

CHAPTER-ONE

INTRODUCTION

1.1 BACKGROUND OF THE STUDY:

Nepal is an underdeveloped, landlocked country lying between China and India. The greatest challenge to our economic development effort is mass poverty, which is in all corners of the country. Poverty in Nepal is deeply rooted, largely chronic and reflected in all dimensions of social, economic, political and humanistic aspects of development. There are 25.16% people who are bounded to live in below poverty line. The state has to raise the living standard of the people by implementing various poverty alleviation programs targeted to the poorest of the poor. Different micro finance credit programs devoted to the alleviation of the poverty in rural Nepal. There are many NGOs and saving and credit co-operatives that are involved in micro finance programs. The share of financial intermediaries NGOs and saving & credit co-operatives in the total outstanding rural institution credit is still negligible.

Nepal is predominately an agriculture country where about 80% to 90% of total economically active population is engaged in agriculture and its contribution to national income is around 53% but, employment in agricultural sector is only for employment sake. Since there are few employment opportunities in the rural areas, the populations are forced to work in agricultural sector. More than half of the man-days of the rural people are inutilities in a year. In this situation, under employment rather unemployment is not only axiomatic but a proved fact in our country. On the one hand there is increasing population pressure on the other hand production in agricultural sector has not been increasing in the ratio of the population increased. So it has become practically impossible to offer employment gainfully to under employed people in the agricultural sector. So it is essential to fasten the chances of employment by the development in the industries in the country.

Rapid economic development is important for all countries of the world. It is more urgent for the least developed countries like ours. In this context it is but

natural the existing agricultural predominance in our country has to be reduced by transformation into an industrialization process. Nepal like other developing countries has been facing the problem of acceleration in the pace of economic development.

A bank is the financial institution whose principles operations are concern with the accumulation of the idle money of the public for the purpose of advancing to other for expenditure. A bank is a person or corporation, which hold itself out to receive from the public deposits payable on demand by cheque. In other word a bank is a financial institution whose business is to trade in money. Bank is an institution which engaged in monetary transaction. It deposit money from those having saving and lends to those who need money for some purpose on charging at some interest rate.

“A bank is one who in the ordinary course of his business, receives money which he pays by honoring cheque whom or whose account receives.”

Bank plays an important role to the economy development of National economy. Bank is that co-operation or institution which performs the indispensable work of intermediating among two more institution and individual to increase fund and then to give loan of those funds or accumulated amount. In another word, bank is a dealer in capital and he is intermediate party between the borrower and the lender.

According to kindly “ Bank is an establishment which makes to individuals such advances of money or other means of payments as may be required and safely made and to which individuals entrust or means of payment when not required by them for use.”²

“A Bank or a banker is a person, firm or company, having a place of business where credits are opened by the deposit or collection of money or currency subject to be paid or loaned on stocks bonds and bills of exchange and promissory notes are received for account and sale”³

Bank is a very important institution because it acts several roles such as intermediation role, payment role, guarantor role, agency role etc. Same way, bank

motive to the people to mobilize saving, economic development bank promote the private investment and capital formulation for safety of wealth, transfer money from one place to another place, bank is needed.

In summarized, Banks are those financial institutions who offer the widest range of financial services especially saving, credit and payment service. And receiving deposits of various kinds, lending money, issuing cheques and collecting cheques etc are the essential function of a bank.

In the context of Nepal, there is no longer history of bank and financial institution. In 780 B.C. the king of Kathmandu Guanakamdev who had borrowed loan to build the city of Kathmandu but later on in 937 BS Shankhadhar who was the famous merchant, paid borrowing loan of people and started “Nepal Shambat”. But later on in 14th century the famous Malla King Jayasthity Malla divided people in 64 castes on the basis of their profession then among different castes there was a people who use to perform borrowing and lending function at that time he was known as “Tankadhari”. But during the Rana period, prime minister Ranodeep Singh established, “ Tejarath Adda” at Kathmandu. At that time, the main function of Tejarath Adda was to provide loan for government officer and staffs and also for general public under the collateral of silver, gold at 5% per annum interest rate. But later on due to increasing of the banking transaction modern bank or institutions was going to established.

On the course of growth of Bank, Nepal Bank Limited is 1st modern bank. NBL was established on BS 1994 Kartik 30 under the Nepal Act with one corer authorized capital. NBL has been providing banking facilities and services from established date up to now. Later on In 2012 BS for developing and controlling of banking management and monetary system, central bank was felt necessary according to Nepal bank act 2012, NRB was established under the Act with one corer capital.

Later on 2022 BS under the ownership of government, Rastriya Banijya Bank was established with authorized capital of one corer. The Agriculture Development Bank was established on 24 Magh 2024 B.S. for purpose of developing

agricultural sector and banking activities. Then after some year the government felt the necessity of economic liberalization policy for the development of commercial bank. Then government issued economic liberalization policy. As the result it becomes successful to attract or motivate foreign investor. So , Nepal Arab Bank Limited was established as first joint venture Bank in Nepal. Then more and more joint venture has been increased rapidly in Nepal. As a result at present 32 commercial banks, 88 Development Banks, 70 finance companies, 24 Micro-Credit development banks and 22 NGOs (Micro loan provider) are operating banking activities. Foreign commercial banks are playing dominant role to manage the joint venture bank in Nepal. All joint venture banks are established and operating under the rules and regulation of NRB.

Reducing poverty is the fundamental objective of economic development. It is estimated that more than one billion people in the developing world are poor and nearly half of those are in extreme poverty line in South Asia. Nepal's level of per capita income in U.S. \$650 is one of the lowest in the world. More than half of the population survives on less than one dollar than that of the Asia and South Asia countries. More than 80% to 90% population lives in rural area in Nepal. People's economic condition is very poor. To improve their economic condition, many NGOs, INGOS, Banks co-operatives and other related political parties are given importance.

