the total loan portfolio. Higher ratio implies the good quality of loans of the banks. It should be 100 percent for the better performance and good financial health of the bank. As per NRB directives the loan falling under category of sub-standard, doubtful and loss are regarded as non- performing or overdue loan. Higher ratio implies the bad quality of assets of banks in the form of loan and advances. Hence lower NPL to total credit ratio is preferred. As per the

international standard only 5% NPL is allowed but in the context of Nepal 10% NPL is acceptable.

Table 4.18
Comparative analysis of Pass and Overdue Loan and Advances
(In Million)

	Performing Loan	PL %	Non-Performing Loan	NPL %	Total Loan
2006/07	1,501.92	100	0	0.00	1501.92
2007/08	2,495.05	98.49	38.33	1.51	2533.38
2008/09	4,029.92	99.82	7.07	0.18	4036.99
2009/10	5,141.49	99.92	4.36	0.08	5145.85
2010/11	6435.90	99.996	0.29	0.004	6436.18
Mean		99.64		0.36	
S.D.		0.65		0.65	
C.V		0.0065		1.83	

Source: Annual Reports of SBL

The above Table 4.19 shows the performing loan, non-performing loan and total loans and advances of the bank for five consecutive years. The overall ratios of performing loan and Non-performing loan (NPA percent) had been ranged from 98.49% to 100% and 0% to 1.51% respectively in five consecutive years. The table shows that the performing loan was in increasing trend in the study period i.e. the FY 2006/07/ to 2010/11. The performing loan was Rs. 1501 million in the FY 2006/07, which was the 100percent of total loan and advances. After increasing, it reached 6435 million the FY 2010/11, which constitutes 99.996% of the total loan. According to the above table, it can be concluded that the amount of performing loan of Sanima Bank was in increasing trend during the study period.

Similarly, the above table indicates that the Non-performing loan and NPA percent of bank was in decreasing trend in the last three years of period. The overdue loan of bank was Rs. 0 million in the FY 2006/07, which was 0% of total loan and advances. The NPL reached to Rs. 38.33 million in the FY 2007/08, after which NPL has decreased to Rs. 7.07 million in the FY 2008/09. Then again NPL further decreased to 4.36% and 0.29% of the total loan in the FY 2009/10 and 2010/11.

The mean ratio and standard deviation of performing loan were 99.64 and 0.65, respectively. Likewise they were 0.36 & 0.65 in the case of Non- performing loan. Thus it signifies that the Non- performing loan has higher degree of variation and the performing loan has lower degree of variation in this ratio.

4.1.10Analyzing Interest Income Generating from credit to Total Income

Profit is the ultimate goal of every commercial bank. They involve in business for making profit. Profit cannot be achieved easily. It should be managed well with better managerial skills. There are different sources of income which generate profit in the bank. Income from interest of commercial bank is a main source of income. The interest income is received from providing credit facility to various manufacturing, non-manufacturing industries, service sector business as well as financing to government bond, debt, company's debenture etc. Although, interest income receives from various sources, the interest income generating from loan and advances cover huge proportion out of total income of bank. Total income includes interest income, commission & discount, exchange equalization income, non-operating income, other income and writes back provision for possible losses etc. The interest income and total income of bank are presented below.

Table 4.19
Interest Income from Loan to Total Income

(Rs. In Million)

Period	Interest Income from Loan & Advances	Total Income	Ratio(%)
2006/07	60.83	66.22	92
2007/08	124.80	130.65	96
2008/09	358.55	396.85	90
2009/10	615.64	655.93	94
2010/11	1038.46	1078.72	96
Total	2198.28	2328.37	
Mean	439.66	465.67	
S.D.	399.61	414.89	
C.V.	0.91	0.89	

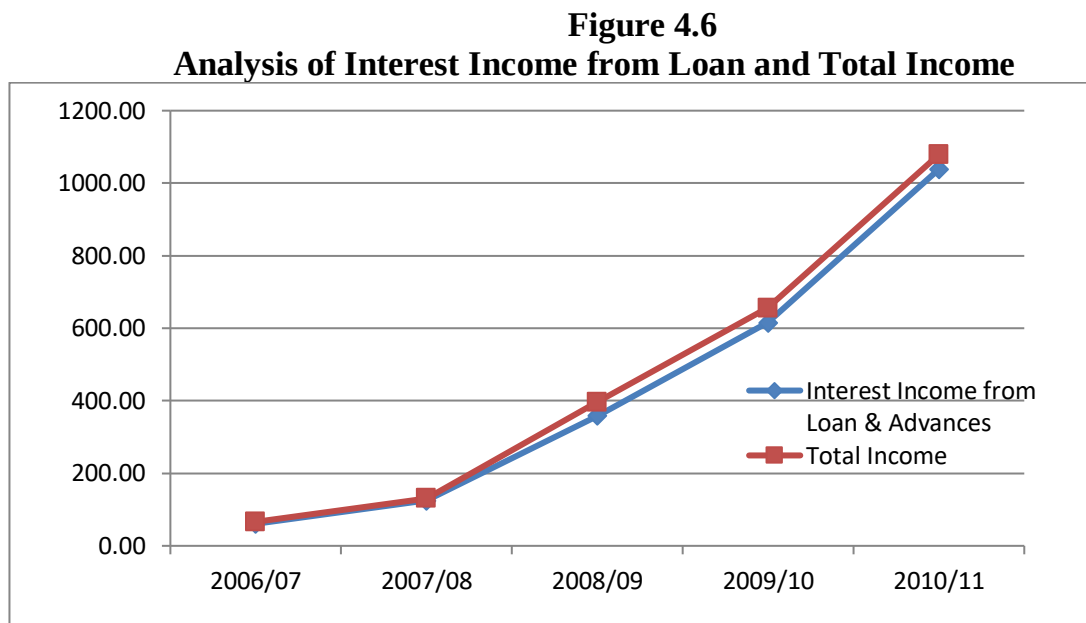
Source : Annual Reports of SBL

The Table 4.20 shows the comparative analysis of interest income generating from loan and advances which is the main source of bank for five consecutive years. The ratio of interest income from credit to total income ranged from 96% highest ratio in the FY 2010/11 to 90% the lowest ratio in the FY 2008/09. According to the table, interest income was Rs. 60.83 million in the FY 2006/07, which occupied 92% of total income i.e. Rs. 66.22 million. After increased than previous year, it reached to Rs. 124.80 million in the FY 2007/08, which occupied 96% of total income. Similarly, the interest incomes were Rs. 358.55, Rs. 615.64 and Rs. 1038.46 million whereas total incomes were Rs.396.85, Rs. 655.93 and Rs. 1078.72 million in the FY 2008/09 to 2010/11 respectively. As per the above table it can be found that the interest income was in increasing trend, which ranged between Rs. 60.83 million to Rs. 1038.46 million. On the other hand the total income of bank is also in the increasing trend during the study period.

The above table also shows that the proportion of interest income were 92%, 96%, 90%, 94% and 96% out of total income of bank in the FY from 2006/07 to 2010/11 respectively. Which proportion indicates that the interest income generating from loan and advances played the major role to total income of bank. As a result it can be concluded that the interest income is major source of every bank's total income.

The standard deviation of interest income generated from loan and advances and total income were 399.61 and 414.89 respectively. Thus it signified that the interest income had lower deviation with lower degree of variation and total income had higher deviation with higher degree of variation.

The interest income generated from loan & advances and total income received by the bank in five consecutive years can be shown from the following Figure:



Source: Table 4.19

The diagram 4.7 shows amount & proportion of interest income received from loan and advances of Sanima Bank in during the study period. From the figure 4.7 demonstrates fact that the interest income generating from loan and advances was in slightly increasing than the previous years where as the total income of bank was in increasing trend.

4.1.11 Correlation Analysis

Correlation may be defined as the degree of linear relationship existing between two or more variables. The variable are said to be correlated when the change in the value of one results change in another variable.

4.1.11.1 Correlation between Loan & Advances and Loan Loss Provision

The correlation between loan and advances and loan loss provision shows the degree of relationship between these two items. How a unit increment in loan and advances affect the loan loss provision is measured by this correlation. Here loan and advances is independent variable and LLP is depending variable.

Table 4.20
Correlation between Total Loan and Advances and LLP
(Rs. In Million)

Periods	Total Loans	Loan Loss provision
2006/07	1501.92	15.02
2007/08	2533.38	35.60
2008/09	4036.99	44.90
2009/10	5145.85	53.75
2010/11	6436.18	64.86
Total	19654.31	214.13
Correlation, r	0.98	
t-test	Calculated t=8.52	Tabulated t=2.31

Source: Appendix III (A)

Above table 4.21 explains the relationship between loan and advances and loan loss provision. Here the correlation coefficient between loans and loan loss provision was 0.98. It shows that there was the positive correlation between two variables. Comparing calculated' with tabulated', it can be said that there was significant relationship between them because; calculated't' was greater than tabulated't'. In other words, the total LLP of SBL was positively correlated with the NPL, increased in LLP was due to increase in total loan and advances.

4.1.11.2 Correlation between Non- performing Loan and Loan and Advances

The correlation between NPL and loan & advances shows the degree of relationship between these two items. How a unit increment in loan & advances affect the NPL measured by this correlation. Here loan & advances is independent variable and NPL is

depending variable.

Table 4.21
Correlation between Total Loan and Advances and NPL
(Rs. In Million)

Periods	Total Loans	NPL
2006/07	1501.92	0
2007/08	2533.38	38.33
2008/09	4036.99	7.07
2009/10	5145.85	4.36
2010/11	6436.18	0.29
Total	19654.31	50.04
Correlation, r	-0.37	
t-test	Calculated t=-0.69	Tabulated t=2.31

Source: Appendix III (B)

The above table 4.22 shows the relationship between non-performing loan and loan advances. Here the correlation coefficient between loan and advances and NPA loan was -0.37. It shows that there was the negative correlation. Comparing calculated, 't' with tabulated, 't', it can be said that there was no significant relationship between them because; calculated, 't' was less than tabulated 't'. In other words, the total NPA loan was positively correlated with the total loan and advances. The decrease in NPL was due to increase in total loan and advances in study period.

4.1.11.3 Correlation between Performing Loan and Loan and Advances

The correlation between PL and loan & advances shows the degree of relationship between these two items. How a unit increment in loan & advances affect the PL measured by this correlation. Here loan & advances is independent variable and PL is depending variable.

Table 4.22
Correlation between Total Loan and Advances and Performing Loan

(Rs. In Million)

Periods	Total Loans	Performing loans
2006/07	1501.92	1,501.92
2007/08	2533.38	2,495.05
2008/09	4036.99	4,029.92
2009/10	5145.85	5,141.49
2010/11	6436.18	6435.90
Total	19654.31	19604.27
Correlation, r	0.99	
t-test	Calculated t=12.15	Tabulated t=2.31

Source: Appendix III (C)

The table 4.28 explains the relationship between performing loan and loan advances. The correlation coefficient between loan and advances and performing loan was 0.99. It shows that there was the positive correlation between two variables. The value of calculated, 't' was greater than tabulated, 't' so, the relationship is said to be significant. It means increase in total loans had led to increase in performing loans. The total performing loans of SBL was positively correlated with the total loan and advances. The correlation coefficient was positive because the total loans and advances and performing loans both were increasing in the five years of period.

4.1.11.4 Correlation between Non-Performing Loan and Net Profit

The correlation between NPL and Net profit shows the degree of relationship between these two items. How a unit increment in NPL affect the Net Profit is measured by such correlation.

Table 4.23
Correlation between NPL and Net profit

(In Million)

Periods	NPL	Profit/Loss
2006/07	0	8.78
2007/08	38.33	18.74
2008/09	7.07	57.75
2009/10	4.36	85.73
2010/11	0.29	155.22
Total	50.04	326.25
Correlation, r	-0.45	
t-test	Calculated t=-0.87	Tabulated t=2.31

Source: Appendix III (D)

The table 4.24 explains the relationship between the net profit and non-performing loan and advances. The correlation coefficient between net profit and NPA loan was -0.45. It shows that there was the negative or adverse correlation. The value of calculated, 't' was lesser than tabulated, 't', so the correlation said to be non-significant. That means decrease in NPL had no contribution to the increase in total profit. The Net Profit of SBL was negatively correlated with the NPL. The correlation coefficient was negative as the net profit was in increasing and NPL was in decreasing trend during the FY 2006/07 to 2010/11. It means the bank was able to earn reasonable profit due to downsizing the NPL in the last four years.

4.1.12 Trend Analysis

In this chapter, examines the trend analysis of deposit, loan and advances and net profit and forecast trend for next five years. The measures of trend analysis show the behaviours of given variables in series of time. Commercial bank does not carry consistency overall the period. Sluggish economic situation, internal security situation, and other various factors affects in performance of the commercial banks. The objectives of this analysis are to analyse the trend of deposit collection, its utilization as a loan and advances and return as net profit of SBL.

4.1.12.1 Trend Analysis of Total Deposit

Deposit is one of the major liabilities of commercial banks. Its trend is determined by various factors. Under this chapter, the trend values of deposit of SBL for five years have been calculated from the F.Y. 2011/12 to 2015/16 to forecast for next five years from the F.Y. 2011/12 to 2015/16. The following table shows trend value of deposits for next five fiscal years.