Many Banks like commercial bank, development bank and other financial institutions and enterprises play significant role for improving the economic condition. One of them is rural development bank that is playing vital role to alleviate poverty since it is establishment. With the realization of these facts, urgent need of a program, which is targeted effectively towards poorest of the poor is felt. Highly impressed with performance of Grameen Bank of Bangladesh and it's operational management and organizational system, some sort of government sponsored formal banking institution to introduce. Grameen Bikash Financial System (GBFS) concept in Nepal was tried but failed to achieve the above-mentioned objectives during 1980. micro finance institutions have sprung up all

over the developing world, from Bangladesh , India , Nepal to Bolivia to Serbia; by one estimate, over 150 million people worldwide have taken out a micro loan. Government aid groups and NGOs have rushed to fund them, and so have community banking and hedge funds, enticed by the promise of an anti poverty program that can do so much while paying for itself and even turning a nice profit. Micro finance Development Banks, Grameen Banks, Micro finance NGOs and all MFIs prove as micro finance is a sustainable tool for poverty throughout from the country. In 1991, with encouragement from professor Muhammad Yunus, founder of Grameen Bank Bangladesh and in co-operation with some friends, the Nepalese Banking on NGO namely, NIRDHAN was registered to replicate the GBFS. This was the first effort to replicate the GBFS in Nepal.

FORWARD also inspired from the success of micro-finance program and initiate it to alleviate the poverty from Nepal. The recent evidence suggest that nearly 15% of micro-finance clients in Nepal are among the poor of the poorest which we can see in the forward report.

BACKGROUND OF FORWARD

Forum for Rural women Agency development (FORWARD) is a non governmental Microfinance Organization, which is located in the eastern part of Nepal. The organization is headed by like-minded committed professional groups. FORWARD works for backward poor vulnerable, indigenous, tribal people and their communities to awareness-campaign, advocacy for their rights to empower women. The organization develops trust from supporters with the cooperation ideas and collective views to significant role in the poverty alleviation and community development through women and children. FORWARD has been improving its traditional culture and bad-habits through microfinance to uplift the poor communities.

FORWARD was established on B.S. 18 Baisakh, 2052(1st May, 1995). And it has been started micro credit since 2053 BS (March 1996) to serve the poor marginalize women groups and their vulnerable and poor communities. It was

licensed by NRB (Nepal Rastra Bank) central bank of Nepal as a *micro-finance intermediary* FMI at 15 paush, 2059 BS (30 December, 2002). The organization had been transform as a microfinance institution it renewed a banking license under the financial intermediary Act 1999 from central bank to run as a formal service provider of microfinance. This organization has been working together since 2002 with rural Microfinance Development Centre (RMDC) and other working partners are Himalayan Bank, NIC Bank, NMB Bank, KIST Bank, Sri Invest Finance Com. FORWARD Cooperative, Asian Development Bank (ADB), CADP, other local Development agencies and related District Development committees, District Administration Offices, District Education Office, Regional and District Health and Agriculture Development units and Various founding NGOs, INGOs.

The central office of FORWARD is located at Duhabi Urbanizing VDC, sunsari District, Koshi Zone, Nepal, it's contact liaison point at Babarmahal Kathmandu, similarly Area Office is at Inaruwa sunsari and Damak Morang

Vision of FORWARD

Develop the self-sustainable creative society for the poor vulnerable Communities.

Mission :

-) To raises the voices against exploitation and custom of strengthen of Human rights.
-) To makes the community self-dependent on the socio-economic with optimum utilization of local sources.
-) Increase the membership in rural poor areas to spread out the organization and improves the local traditional habits.
-) To run the income-generation and Microfinance activities and develops for marginalize and is poor communities.
-) To makes effective information media, which existing in the local level and access the linkages in the markets.
-) Mass mobilization and Enhancement as poverty reduction through microfinance.

Goal:

-) Expands the organization through increasing more group members, clients in the rural, remote and semi urban areas.
-) Improves the social-financial condition of the Nepalese woman and poor people.
-) Accesses to the community on their resources, and their Human rights and good governance.
-) Creates awareness raising micro-credit program and other community base(Education, Health, Hygiene, Nutrition, Advocacy and institutional development).
-) Awareness Campaigns against the domestic violence of child, girls and women even campaign against the trafficking.

Objectives:

-) To develops the micro finance groups as autonomous, self sustain and institutional capacity development of its leader, staffs, and clients.
-) To makes as much as financial resources accessible for poor woman groups.
-) To makes awareness for rural people for good health and social practices.
-) To capacitates local groups in cooperation of different issues with different agencies.
-) To improves the social and economic condition of women through credit mobilization.
-) To aware the women right and humanitarian development for poor vulnerable people.
-) To provides group and individual skill for income generation and enterprises activities.
-) To conducts social community base trainings (various interlink with agriculture and microfinance).

-) Ensure the coordination and linkages with government of national and international agencies and related financial institutions.

Major Activities of FORWARD:

-) Baseline survey and impact study at the organizational programs.
-) Selection of Areas (VDCs, DDCs) and clusters. PGT, CGT, GRT.
-) To conduct DDCs/VDCs orientation program.
-) To collect the local level small savings.
-) To develops the group autonomous and independent.
-) To develops the group leaders of women
-) Coordinates with various institutions for social development and human resources.
-) Provides banking service for the poor people who are involved on saving and credit mobilization.
-) To improves the socio-economic status of poor women and children through Microfinance and other social programs.
-) Enhance awareness raising trainings to the poor vulnerable communities.
-) Yearly reviews the program and projects, Business planning / Half yearly / quarterly review meetings.
-) Develop the MIS system in both computer software and manually.

Key Strategies:

-) FORWARD has adopted the participatory strategies in order to implement the above policies as per the operational nature of various programs. It's formulating the action oriented strategies for the smooth operation of the socio-economic programs.

-) Active participation of the community women, it makes automatic empowerment to upgrade in Socio-economic condition of the poor families.
-) To generate the innovative concepts, collective vision for participatory development work effort to the team.
-) Optimum utilization of local resources in Socio-economic business oriented on sustainable community development.
-) Coordination and cooperation of target group / units on the community environment to upgrade sustainable human rights, peace and commitments on governance.

Departments of FORWARD:

This organization has been operating three departments to serve their programs to women groups. They are as follows,

1. Micro Finance Department,
2. Social Department,
3. Institutional Department,

Micro Finance Department:

Introduction:

The main goal of this department is to provide loans without collateral for the poor vulnerable community to improve socio-economic status and upgrade their saving habits. Conducts small socio-enterprises trainings for loaner groups members to improve agriculture development, microfinance industrial trainings and their group monitoring program. It improves economic condition to strengthen and unity of the rural women in their communities.

FORWARD was licensed by Nepal Rastra Bank (central bank of Nepal) since on B.S.2059 paush 15, as a financial intermediary act to operate Microfinance Banking Workes. Although FORWARD had been working Micro-credit since on

B.S.2053(1997). The organization has been operating its program in Socio-economic development since last 16 years.

Microfinance Policy of FORWARD:

FORWARD follows the 'Grameen' methodology for microfinance service delivery and lending modality through group guarantees. All groups have been consisted five members, however it consists three to eight groups is called one center, when it has an eight group is called full center. Which groups operational lending with terai 2 is to; 1(2:2:1), but in hill 3 is to; 2(3:2) with jointly liabilities on repayment installment. The organization's microfinance policy is held the meeting fortnightly for terai and monthly for hilly region, however the system of center meetings are slightly as well as Gramin model.

Clients receive 7-9 days Pre Group Training (PGT) and clearing Group Recognition Test (GRT), after all prior process of the group members are becoming eligible to obtain the first cycle of loan. For succeed and matured clients eligible for various types of loan which provides Micro enterprises, livestock's, housing, Biogas, Foreign employee, Drinking water and toilet construction as on members pass track record with performance base. Loans are disbursing from branch offices with the hand of their Center chief. And graduate loaners whose are mobilized first and second loan with good performance on good repayment track records, can easily take 1st, 2nd, 3rd, 4th and 5th cycle of loans. Micro enterprises and foreign Employee loaners are personally responsible with their family liabilities for that loan mobilization although it is in group guarantee of center model.

1.2 Focus of the study:

Nepal, being an agrarian country, over 85% of the total population lives here in the rural areas and depends on agriculture that accounts for 54% of household income. A study carried out by NRB in 1994 reveled that only 20% rural households have access to formal credit and the remaining have to on informal credit. According to the study, the formal financial structure could not meet the needs of the rural borrowers due to their formal and bureaucratic structure of financing. Consequently, the formal structure could not extend into the depth and

breadths of the rural community. Realizing the limitations, shortcomings and weakness, the government encouraged financial institution to contribute to the saving mobilization and credit extension.

Nepal is predominantly an agricultural country, which has an area of 147181 square kilometers and runs all along 885 kilometers from east to west and 145 to 241 k. M. from north to south. It is land locked country, which is sandwiched between India in south, east and west and Tibet region of China in the north. Agriculture is the chief occupation of the Nepalese people living in rural areas and plays vital role to uplift the poor conditions of rural people.

Our country is the country of rural poverty. FORWARD (Forum For Rural Women Ardency Development) is playing vital role for rural women empowerment and poverty alleviation. FORWARD is operating its micro-finance program and saving & credit program in 17 districts i.e. *Taplejung, Sankhuwasabha, Tehrathum, Pachathar, Ilam, Dhankuta, Jhapa, Morang, Sunsari, Saptari, Siraha, Udayapur, Sindhuli, Sarlahi, Mahottari, Rautahat, Dhanusa*. FORWARD cover 280 V.D.C and 11 municipality of Nepal. FORWARD has established 44 branch offices to run the program smoothly and to serve more and more facilities to rural poor person at rural area. Some one tells its financial position, after the study is the profitable. The profitability study of the organization will be added to save organization for the long life to help on poverty alleviation programs. Financial performance shows its efficiency, capital structure, profitability, liquidity and future progressive trend which are helpful for the bank management client and ministry of finance of Nepal to provide supportive decision.

Table 1

S.N.	Particulars	064/65	065/66	066/67	067/68	068/69
1.	No. of District covered	8	8	10	17	19
2.	No. of V.D.C. covered	177	186	193	280	300
3.	No. of municipality covered	8	9	10	11	17
4.	No. of Branch office	28	28	28	44	51
5.	No. of employees	159	174	183	211	264
6.	No. of centers	1756	2124	2349	2982	3557
7.	No. of Groups	8347	9737	10755	13019	16030
8.	No. of members	41736	48667	53645	68962	80148
9.	No. of borrowers	32008	35645	38238	47858	53375

Source: Annual Report of FORWARD

1.3 Statement of Problem:

The following problems make the Micro-Finance Institutions endanger. Micro-Finance Institutions can not bloom until the problems are solved.

1. Lack of partnership in local development project.
2. Lack of vivid rules and regulation.
3. Lack of long term policy in Micro-credit field.
4. Lack of change in government policy on time.
5. There is no flexible policy in government about Micro-Finance Institutions development.
6. Shortage of the men poor, organization structure, the lowest sources of income of the community people.
7. Lack of true vision in government policy about Micro-credit.
8. There is no long term policy and co-ordination between Micro-Finance Institution and government.
9. Lack of investment's environment to attract the foreign investors in Micro-Credit field.
10. Lack of the education in community about Micro-Credit program.