Table 4.24
Trend Value of Total Deposit of SBL
(In Million)

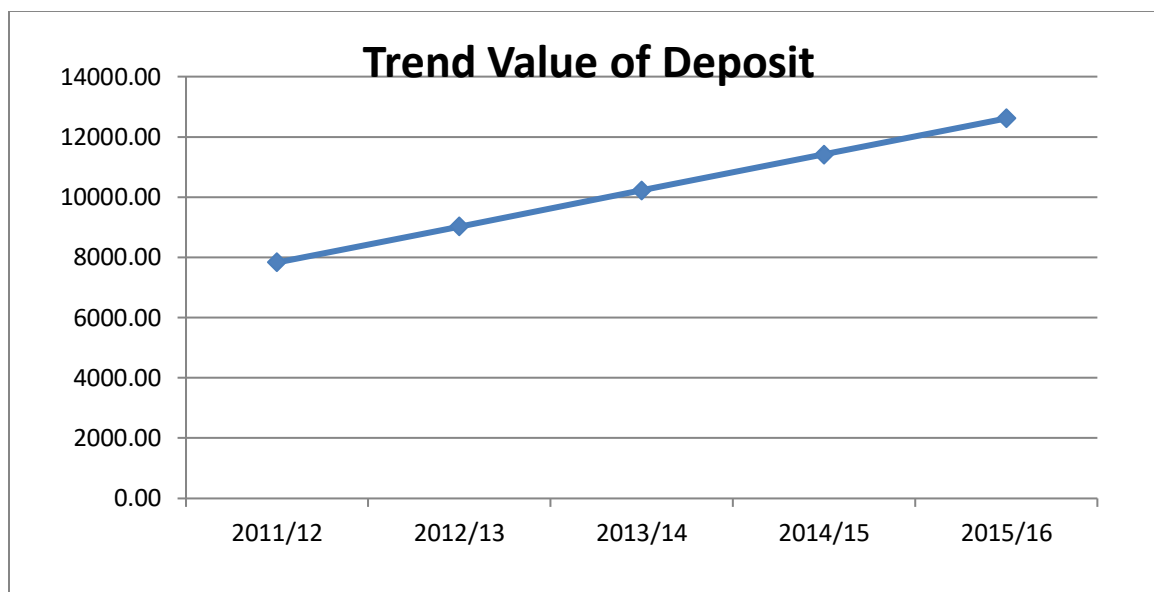
Periods	Trend Value of Deposit
2011/12	7831.95
2012/13	9026.71
2013/14	10221.47
2014/15	11415.23
2015/16	12610.99

Source: Appendix IV (A)

The above table shows the trend behaviour of total deposit in SBL. It was increasing trend other thing remaining the same, the total deposit of SBL in end of FY 2015/16 is predicted to be Rs. 12610.99 million, which is the highest amount of bank during the study period.

The calculated value of trend of total deposit is presented in graph as trend line as follows.

Figure 4.7
Trend Value of Deposit



Source: Table 4.24

The figure 4.8 shows the trend value of deposit of SBL. It was increasing trend during the study period. As per the figure, the trend value of total deposit of bank was Rs. 7831.95 million in the F.Y. 2011/12. Likewise the trend values of deposits were Rs. 9026.71, 10221.47, 11415.23 and 12610.99 in the F.Y.2012/13 to 2015/16 respectively. As per the figure, it can be forecasted that, the total deposit of bank will be in the increasing trend, if other things remaining the same.

4.1.12.2 Trend Analysis of Loan and Advances

Lending is one of the major functions of commercial banks; its trend is determined by various factors. Under this topic, the trend values of loan and advances of SBL for five years from the F.Y. 2011/12 to 2015/16. The following table shows the trend value of loan and advances for five years from the F.Y.2011/12 to 2015/16.

Table 4.25
Trend Value of Total Loan and Advances of SBL

(In Million)

Periods	Trend Values of Loan and Advances
2011/12	10104.09
2012/13	11340.41
2013/14	12576.73
2014/15	13813.05
2015/16	15049.37

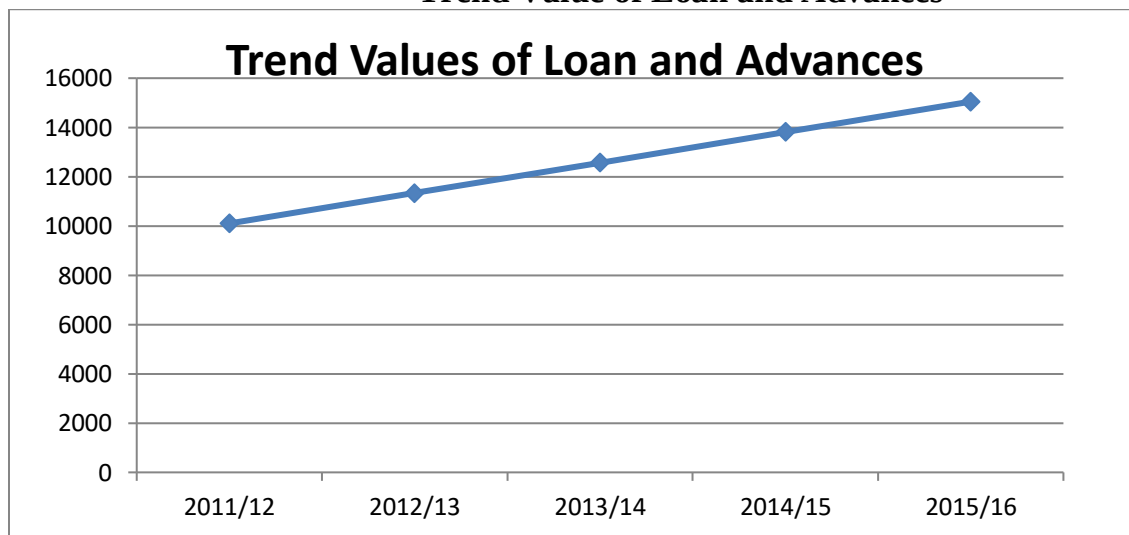
Source: Appendix III (B)

The above table shows the trend behaviour of total loan and advances of SBL. It was increasing trend other thing remaining the same, the total loan and advances of SBL in end of FY 2015/16 is predicted to be Rs. 15049.37 million, which is the highest amount of bank during the study period.

The calculated value of trend of total deposit is presented in graph as trend line as follows.

Figure 4.8

Trend Value of Loan and Advances



Source: Table 4.25

The figure 4.9 shows the trend value of loans and advances of SBL. It was increasing trend during the study period. As per the figure, the trend value of total deposit of bank was Rs. 10104.09 million in the F.Y. 2011/12. Likewise the trend values of deposits

were Rs. 11340.09, 12576.73, 13813.05 and 15049.37 in the F.Y.2012/13 to 2015/16 respectively. As per the figure, it can be forecasted that, the total loans of bank will be in the increasing trend, if other things remaining the same.

4.1.12.3 Trend Analysis of Net Profit

Net profit measures the success of a firm in every aspects of its operation and strategy, its trend is determined by various factors. Under this chapter, one can calculate the trend values of Net Profit of SBL for five years from the F.Y. 2011/12 to 2015/16.