Besides these problems there are lots of risk and challenge seems to operate the Micro-Credit program smoothly in rural area, i. e. Credit risk, Liquidity risk, Interest rate risk, Security risk, Fraud risk, Competition risk, Regulatory risk, Physical environment risk, Macroeconomic risk etc.

1.4 Objectives of the study:

Objectives are determined according to the nature of study. The objective of the financial performance of FORWARD (Forum For Rural Women Ardency Development) is mainly to identify the existing financial position. The detail objectives of the study are the following:

- (i) To identity the existing financial position of FORWARD.
- (ii) To evaluate the sources and application of funds.
- (iii) To test the financial situation with the help of trend analysis.
- (iv) To compare the present situation with the help of trend analysis.

- (v) To find out the relationship among the variable.
- (vi) To provide reformative suggestion for future improvement.

1.5 Needs of the study:

In the rural sector commercial banks are scanty or less attention. Private moneylenders charge very high rate of interest. More over them are demanding security for loan. In the perspective looking into the great success of rural bank in Bangladesh so FORWARD (Forum For Rural Women Ardency Development) decided to establish micro finance program and saving & credit program. FORWARD (Forum For Rural Women Ardency Development) is operating its program in 17 Districts, 11 Municipality and 280 V.D.C in Nepal. So it is naturally a matter of interest to keep in to its financial performance especially due to striking fact that it never ask for any security for the disbursement of loan. The researcher wants to find out what the financial performance is in the FORWARD (Forum For Rural Women Ardency Development). It helps to show the financial strength and weakness affects to their effectiveness to earn profit and goodwill. Unless the FORWARD explore the exiting financial weakness evaluating and observing the source and application of the fund, it can't be mobilize the fund effectively. The above relevant facts come to know after study it.

1.6 Limitation of the study:

Every study is bound by the limitation due to different factors. It means that different study has different but certain limitation. The following limitations are pointed out to study the financial performance of FORWARD.

- a) This study is based on five year's data i.e. FY 2063-64 to 2067-68 B.S. So, generalization based on only five years may not be true which is assuming to be true and correct.
- b) This data based on secondary data.
- c) The figures of different accounts are considered as the year end only.
- d) Its financial performance is based only on the funds flow analysis, ratio analysis, trend analysis and correlation analysis.

- e) This study has not considered the NPV (Net present value) of money during 7 years. So, a detailed analysis beyond true and correct.
- f) This study is to suggest rather than direct.
- g) Share has not issued, so the ratios related to share capital is not possible to compute in this study.

1.7 Research methodology:

A systematic research study needs to follow a proper methodology to achieve the pre-mentioned objectives. Research methodology is a sequential procedure and methods in order to conduct the research. The entire research methodology followed in this chapter has focused on research design, nature and sources of data, procedure employed and financial and statistical tools.

1.7.1 Research Design:

It is devising the plane for the research. It describes the general framework for collecting, analysis and evaluating data after identify: (i) what researcher wants to know and (ii) what has to be dealt with in order to obtain required information.

The basic aim of this study is to evaluate the situation and to provide constructive suggestions for better mobilization and utilization of sources and resources and other aspect of financial management of FORWARD. Evaluation has been done on the basis of profit and loss A/C and balance sheet by using financial tools and statistical tools. Hence, discriptive and analytical research design has been followed.

1.7.2 Nature and sources of data:

This study is based upon the secondary data published in the form of annual report about profit & loss a/c and balance sheet and concerned notes of FORWARD for five year from FY 2064/65 to 2068/69 BS. The chairman's reports for different AGM have also furnished some important data.

1.7.3 Population and sample of the study:

The population of the study is the totality of all observations that have been selected for the study. Thus, in the case of FORWARD if the researcher studies the past whole life of FORWARD is called population study. It is quite difficult to

analysis all the data of population. So the sample has been selected for the study, which starts from FY 2064/65 to 2068/69 BS.

1.7.4 Data collection procedure:

The study is mainly based on the secondary data. The data related to financial performance of FORWARD is directly obtained from the head office. The supplementary data and information are obtained from the journals NRB's yearly book and other sources.

1.7.5 Data processing procedure:

The data collected from the above sources of the bank are classified, tabulated and analyzed. Financial ratios are basically used for interpretation.

1.7.6 Research Questions:

The researcher tries to give answer of the following questions to measure the financial situation of FORWARD. These questions are as follows:

- (i) How is the funds collected and applied by the FORWARD?
- (ii) How is the financial position shown by the relevant ratios?
- (iii) What is the trend of financial performance of FORWARD with parameters like trend of percentage analysis and trend least square method analysis?
- (iv) What is the relationship among the deposit and investment, loan disbursement and collection, borrowing and loan outstanding?

1.7.7 Use of Analytical Tolls:

The performance measurement of business is more difficult and complex. With regard to the financial performance of firm depend on effectiveness in capital management, efficiency and profitability in operation, risk and uncertainty in competition etc. The collected data are analyzed by using various financial tools, out of these are given and defined below:

(1) Financial tolls:

- (i) Funds flow analysis
- (ii) Ratio analysis

(2) Statistical tolls:

- (i) Trend percentage analysis
- (ii) Trend least square method analysis
- (iii) Simple correlation analysis (coefficient of determinants)

1.8. Organization of the study:

A study on the financial performance of FORWARD has been divided into five chapters, viz. Introduction, and review of literature, research methodology, presentation analysis & interpretation of data, summary, conclusion and recommendation.

Chapter 1: Introduction: This is introductory chapter which is related to the introduction of the study. It deals with the background of the study, statement of the problem, important of the study, objective of the study and assumption and limitation of the study.

Chapter 2: Review of Literature: The second chapter deals with review of literature relating to the financial performance. In this chapter presentation of the related studies and findings as well as concept of the financial performance discussed briefly.

Chapter 3: Research Methodology: In the third chapter the research methodology used for the study has been described. It included as introduction, research design, nature of data processing procedure and tools for analysis.

Chapter 4: Presentation analysis and interpretation: Presentation analysis and interpretation of data in the fourth chapter the acquired data are presented analyzed and interpreted by using differs financial tools and present the result relating to the study.

Chapter 5: Summary conclusion and recommendation: This fifth and last chapter deals with the summary and conclusion of the study and some suggestion for the improvement of the financial performance in a company are also presented in this chapter.

CHAPTER-TWO

REVIEW OF LITERATURE

2.1 Introduction

In this study, the review of literature covers the review of analysis of financial performance of Forum For Rural Women Ardency Development (FORWARD) Micro-Finance Institute. Literature review is basically a “stock taking” of available literature in once field of research. The purpose of literature is to find out what research studies have been conducted in once chooses field of study, and what remains to be done. It provides the foundation of developing a comprehensive theoretical framework for which hypothesis can be developed for testing. The literature survey also minimize of risk of pursuing the dead-ends in research. “The main purpose of reviewing the literature is to develop some expertise one’s area to see what new contribution can be made and to receive some ideas for developing a research design.” (*Wolf, Panta; 1999:30*)

Some light/vision has been mention with the purpose of reviewing the literature in this chapter. It contains the financial performance, financial statements, financial statement analysis and review of the related studies. In addition to these, some logics, issues finding and suggestions are mentioned which are found to be guideline to prepare the current study. In course of reviewing the literature various books, journals, articles, seminar paper, relative acts, rules regulations and policies on the subject matter have been used.

2.2 Conceptual and theoretical review

2.2.1 Financial performance

Financial performance is that managerial activity which has concern with the planning, raising, controlling and administrating of financial resource of an enterprise. Again it is basically concern with analysis of financial statement of an enterprise by using different tools and techniques. Financial performance is not

only the evaluation of financial condition but also the evaluation of planning and it helps to improve the planning in future. The real picture of financial performance mainly depends upon the past, present, and anticipated profit and current financial position of an enterprise. Thus the financial performance prefers to treatment of the information confined in the financial statement to afford a full diagnosis of profitability and financial position of the concern enterprise.

The performance of a firm can be accessed by computing key ratios and analyzing:

1. How is the firm performing relative to the industry?
2. How is the firm performing relative to the leading firm in their Industry?
3. How does the current year performance compare to the previous years?
4. What are the variables driving the key ratios?
5. What are the linkages among the ratios?
6. What do the ratios reveal about the future prospect of the firm for various stakeholders such as shareholders, employees, customers etc.?

The profit earning capacity and the current financial position of an enterprise is the main financial performance indicator of the organization. Profit and strong financial position of enterprise is the result successful management, cost control, sound information system, better labour relation and their efficiency and regular performance appraisal. The performance of enterprise is affected by the existing government economic rules and regulation, policy (monetary & fiscal), investment tax, labour law, rate of inflation etc.

“Profit is essential for an enterprise to service and grow as well as the maintain adequacy through retained earning. It is essential to access market for both debt and equity to provide funds for increased assistance to the productive sector.” (*Ronald; 1951: 21 & 22*)

“Management should be particularly interested in knowing the financial strength of the firm to make their best use and to be able to spot out the financial weakness of the firm to take suitable corrective action. The future plans of the firm should be laid down in view of firms financial strength and weakness.” (*Pandey; 1983:1*)

In fact the better financial performance means to generate the reasonable profit by giving high quality of goods and service offered of the consumer\concern parties. An effective financial performance is that; which has management effectiveness by the return, generated investment, the firm’s ability to maintain its economy to use the proper advantage and to take the corrective action of the financial strength and weakness. The strength must be understood if they are to be used to proper advantage and the weakness must be recognized if corrective action is to be taken.

2.2.2 Financial management

Financial management is the management of the flow of money and any credit instrument in an organization whether it is corporation, school, enterprises, bank or government agency. The successful financial management of an organization is beneficial to customers, employees, investors and general public.

“The term ‘financial management’ connotes that the funds flow are directed according to some plan; it is with managing the flow of fund within the firm.” (*Van, Horne; 1984: 2*)

“Financial management is that managerial activity which is concern with the planning controlling of the firm’s financial resources.” (*Pandey; 1991:1*)

The financial management is a business activity which is concerned with the acquisition of utilization of capital funds in meeting the financial needs and overall objectives of the business organization. It stresses the analytical approach for solving the financial problems. It is considered as an integral part of overall

management and decision of each and every functional area as contribution to achieve the financial objective of the business organization.

The function and scope of financial management covers the three major decision making areas, which are:

(1) The investment decision

(2) The financing decision and

(3) The dividend decision

These above financial decision are not sequential; they are performed by the firm simultaneously and continuously. Thus the process of raising fund, investing them in the required assets is the key point of the financial management.

2.2.3 Financial statement

Financial statement at least refers to the two statements, which are prepared by a business concern at the end of the year. They are (i) income statement, which is prepared by a business concern in order to know the profit earned and loss sustained during a specified period (ii) Balance-sheet, which is prepared at a particular date in order to know the financial position of the firm. Financial statements are annual documents prepared by the organization. They are prepared for the periodical review on the progress made and results achieved during the period review. Financial statements generally provide the following information:

- Whether earning is adequate or not to attract the potential investor to invest.
- Whether the sales/service is profitable or not.
- Liquidity position of the organization.