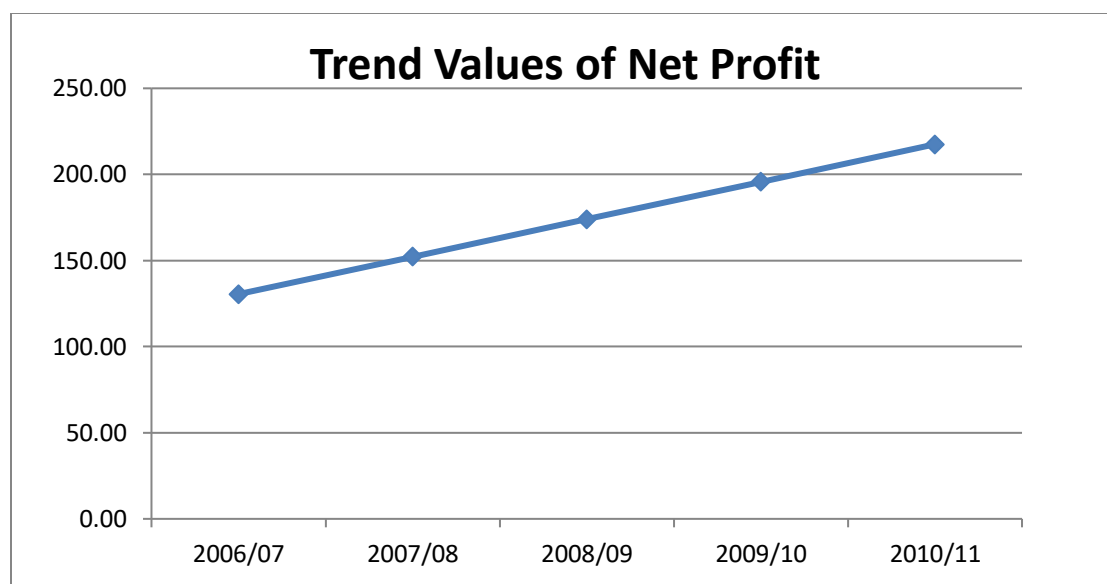
Table 4.26
Trend value of Net Profit
(In Million)

Periods	Trend Values of Net Profit
2011/12	135.50
2012/13	152.25
2013/14	174.00
2014/15	195.75
2015/16	217.50

Source: Appendix III (C)

The above table shows the trend behaviour of Net Profit of SBL, which is in increasing trend from 2011/12 to 2015/16. Other things remaining the same, the net profit of SBL will be Rs. 135.50, 152.25, 174, 195.75 and 217.50 million during FY 2011/12 to 2015/16. The calculated behaviour of trend analysis of net Profit predicted in the trend line as follows.

Figure 4.9
Trend Value of Net Profit



Source: Table 4.26

The figure 4.10 shows the trend value of net profit of SBL. As per the figure, the trend value of net profit of bank is increasing. As per the figure, it can be forecasted that, the net profit of bank will be Rs. 217.50 millions in the F.Y.2015/16, other things remaining the same.

4.2 Analysis of Primary Data

Table 4.27
Key Risk in SBL

S.N.	Risk	1	2	3	4	Total	Weight Value	Mean	Rank
1	Credit Risk	12	2	1	0	15	19	1.26	1
2	Liquidity Risk	2	3	4	6	15	44	2.93	3
3	Interest Rate Risk	1	8	6	0	15	35	2.33	2
4	Exchange Risk	0	2	4	9	15	52	3.47	4
Total		15	15	15	15				

Source: Survey, 2012

In above table there is ranking of the risk of SBL. The key risk of SBL is credit risk. The researcher has visited the bank and has asked the fifteen staffs of the bank which is the key risk of your bank? The respondent answered this question. Out of total respondent twelve respondents assigned first rank to the credit risk. Similarly two respondents gave first rank to the liquidity risk, one gave interest rate risk and nobody gave exchange risk. However, using statistical tools of ranking, out of fifteen respondents they give first rank

to the credit risk, second rank in interest rate risk, third in liquidity risk and fourth in exchange risk.

Table 4.28
Basis of Loan

S.N.	Steam	1	2	3	4	5	Total	Weight Value	Mean	Rank
1	Collateral	7	8	0	0	0	15	23	1.53	1
2	Profitability of Business	8	7	0	0	0	15	22	1.46	2
3	Projected Financial Statement	0	0	3	4	8	15	65	4.33	5
4	Image of Business	0	0	5	6	3	15	54	3.6	3
5	Image of Business Person	0	0	7	5	4	15	61	4.06	4
Total		15	15	15	15					

Source: Survey, 2012

In the above table the respondents were asked to rank the basis of loan to the applicants. Fifteen respondents answered this question. The respondent gave first rank to the collateral; second profitability of the business, third image of the business, fourth image of the business person and fifth projected financial statement.

Table 4.29
Default Loan should berescheduled

S.N.	S.N.	Number	Percent
1	Yes	3	20
2	No	12	80
	Total	15	100

Source: Survey, 2012

The majority of staff said that default loan should not be rescheduled. But, three respondents have said that default loan should be rescheduled.

Table 4.30
Remedies of Recovering Loan

S.N.	Steam	1	2	3	4	5	Total	Weight Value	Mean	Rank
1	Collateral	6	4	3	2	0	15	31	2.07	2
2	Guarantor	0	2	3	4	6	15	59	3.93	4
3	Counseling	1	2	5	3	4	15	52	3.47	3
4	Technical Support	0	2	2	6	5	15	59	3.93	4
5	Follow Up	8	5	2	0	0	15	24	1.6	1
Total		15	15	15	15	15				

Source: Survey, 2012

In above table the majority of staffs are willing to use follow up action as the instrument for the recovery of loan provided to the business. So out of fifteen respondents eight respondents said the bank should adopt follow up method. By analysing these data using statistical tools respondents gave first rank in follow up method, second in collateral, third in counselling. Respondents assigned both, guarantor and technical support, as fourth rank.

Table 4.31
Percentage of Loan to Total Requirement

S.N	Alternative	Number	Percent
1	Above 50%	1	6.67
2	Above 60%	12	80
3	Above 70%	2	13.33
	Total	15	100

Source: Survey, 2012

The respondents agree granting loan is generally above 60 percent of total requirement of the business. In this regard, 13.33 percent respondents have willingness to provide above 70 percent and 6.67 percent respondents have willingness to provide above 50 percent of requirement of fund as loan to the applicants. Though the above percentages have been assigned by respondent, they were verbally agreed with the researcher that the most of the loan and advances has been granted under the guidelines of credit policy of the bank.

Table 4.32
Any Problem Related to NRB

S.N	Alternative	Number	Percent
1	Yes	0	0
2	No	15	100
	Total	15	100

Source: Survey, 2012

Cent percent of the respondents said that they did not have faced any problem related to NRB. It shows that they are fully satisfied towards the regulatory body.

Table 4.33
Need of Assets Management Company

S.N	Alternative	Number	Percent
1	Yes	9	60
2	No	6	40
	Total	15	100

Source: Survey, 2012

Majority of the respondents said that there is the need of assets management company for recovery from the non-performing assets viz a viz land, building etc. 60 percent of respondents agreed the need of assets management company for NPA management of the bank and financial institutions. Rest of the respondents did not felt need of the same company for the purpose.

Table 4.34
Support of Judiciary Help

S.N	Alternative	Number	Percent
1	Yes	13	86.67
2	No	2	13.33
	Total	15	100

Source: Survey, 2012

Out of fifteen respondents, 86.67 percent said that judiciary should help bank and 13.33 percent said not need of judiciary help. So, majority of the staff felt support of judiciary help.

Table 4.35
Verification of Collateral before Granting Loan

S.N	Alternative	Number	Percent
1	Office Staff	7	46.67
2	Related Specialist	8	53.33
3	Independent Person	0	0
	Total	15	100

Source: Survey, 2012

Out of fifteen respondents, 66.67 percent respondents said that related specialist should involve in the verification of properties being kept as collateral before granting loan, 58.33 Percent respondents said that office staff should do that work and nobody said independent person should take involvement in verification of collateral.