Financial statement reflects a combination of recorded facts; accounting conventions and personal judgments and conventions applied affect them materially. In this sense, financial statements are affected by recorded fact, accounting conventions and personal judgments. In fact, financial statements are

historical documents and relate to the past period and are expressed in monetary terms to indicate the financial position in terms of assets and liabilities through balance sheet. “Financial statements are prepared for the purpose of presenting and periodical review or report on progress by management and deal with the status of the investment in the business and the results achieved during the period under review. The soundness of the judgments necessarily depends upon the competence and integrity of those who make them and on their adherence to generally accepted accounting principles and conventions.” (American institute of accounts)

“The financial statements provide a summary of the accounts of a business enterprise, the balance sheet reflecting the assets, liabilities and capital as of a certain date and the income statement showing the results of operations during a certain period.” (Myer; 1974: 95)

“Financial statement reports what has actually happened to earning and dividends over the past few years. It may show a position at a moment in time as in the case of an income statement.” (Hampton; 1974: 95)

“Financial statements represent the summation of a variety of conventions governing the recording of financial transaction. Unless specially prepared, they do not customarily reflect current economic values.” (Kennedy; 1973: 95)

“Financial statement attempt to do several things. First they portray the assets and liabilities of a business firm at a moment in time, usually at the end of a year. This portrayal is known as the balance sheet. On the other hand, an income statement portrays the revenues, expenses, taxes & profit of the firm of a particular period of time, again usually a year. While the balance sheet represents a snapshot of the firm’s financial position at a moment in time, the income statement depicts its profitability over time.” (Van, Horne; 1984: 2)

“Financial statement contains summarized information of the firm’s financial affairs organized systematically.” (Megis; 1978: 1049)

As above discussion, the nature of financial statement can be stated below.

- a) These are reports or summarized reviews about the performance, achievements and weakness of the enterprise.
- b) These reports are prepared at the end of the accounting period so that various parties may take decisions of their future actions in respect of the relationship with the business.
- c) The reliability of financial statement depends on the reliability of accounting data.
- d) The figures in the financial statements are a combination of recorded facts.
- e) These statements are prepared as per accounting concepts and conventions.
- f) These statements are influenced by the personal judgment of the accountant through he/she is expected to be more objective in his/her approach.

2.2.3.1. Balance sheet:-

In early sixteenth century, Simon Steven of Burger (Belgium) first devised what he called a statement of affairs of business. The modern name of statement of affairs is called balance sheet. The assets and liabilities should be arranged in balance sheet in some specific order. The arrangement of assets and liabilities in the balance sheet is called 'Marshalling of assets and liabilities.' These are two systems of arrangement of assets and liabilities in the balance sheet.

1. Order of liquidity

2. Order of permanence

In liquidity order most easily realizable are shown first and are followed by assets, which are less easily realizable. So, the assets most difficult to realization will be shown last. In case of liabilities, these will be shown in the order in which they are payable the most pressing liabilities being placed first. But, the order will be reversed if balance is prepared under the order of permanence.

The balance sheet is a significant financial statement. In fact it is called the fundamental accounting report. Balance sheet provides the value of firm's assets

(what the firm owns), liabilities (what the firm owes to outsiders) and equity (what the inside shareholders or owners own) on a particular date. The value of assets will equal the value of liabilities plus owner's equity (or $A=L+E$). Items in the balance sheet are listed based on conservative principle i.e. if estimating or in doubt of the actual value, the value of assets is not be overstated and the value of liabilities is not be understated.

Assets includes current assets (ex. cash, marketable securities, account receivable, inventory, prepaid expensed) that are more liquid than the long term/fixed assets (ex. equipment, machinery, furniture, land, building), assets that are intangible and yet valuable (ex. goodwill, patent, deferred charges). Liabilities could include current liabilities (ex. bank advances, income tax payable, and account payable, accrued expenses), deferred income taxes (difference between the tax reported on income statement and tax reported on the tax return), long-term debt (ex. bonds, capital leases). Shareholder's equity includes share capital (par or stated value of shares received at the time of original issue), paid-in-capital (when shares are sold for more than the par or stated value), retained earning (undistributed earning), foreign currency translation adjustment (fluctuation in the value of assets of foreign subsidiaries due to change in exchange rates). Equity is also expressed as "residual interest ($E=A-L$). If E is negative, the firm is technically bankrupt.

Use of Balance-sheet

Balance sheet is helpful in ascertaining the financial position of the business by showing assets and liabilities of the concern on a specific data.

1. It discloses a solvency of the business/firm by showing how much assets are available for the payment of liabilities.
2. It also discloses the proprietary interest of owner.
3. It helps in calculation of various ratios which help in better management of business.

4. It helps in comparison of assets and liabilities of business on two dates to ascertain the progress being made by the organization.
5. It helps to ascertain the amount of capital employed in the business.

Limitation of Balance-sheet

The major limitations of the balance sheet are as follows:

1. Balance sheet cannot reflect those assets, which cannot be expressed in monetary terms such as skill, honesty, loyalty & efficiency of workers etc.
2. Some of the current assets are valued on estimated basis, so the B/S is not in a position to reflect the true financial position of the firm.
3. Fixed assets are shown in the B/S at original cost less depreciation up-to-date. Thus B/S does not show true value of assets.
4. Intangible assets like goodwill are shown in B/S at imaginary figures, which may bear no relationship to the market value.
5. An analyst should pay close attention to 'off-balance sheet item' too.

2.2.3.2 Income Statement

The second major statement of financial information is income statement. It is also known by several other titles such as profit and loss account, Statement of earnings, statement of operations & profit and loss statement. Income statement portrays, as a statement, the operations over/during a particular period of time. The purpose of every business firm is to earn profit, the operation of a firm in a given period of time will truly be reflected in the profit earned by it. "The income statement/profit and loss account of a firm reports the result of operations in terms of income/net profit in a year." (*Khan & Jain; 2000: 28*)

Thus income statement basically provides information on the various revenue and expense items during a certain period. This statement shows the total income generated in a certain period and the expenses made by the firm on that

date. “The earning capacity and potential of the firm are reflected by income statement and it is the ‘Score-board’ of the firm’s performance during a particular period of time.” (*Anthrony; 1970: 1*)

“In operation terms, the accounting report that summarizes the revenue items, the expenses items and the difference between them (net income) for a accounting period is called the income statement.” (*Pallai; 1994: 1325*)

Items in the income statement are based on accrual principle. Further more the expenses are matched to when the revenue is recognized and not when the actual payment is made. The above principle makes it obvious that there could be wide discrepancy a firm’s revenue and actual cash flow. There are several forms of income statement. The common format of incomestatement as per step form is given below.