Table 4.36
Source of credit risk

S.N	Alternative	Number	Percent
1	Increase In Interest Arrears	6	40
2	Not Paying Attitude of Loan Taker	5	33.33
3	No Profitability of Loan Taker	4	26.67
	Total	15	100

Source: Survey, 2012

Out of fifteen respondents, 40 percent respondent said that a source of credit risk is increase in interest arrears. Similarly 33.33 percent respondents said not paying attitude of loan taker and 26.67 percent said no profitability of loan taker.

Table 4.37
Information about Customer

S.N	Alternative	Number	Percent
1	Yes	15	100
2	No	0	0
	Total	15	100

Source: Survey

All of the respondents said that the bank should receive regular information about their customer's business.

4.12 Major Findings

- i. Sanima Bank Limited is the 32nd commercial bank of the country, which was recently promoted to commercial bank from development bank with the deposit, loan portfolio and net profit of Rs. 6356.74, Rs. 6371.32 and Rs. 155.22 million respectively in the FY 2010/11.
- ii. During the study period total good loan increased to Rs 6435.90 million with improved credit portfolio concentration across the diversified sectors and NPA reduced to 0.004% from 1.51% with total bad loan recovery of Rs. 4.15 million during the study period.
- iii. The analysis of the total loan and advances against total deposit revealed that the CD ratio of bank decreased to 81.57% from 100.23% in five consecutive years of study period. It showed that the collected deposit of bank was fully utilized as loan and advances.
- iv. The analysis of liquidity ratio revealed that the liquidity ratio of bank was satisfactory in terms of standard norms over five year's study period. The calculated ratio indicated that the bank is in satisfactory liquidity position.
- v. The sector wise loan classification ratio indicated that SBL disbursed average amount of total loan and advances in every sector except mining, fishery and local government.
- vi. The loan loss provision has increased to Rs. 64.86 million from Rs. 15.02 million during the study period. It showed that the proportion of non-performing loan of bank has been increasing, but is not due to the increase in non-performing loan, it is due to the increase in the total loan and advances.
- vii. The ratio of performing loan to total loan and advances of bank has remained constant within 98% and 100% during the study period. It showed that the bank has not suffered from the problem of NPA loans during the five years of study period.
- viii. The main objective of commercial bank is to earn profit through mobilization of fund. The average ratio of return on loan and advances is in positive sign, which revealed that SBL has succeeded to earn return on loan and advance during the study period.

The bank has been able to increase its net profit with the increase in interest income

- ix. The correlation coefficient between loans & advances and loan loss provision of SBL was 0.98. Here, calculated ' t '=8.52 is greater than tabulated ' t '=2.31. Hence, the relationship between loan and advances and LLP is significant.
- x. The degree of relationship between NPL and loan & advances was found to be -0.37. It showed that there is a negative correlation coefficient between them. Here, calculated ' t '=-0.69 is less than tabulated ' t '=2.31. Hence, the relationship between loan and advances and NPL is insignificant.
- xi. The degree of relationship between performing loan and loan & advances was found to be 0.99. It showed that there was a positive correlation between two variables during the study period. Here, calculated ' t '=12.15 is greater than tabulated ' t '=2.31. Hence, the relationship between loan and advances and performing loan is significant.
- xii. The degree of relationship between net profit and NPL was negative i.e. -0.45, which showed that there was a negative correlation between them. Here, calculated ' t '=-0.87 is less than tabulated ' t '=2.31. Hence, the relationship between LLP and Net profit is insignificant.
- xiii. The trend behaviour of total deposit, total credit and net profit in SBL is in increasing trend during the study period. The total deposit, loan and net profit of SBL will be Rs. 12610.99, Rs. 15049.40 and Rs. 217.50 million respectively in the F.Y. 2015/16 if other things remain constant.

CHAPTER-FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The study basically focuses on the credit management of Sanima Bank Limited out of 32 commercial banks of Nepal that covers the period from FY 2006/07 to 2010/11.

In this study, Introduction is the first chapter. Under this chapter, nine sub topics have been presented namely general background, credit management, commercial banks and the economy, brief profile of the Sanima Bank Limited, statement of the problem, objectives of the study, significance of the study, limitations of the study and organization of the study. Under the sub-topic credit management, general explanations of the credit management have been done. Sub-top commercial banks and the economy include the brief description about the commercial banks of Nepal and the effect of banking industry in the economy. Brief profile of Sanima Bank Limited includes its history, share holding pattern and products and services etc.

In the second chapter literature review, there are mainly three sub heading namely, conceptual review, review of legislative provision and review of past thesis. The researcher has used different books, reports, journals and research studies published by various institutions, unpublished dissertations submitted by master's level students in order to review the credit management. In this section definition, types of credit, process of loan disbursement, lending principles, management of loan recovery and other matters related with credit management has been discussed. Similarly, the legislative provisions put forward by NRB have also been discussed in this section. The review of the past theses submitted by the master's level students under the topic "Credit Management" has also been done. Finally, research gap has been presented citing the gap between the previous studies and this study.

Research Methodology is the third chapter, which gives the brief definitions and explanations about the research design, nature and sources of data, population and samples, respondent profile and method of data analysis which have been used in this

study. In case of research design, descriptive analysis has been adopted and for sources of data, both primary and secondary data have been used. Financial as well as statistical tools have been used while analysing the data. Different financial tools and statistical tool which have been used are briefly defined in this section. Under financial tools, liquidity ratios, asset management ratios, profitability ratios and lending efficiency ratios have been used. Statistical tools like mean, standard deviation, coefficient of variation and t-test have been used.

Data Presentation and analysis is the fourth chapter under which data analysis have been done using various financial tools and statistical tools. The data have been presented in tabular and graphical forms. Under the liquidity analysis, NRB balance to total deposits, cash balance to total deposits and liquid fund to total deposits ratios have been calculated. Under the profitability ratio, interest income to total income, interest income to interest expenses and return to loan and advances ratios have been calculated. Total assets to total liabilities, loan and advances to total assets and total loan and advances to total deposit ratios have been calculated under the asset management ratio. LLP to total loan and advances, NPL to total loan and advances and performing loan to total loan and advances ratios have been calculated under the lending efficiency ratio. Sector-wise loan and security-wise loan, LLP, performing and non-performing loan and interest income to SBL has been studied in detail in this chapter. Further, correlation between loan and advances and LLP, NPL and loan and advances, performing loan and loan and advances and NPL and Net profit have also been analysed. Similarly, trend analysis of loan and advances, deposit collection and net profit of SBL for the next five years has been done.

5.2 Conclusions

The loan management of SBL is not only necessary but also compulsory for better performance of the organization. This study is just a small part to fulfil the partial requirement of MBS. Therefore, it helps to improve and draw attention to bring some improvement in loan management of SBL.