The Hypothetical Ltd.

Income statement for the year ending March 31, 2011

Sales & other sources revenue		xxx
Less: cost of goods sold		<u>xxx</u>
Gross profit		xxx
Less: Administrative, selling expenses	xxx	
Depreciation	<u>xxx</u>	<u>xxx</u>
Earning before interest and taxed (EBIT)		xxx
Less: Interest expenses (on bank loan & bonds)		<u>xxx</u>
Earning before fax (EBT)		xxx
Less: Taxes (current and deferred)		<u>xxx</u>
Earning after tax (EAT)		xxx
Less: preferred stock dividend		<u>xxx</u>
Earning available to common stockholders		<u>xxx</u>

Limitations of income statement

In finance, the focus is on “valuation” that requires knowledge of expected cash flows rather than historical earning. Net income does not equal the actual cash flow. This is because the income statement reports revenue/expenses when they earned/accrued and not when actual cash is received. Several items such as: depreciation, are subjectively determined. Depreciation is based on historical cost of assets and during the periods of inflation, it will be understated as it is based on historical cost while the revenues reflect the current market price. This type of non-synchronization leads to inflated earnings.

Furthermore tradition income statement/profit & loss on records transecting, it does not maintain any opportunities. Particularly the economist defines income as the change in real worth that occurs between the beginning and the end of a specified time period. In this sense, a more income statement is not sufficient for analyzing firm “financial performance.”

2.2.4 Need & significance of financial statements

The figure appearing in financial statements may be said to have significance in the following aspects: (*Nagaratnam; 1980: 141*)

1. They have the measures of absolute quantity. Where the financial statements contain an item of current assets the analyst understands the figure in terms of the current purchasing power and it can not tell him whether it is sufficient to meet the current obligations. Therefore some other means of determining its significance is necessary.
2. When figures are compared with those of other years and similar types of industries a degree of significance is disclosed by the financial statements.
3. The margin of safety can be assessed by comparing the current assets with current liabilities by analyst.

2.2.5 Uses of financial statement

The most important users of the financial statement are the present and prospective shareholders, creditors, employees, financial analysts, customer and government agencies. Each of them has different needs for the kinds of financial information from the statement. Such a:

1. The owners/shareholders want to know whether their funds are being properly utilized or not. The financial statements are prepared from time to time satisfy their curiosity.
2. The creditors/money lender use financial statement to judge financial position of the firm before giving loan or granting credit.
3. It is more useful to the prospective investors to measure the safetiness of their proposed investment.
4. It is also useful to the employees working in the firm, to know that the bonus being paid to them is reasonable; so they become interested in the preparation current profit & loss account/income statement.
5. The regulating authorities like government agencies use the financial statement in determining tax liabilities and formulating effective plan and policies. Moreover, these statements are used for compiling statistics concerning business, which in turn help in compiling national accounts.
6. The financial statements, being a mirror of the position of firm, are of immense value to the researcher who wants to make a study in financial operation of a particular firm.
7. Consumers, who are the receiver of the goods and services from the firm, are interested in the establishment of good accounting control. So that cost of production may be reduced with resultant reduction of the prices of goods they buy.
8. The bondholders, on the other hand, are more interested in the cash flow ability of the firm is present and expected future earning and stability of the

earning about trend as well as their co-variance with the earning of other organization /firm.

9. In fact, management is of getting things done through others. The financial statements are an aid in this respect because they serve the manager in appraising the performance of the subordinates. Thus the management of a firm employs financial analysis for the purpose of internal control.

2.2.6 Limitations of Financial Statement

In spite of the various usefulness, financial statement can nor serve the purpose of giving a free and complete picture of the financial position, the financial health and capabilities of an enterprise. The following are the serious limitations of the financial statement:

1. “The data contained in the financial statements can not be expected to be precise because they are prepared on the basis of the application of precedents, conventions, postulates, assumptions and personal judgment of the accountant preparing them. As the preparations of the statement require the use of judgment and estimates of the accountancy, they may not be uniform and reliable owing to differences in the exercise of personal judgment principles governing the preparation of financial statement vary from one company to another. There is no agreement as to the principles adopted by the companies. Not all companies apply the general principles governing the preparation of financial statements. If alternative practices are followed the result will be different.” (*Nagaratnam; 1980: 151*)
2. Financial statements do not depict the exact position and are essential interim reports. The exact position can be only known if the firm is closed.
3. As the statements are prepared for the use of ‘an average reader’ it will not be possible to satisfy the requirements of the user for special purpose.

4. Financial statements disclose only monetary facts. Those transactions which can not be measured in monetary terms such as, conflict between production manager and marketing manager, goodwill created by the company, efficiency in the management of business operations, the reputation of the company, the company's/firm's cordial relationship with its employees, qualities of research and development, plant efficiency. In absence of non-monetary terms and its uniform unit of measurement, financial statements can not be reliable.
5. The data/information given in financial statements are in historical in nature i.e. this data/information is drawn after the actual happening of events. They attempt to present a view of the past performance and have nothing to do with the accounting for the future. Modern management is forward looking but these statements do not directly help them in making future estimates and taking decisions for the future.
6. These statements provide artificial view as market value or replacement value and the effect of the changes in the price level are completely ignored.
7. It will be very difficult to correctly understand the position of a firm if these statements have been prepared under abnormal condition like high inflation period, war period etc.
8. There are many parties who are interested in the information given in financial statement, but their objectives and requirements are differing. The financial statements are prepared as per the related/required act (i.e. company act, banking act etc.) which leads to far to meet the need of all parties. These are mainly prepared to safeguard the interest of owner/shareholder.
9. Financial statements are prepared in a simple and summarized form so that the user can able to understand with out any difficulties. In this process comprehensiveness and clarity are usually lost and rational economic decision can not be taken.