Despite the fact that there is fierce competition among the financial institutions the deposit collection of the SBL is satisfactory and it is in increasing trend. It demonstrates that the bank has good corporate image in the industry. Although there is narrow area of investment, and cut throat competition in banking sector, loans and advances of the SBL showed continuous increasing trend, which represents the credit efficiency of the bank. During the study period it is found that deposit collection is greater than loan and advances which mean all deposits are not utilized in loan and advances but still CD ratio of the bank is unacceptable level. Further, the bank has been able to minimize its risks by diversifying the loan and advances in the different sectors and has also minimized its default risk by disbursing loan against the different adequate securities. The non-performing loan of the bank is in decreasing trend with the increase in total loan and advances which demonstrates the overall credit efficiency of the bank. Similarly, the LLP of the bank is also increasing but it is not due the increase in bad loan instead it is due to the increase in performing loan, since 1% LLP is compulsory for performing loans also. The major portion of the total income has been occupied by the interest income, so bad loans and LLP has directly affected the profitability.

The major conclusions drawn from the primary data collated are the highest risk of SBL is in credit risk, collateral is the main factor of disbursing the loan. Most of the staff have said that default loan should be rescheduled. Follow up is the main instrument of remedies of the recovery of loan, the loan and advance should be given above 60% of the total requirement of the business and all staffs reported no problem related to NRB. Accordingly, most of the staff has realized the importance of Asset Management Company, support of judiciary help and related specialist in verification of collateral. The main source of credit risk is increase in interest arrears and the bank should receive regular information about consumers business.

5.3 Recommendations

For the better improvement of the "Loan Management of the SBL" some suggestions and recommendation have been portrayed on the basis of analysis and conclusion of the entire

research study.

Being a youngest commercial bank SBL must be very careful in formulating the marketing strategies to serve its customers. The marketing strategy should be innovative that would attract and retain the customers. The bank should develop an innovative approach to promote the bank for its wellbeing and sustainability in the market. As the bank was promoted to 'A' class commercial bank from 'B' class development bank, it should comply all the requisites of the commercial banks as prescribed by Nepal Rastra Bank. Excess concentration of loan lending on some certain area depicts the fact that people lack in identifying new innovation. Most of the people do similar types of business thinking to have more return. This germinates excess competition for the business and risk for bankers. Hence it should provide technical support to prospects for identifying new opportunities and to capitalize those opportunities. The bank should reduce its operational costs. SBL should reduce high cost bearing deposits to get relief from burden of excess payment of interest and to ensure profitability. It is necessary to increase amount on non-fund based investment to maximize return through diversification of lending and decreasing excess dependency on loan.

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Appendices

Appendix-I (A): Comparative Balance Sheet

(Rs. In Million)

Capital and Liabilities					
Year	2006/07	2007/08	2008/09	2009/10	2010/11
Share Capital	320.00	384.00	766.77	806.40	2,016.00
Reserve Funds	27.77	47.06	102.80	74.79	92.61
Borrowings	324.52	505.02	506.00	444.80	658.00
Deposit Liabilities	1822.71	2880.87	4417.50	5760.50	6356.74
Bills Payable	-	-	-	-	-
P/L A/C	-	-	-	-	-
Proposed Dividend	-	-	2.02	80.64	141.12
Income Tax Liabilities	-	-	-	-	-
Other Liabilities	11.74	22.18	50.05	71.43	98.91
Total Liabilities	2506.73	3839.13	5845.14	7238.56	9363.38
Assets					
Year	2006/07	2007/08	2008/09	2009/10	2010/11
Cash Balance	25.41	50.93	79.91	79.14	147.10
Bank Balance with NRB	51.73	147.94	528.85	84.68	326.98
Balance with Bank/Financial Institutions					

	4.52	10.22	24.06	64.62	52.24
Monet at Call and Short Notices	431.43	387.07	370.82	1017.18	1049.94
Investment	466.27	508.14	530.73	495.61	916.65
Loans, Advances and Bills Purchases	1486.90	2497.78	3992.09	5092.10	6371.32
P/L A/C	-	-	-	-	-
Fixed Assets	16.10	204.49	229.11	325.50	361.07
Non-Banking Assets	-	-	-	-	-
Other Assets	24.37	32.56	89.58	79.73	138.09
Total Assets	2506.73	3839.13	5845.14	7238.56	9363.38

Appendix-I (B): Comparative Profit and Loss A/C

(In Million)

Description	2006/07	2007/08	2008/09	2009/10	2010/11
Interest Income	61	125	359	616	1,038
Interest Expenses	26	67	236	399	683
Net Interest Income	35	58	123	216	355
Commission and Discount	1	1	4	4	5
Other Operating Income	5	5	26	31	35
Exchange Fluctuation Income	0	0	8	6	0
Total Operating Income	40	64	161	257	395
Employees Expenses	8	11	24	43	56
Other Overhead Expenses	13	16	38	67	84
Exchange Fluctuation Loss	0	0	0	0	0
Operating Profit Before Provision for Possible Loss	9	37	99	147	255
Provision for Possible Losses	5	7	20	11	13
Operating Profit	13	29	79	135	242
Non-operating Income/Expenses	0	0	0	0	0
Provision Written-Back	0	0	11	2	2
Profit from Regular Operations	13	29	89	138	244
Profit/Loss from extra-ordinary activities	0	0	0	0	0
Net Profit after considering all activities	13	29	89	138	244
Provision for Staff Bonus	1	3	8	13	22

Provision for Income Tax	3	8	23	40	67
This Year's	3	8	24	37	67
Previous Year's	0	0	0	2	0
Deferred Tax Liability	0	0	1	0	-1
Net Profit after	9	19	58	86	155

Appendix-II: Financial Tools

a) NRB Balance to Total Deposit

FY	2006/07	2007/08	2008/09	2009/10	2010/11
NRB Balance	51.73	147.94	528.85	84.68	326.98
Total Deposit	1,822.71	2,880.87	4,417.50	5,760.50	6,356.74
Ratio	0.03	0.05	0.12	0.01	0.05
Mean	0.05				
S.D.	0.08				
C.V.	1.52				

b) Cash Balance to Total Deposit

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Cash Balance	25.41	50.93	79.91	79.14	147.1
Total Deposit	1,822.71	2,880.87	4,417.50	5,760.50	6,356.74
Ratio	0.01	0.02	0.02	0.01	0.02
Mean	0.02				
S.D.	0.008				
C.V.	0.44				

c) Liquid Fund to Total Deposit

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Liquid Fund	81.66	209.09	632.82	228.44	526.32
Total Deposit	1,822.71	2,880.87	4,417.50	5,760.50	6,356.74

Ratio	0.04	0.07	0.14	0.04	0.08
Mean	0.08				
S.D.	0.04				
C.V.	0.54				

d) Total Assets to Total Liabilities

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Total Assets	2,506.73	3,839.13	5,845.14	7,238.56	9,363.38
Total Liabilities	2158.97	3408.07	4975.57	6357.37	7254.77
Ratio	1.16	1.13	1.17	1.14	1.29
Mean	1.18				
S.D	0.07				
C.V.	0.06				

e) Loan and Advances to Total Assets Ratio

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Loan and Advances	1,486.90	2,497.78	3,992.09	5,092.10	6,371.32
Total Assets	2,506.73	3,839.13	5,845.14	7,238.56	9,363.38
Ratio	0.59	0.65	0.68	0.70	0.68
Mean	0.66				
S.D.	0.04				
C.V.	0.06				

f) Loan and Advances to Total Deposit Ratio

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Loan and Advances	1,486.90	2,497.78	3,992.09	5,092.10	6,371.32
Total Deposit	1,822.71	2,880.87	4,417.50	5,760.50	6,356.74
Ratio	0.82	0.87	0.90	0.88	1.00
Mean	0.89				
S.D.	0.07				
C.V.	0.08				

g) Interest Income to total income ratio

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Interest Income	60.83	124.80	358.55	615.64	1038.46
Total Income	66.22	130.65	396.85	655.93	1078.72
Ratio	0.92	0.96	0.90	0.94	0.96
Mean	0.94				

S.D.	0.02
C.V.	0.03

h) Interest Income to Interest Expenses

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Interest Income	60.83	124.80	358.55	615.64	1038.46
Interest Expenses	26.15	66.75	235.89	399.30	683.00
Ratio	2.33	1.87	1.52	1.54	1.52
Mean	1.76				
S.D.	0.35				
C.V.	0.20				

i) Return on Loan and advances

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Return	8.79	18.75	57.76	85.74	155.22
Loan and Advances	1486.90	2497.78	3992.09	5092.10	6371.32
Ratio	0.01	0.01	0.01	0.02	0.02
Mean	0.014				
S.D.	0.007				
C.V.	0.54				

j) Loan Loss Provision to Total Loan and Advances

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Loan Loss Provision	15.02	35.60	44.90	53.75	64.57
Loan and Advances	1486.90	2497.78	3992.09	5092.10	6371.32
Ratio	0.01	0.01	0.01	0.01	0.01
Mean	0.011				
S.D.	0.002				
C.V.	0.15				

k) Non-Performing Loan to Total Loan and Advances

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Non-Performing Loan	0.00	38.33	7.07	4.36	0.29
Loan and Advances	1486.90	2497.78	3992.09	5092.10	6371.32

Ratio	0.00	0.02	0.00	0.00	0.00
Mean	0.004				
S.D.	0.01				
C.V.	1.83				

I) Performing Loan to Total Loan and Advances

FY	2006/07	2007/08	2008/09	2009/10	2010/11
Performing Loan	1501.92	2495.05	4029.92	5141.49	6435.90
Loan and Advances	1501.92	2533.38	4036.99	5145.85	6436.18
Ratio	1.00	0.98	1.00	1.00	1.00
Mean	1.00				
S.D.	0.007				
C.V.	0.007				

Appendix-III: Calculation of Correlation Coefficient

Appendix-III (A): Correlation between total loans and loan loss provision

(Rs. In Million)

Periods	Total Loans	LLP	X ²	Y ²	XY
2006/07	1501.92	15.02	2255753.245	225.5753173	22557.53209
2007/08	2533.38	35.60	6417996.501	1267.453345	90191.52473
2008/09	4036.99	44.90	16297257.53	2015.595505	181242.0454
2009/10	5145.85	53.75	26479761.35	2889.056265	276589.0823
2010/11	6436.18	64.86	41424477.28	4206.950488	417457.4528
Total	19654.31	214.13	92875245.91	10604.63	988037.64
Correlation, r	0.98				

We know,

Coefficient of correlation (r)

$$r_{xy} = \frac{N\sum XY - \sum X \cdot \sum Y}{\sqrt{N\sum X^2 - (\sum X)^2} * \sqrt{N\sum Y^2 - (\sum Y)^2}}$$

$$= \frac{5 * 988037.64 - 19654.31 * 214.13}{\sqrt{5 * 92875245.91 - (19654.31)^2} * \sqrt{5 * 10604.63 - (214.13)^2}}$$

$$= 0.98$$

Where,

X=Total Loans of the Years

Y=Loan Loss Provisions of the Years

N=no of years

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

$$t = \frac{0.98}{\sqrt{1-(0.98)^2}} \sqrt{5-2}$$

$$t=8.52$$

B. Correlation between total loans and NPL(Rs. In Million)

Periods	Total Loans	NPL	X ²	Y ²	XY
2006/07	1501.92	0	2255753.245	0	0
2007/08	2533.38	38.33	6417996.501	1468.913703	97095.2265
2008/09	4036.99	7.07	16297257.53	49.96174136	28534.87981
2009/10	5145.85	4.36	26479761.35	18.9995123	22429.94765
2010/11	6436.18	0.29	41424477.28	0.082454548	1848.144085
Total	19654.31	50.04	92875245.91	1537.96	149908.20
Correlation, r	-0.37				

We know,

Coefficient of correlation (r)

$$r_{xy} = \frac{N\sum XY - \sum X \cdot \sum Y}{\sqrt{N\sum X^2 - (\sum X)^2} * \sqrt{N\sum Y^2 - (\sum Y)^2}}$$

$$= \frac{5 * 149908.20 - 19654.31 * 50.04}{\sqrt{5 * 92875245.91 - (19654.31)^2} * \sqrt{5 * 1537.96 - (50.04)^2}}$$

$$= -0.37$$

Where,

X=Total Loans of the Years

Y=Non-Performing Loans of the Years

N=no of years

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

$$t = \frac{-0.37}{\sqrt{1-(-0.37)^2}} \sqrt{5-2}$$

$$= -0.69$$

C. Correlation between total loans and performing loans(Rs. In Million)

Periods	Total Loans	Performing loans	X ²	Y ²	XY
2006/07	1501.92	1,501.92	2255753.245	2255753.245	2255753.245
2007/08	2533.38	2,495.05	6417996.501	6225274.962	6320901.274
2008/09	4036.99	4,029.92	16297257.53	16240237.73	16268722.65
2009/10	5145.85	5,141.49	26479761.35	26434920.46	26457331.41
2010/11	6436.18	6435.90	41424477.28	41420781.07	41422629.13
Total	19654.31	19604.27	92875245.91	92576967.47	92725337.71
Correlation, r	0.99				

We know,

Coefficient of correlation (r)

$$r_{xy} = \frac{N\sum XY - \sum X \cdot \sum Y}{\sqrt{N\sum X^2 - (\sum X)^2} * \sqrt{N\sum Y^2 - (\sum Y)^2}}$$

$$= \frac{5 * 92725337.71 - 19654.31 * 19604.27}{\sqrt{5 * 92875245.91 - (19654.31)^2} * \sqrt{5 * 92576967.47 - (19604.27)^2}}$$

$$= 0.99$$

Where,

X= Total Loans of the Years

Y=Performing Loans of the Years

N=no of years

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

$$t = \frac{0.99}{\sqrt{1-(0.99)^2}} \sqrt{5-2}$$

$$=12.15$$

E. Correlation between NPL and Net Profit (Rs. In Million)

Periods	NPL	Net Profit	X ²	Y ²	XY
2006/07	0	8.785745	0	77.18931521	0
2007/08	38.33	18.74843	1468.913703	351.5036275	718.560015
2008/09	7.07	57.759774	49.96174136	3336.191493	408.2669917
2009/10	4.36	85.737992	18.9995123	7351.003272	373.7184463
2010/11	0.29	155.220355	0.082454548	24093.35861	44.57136972
Total	50.04	326.25	1537.96	35209.25	1545.12
Correlation, r	-0.45				

We know,

Coefficient of correlation (r)

$$r_{xy} = \frac{N\sum XY - \sum X \cdot \sum Y}{\sqrt{N\sum X^2 - (\sum X)^2} * \sqrt{N\sum Y^2 - (\sum Y)^2}}$$

$$= \frac{5 * 1545.12 - 50.04 * 326.25}{\sqrt{5 * 1537.96 - (50.04)^2} * \sqrt{5 * 35209.25 - (326.25)^2}}$$

$$= -0.45$$

Where,

X=Non-Performing Loan of the years

Y=Net Profit of the Years

N=no of years

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

$$t = \frac{-0.45}{\sqrt{1-(-0.45)^2}} \sqrt{5-2}$$

$$=-0.87$$

Appendix-IV: Trend Analysis

Appendix-IV (A): Trend of Total Deposit Collection of SBL (Rs. In Million)

Fiscal Year	Year (x)	Deposit Collection(y)	XY	X ²
2007	1	1822.77	1822.77	1
2008	2	2880.87	5761.74	4
2009	3	4417.50	13252.51	9
2010	4	5760.50	23041.98	16
2011	5	6356.74	31783.69	25
Total	15	21238.37	75662.69	55

Here, actual trend equation of the linear trend is :

$$Y=a+bx$$

Two normal equations are :

$$\sum XY=a\sum X+b\sum X^2$$

Putting the values in the normal equations from the above table

$$21238.37=5a+b15 \dots\dots\dots i$$

$$75662.69=15a+b55 \dots\dots\dots ii$$

Multiplying equation(i) by 3 and subtracting equation (ii) from equation (iii)

$$63715.11=15a+b45 \dots\dots\dots iii$$

$$75662.69 = 15a + b55 \dots\dots\dots \text{ii}$$

$$b = 1194.76$$

Substituting the value of "b" in the equation (i)

$$a = 663.394$$

In 2011/12, Thus the required trend of $Y = a + bX = 663.394 + 1194.76 \times 6 = 7831.954$

In 2012/13, $= 663.394 + 1194.76 \times 6 = 9026.71$

In 2013/14, $= 663.394 + 1194.76 \times 6 = 10221.47$

In 2014/15, $= 663.394 + 1194.76 \times 6 = 11416.23$

In 2015/16, $= 663.394 + 1194.76 \times 6 = 12610.99$

B. Trend of Loan and Advances SBL(Rs. In Million)

Year	Year (X)	Loan and Advances (Y)	XY	X ²
2006/07	1	1486.90	1486.90	1
2007/08	2	2497.78	4995.55	4
2008/09	3	3992.09	11976.27	9
2009/10	4	5092.10	20368.40	16
2010/11	5	6371.32	31856.62	25
Total	15	19440.186	70683.74	55

Here, actual trend equation of the linear trend is :

$$Y = a + bx$$

Two normal equations are :

$$\sum Y = na + b \sum x \text{ and}$$

$$\sum XY = a \sum X + b \sum X^2$$

Putting the values in the normal equations from the above table

$$19440.19 = 5a + 15b \dots\dots\dots \text{(i)}$$

$$70683.74 = 15a + 55b \dots\dots\dots \text{(ii)}$$

Multiplying equation(i) by 3 and subtracting equation (ii) from equation (iii)

$$58320.57 = 15a + 45b \dots\dots\dots \text{(iii)}$$

$$70683.74 = 15a + 55b \dots\dots\dots (ii)$$

$$b = 1236.32$$

Substituting the value of "b" in the equation (i)

$$a = 2686.17$$

In 2011/12, Thus the required trend of

$$Y = a + bX = 2686.17 + 1236.32 \times 6 = 10,104.10$$

$$\text{In } 2012/13 = 11340.40$$

$$\text{In } 2013/14 = 12576.70$$

$$\text{In } 2014/15 = 13813.10$$

$$\text{In } 2015/16 = 15049.4$$

C. Trend of Net Profit SBL (Rs. In Million)

Periods	Year (X)	Profit/Loss(Y)	XY	X ²
2006/07	1	8.79	8.79	1
2007/08	2	18.75	37.50	4
2008/09	3	57.76	173.28	9
2009/10	4	85.74	342.95	16
2010/11	5	155.22	776.10	25
Total	15	326.25	4893.78	225

Here, actual trend equation of the linear trend is :

$$Y = a + bx$$

Two normal equations are :

$$\sum Y = na + b \sum x \text{ and}$$

$$\sum XY = a \sum X + b \sum X^2$$

Putting the values in the normal equations from the above table

$$326.25 = 5a + b15 \dots\dots\dots i$$

$$4893.78 = 15a + b225 \dots\dots\dots ii$$

Multiplying equation(i) by 3 and subtracting equation (ii) from equation (iii)

$$978.75 = 15a + b45 \dots\dots\dots iii$$

$$4893.78 = 15a + b225 \dots\dots\dots ii$$

$$b = 21.75$$

Substituting the value of "b" in the equation (i)

$$a = 0$$

In 2011/12, Thus the required trend of

$$Y = a + bX = 0 + 21.75 * 6 = 130.50$$

$$\text{In } 2012/13 = 152.25$$

$$\text{In } 2013/14 = 174$$

$$\text{In } 2014/15 = 195.75$$

$$\text{In } 2015/16 = 217.50$$

**Appendix-V: Questionnaires to Sanima Bank Limited for the purpose of the study on
“Credit Management of Sanima Bank Limited: A Case Study”.**

Please tick (✓) or rate as 1, 2, 3, 4 where ever necessary in the blank.

Q.N.1. Which is the key risk in your bank?

i) Credit risk

ii) Liquidity risk

iii) Interest risk

iv) Exchange risk

Q.N.2. which factor play important role at disbursing loan?

i) Collateral

ii) Profitability of business

iii) Projected financial statement

iv) Image of the business

v) Image of the business person

Q.N.3. Is default loan is should reschedule?

i) Yes

ii) No

Q.N.4.Which method should practice in remedies for recovering loan?

i) Collateral

ii)Guarantor

iii)Counseling

iv)Technical support

v) Follow up

Q.N.5.Which percentage should give loan to total business requirement?

i) Above 50%

ii) Above 60%

iii) Above 70%

Q.N.6 Does your organization has any problem related NRB?

i) Yes

ii) No

If Yes Please write in Points:

-
-
-

Q.N.7.Did you feel about the need of Asset Management Company?

i) Yes

ii) No

Q.N.8 Have you feel any support Judiciary Office support?

i) Yes

ii) No

Q.N.9. Who should take involve in verifications of properties being kept as collateral before granting loan?

i) Related Specialist

ii) Office Staff

iii) Independent person

Q.N.10. Which is the source of credit risk in your bank?

i) Increase in interest arrears

ii) Not paying attitude of borrower

iii) No profitability of loan taker

Q.N.11. Does the bank should receive regular information about costumer?

i) Yes

ii) No