10. These statements are sometimes prepared according to the needs of situation or the whims of management. A highly efficient concern may conceal its real profitability by disclosing loss or minimum profit where as an inefficient concern may declare divided by wrongly showing profit in the income statement. For this purpose under or over valuation of inventory, over and under charge of depreciation excessive or inadequate provision for anticipated loss and other such manipulation may be resorted, window dressing may also be resorted in order to show better financial position of a concern than it's real position.

2.2.7 Financial Statement analysis and interpretation

Many organization, nowadays, are facing much problem about making better analysis on their financial position. Financial analysis is only key tool to analyze the firm's financial performance and it's position. A poor financial analysis may lead the firm to become failure. Furthermore, the organization with poor financial analysis could not make a better planning for it's perpetual growth. "In order to bargain more effectively for outside funds, the management of a firm should be interested in all aspect of financial analysis that outside suppliers of capital use in evaluating the firm." (*Van Horne, 2000:691*)

In fact a financial analysis is a systematic study and analysis of financial statement like balance sheet, income statement and cash flow statement etc. of the firm. The major purpose of financial analysis is to get the detail knowledge of financial/economic condition of an organization. Financial analysis flow the information about relationship of several items shown in financial statement. It involves analyzing the firm's financial statements to extract information that can facilitate in decision-making. An analysis of financial statements can reveal whether the firm will be able to meet it's long term debt commitment whether the firm is financially distressed, whether the firm is using it's physical assets

efficiently, whether the firm has an optimal financial mix, whether the firm is generating adequate returns for its shareholders, whether the firm can sustain its competitive advantage. “The analysis of financial statement is done to obtain a better insight into a firm’s position and performance.” (*Munakarmi; 2002: 461*)

“The analysis of financial statement is a process of evaluating relationship between component part of financial statement to obtain a better understanding of the firm’s position and performance.” (*Metcalf & P.L.; 1976: 197*)

In this sense, financial analysis is the process of critically examining in detail accounting information given in financial statement. For the purpose of analysis individual items are studied, their interrelationship with other related figures established, the data is rearranged to have better understanding of the information with the help of different techniques or tools. The main function financial analysis is a pinpointing of the strength and weakness on a business undertaking by regrouping and analysis of figures contained in the financial statement by making comparisons of various components and examines their content.

The data contained in the financial statements are dumb; they do not speak themselves. Human judgment is always involved in the analysis and interpretation of statements. Financial statement is the analyst or user who provides tongue to those data and makes them to speak. The financial analysis basically depends upon the financial statements prepared by the firm and personal judgment of the analysts.

The analysis of bank statement is undertaken by analysts, depositors, regulating authorities, stockholders, borrowers, the bank management and authors of books. A depositor is interested in the solvency of the bank, i.e. the safety and availability of his funds. The regulating authorities desire to assure themselves that bank are operating in accordance with the requirements of the law and are in sound financial condition stockholders are primarily interested in the general financial condition of the bank and the earnings, the dividends, and the management’s

policy with reference to the accumulation of surplus. The borrower is interested in knowing the extent of available funds and the use that is made of the bank's resources.

The management of a bank has several obligations the fulfillment of which is made easier and more certain with the aid of financial statement analysis. These major obligations are to meet the demand of the depositor, both for financial services and for safekeeping of funds; to satisfy the sound credit needs of the community; to earn the fair return on the equity of the stockholders; and to fulfill the legal requirements as reflected by laws and the rules and regulation of the regulating authorities.

In the words of Myers "financial statement analysis is largely a study of relationship among the various financial factors in a business as disclosed by a single set of statement and a study of the trend of these factors as shown in a series of statements. "In brief financial analysis is the process of selection, relation and evaluation." (*Meigs; 1978: 1049*)

"The analysis of financial statements refers to the treatment of the information contained in the financial statement in a way so as to afford a full diagnosis of the profitability and financial position of the firm concerned. For this purpose, financial statements are classified methodical analysis and compared with the figures of previous years or other similar firms." (*Jain & Narang; 1991: 114*)

In fact the financial analysis includes: (*Paillai & Bhagavathi; 1994: 1330*)

-) Breaking financial statement in to simpler one.
-) Regrouping
-) Rearranging the figures given in financial statement and
-) Finding out ratios and percentage.

"The work of and accountant/analyst in making analysis of financial statement is the same as that of a pathologist, who takes a drop of blood and analysis it to

point out its various components and gives a report on the basis of his/her analysis.” (*Ibid...*1330)

After analysis of financial statement its interpretation is most necessary. Interpretation is impossible without analysis and without interpretation analysis has no value. In fact analysis means breaking down a complex set of facts or figures into simple elements and interpretation means to put the meaning of statement into simple terms and to explain in such a simple language of the financial position and earning capacity of the firm which may be understood even by a layman who does not know accounting. Thus interpretation acts as a bridge between the art of recording and reporting financial information and the acts of using this information. So analysis refers to the process of fact finding and breaking down complex set of figures into simple components while interpretation status for explaining the real significance of these simplified components. Interpretation is mental process based on analysis and criticism and it is dependent on the interpreter him/herself. It is the drawing of inference and stating what the figures in financial statements actually mean. Interpreter must have experience, understanding and intelligence to draw correct conclusions from the analyzed data.

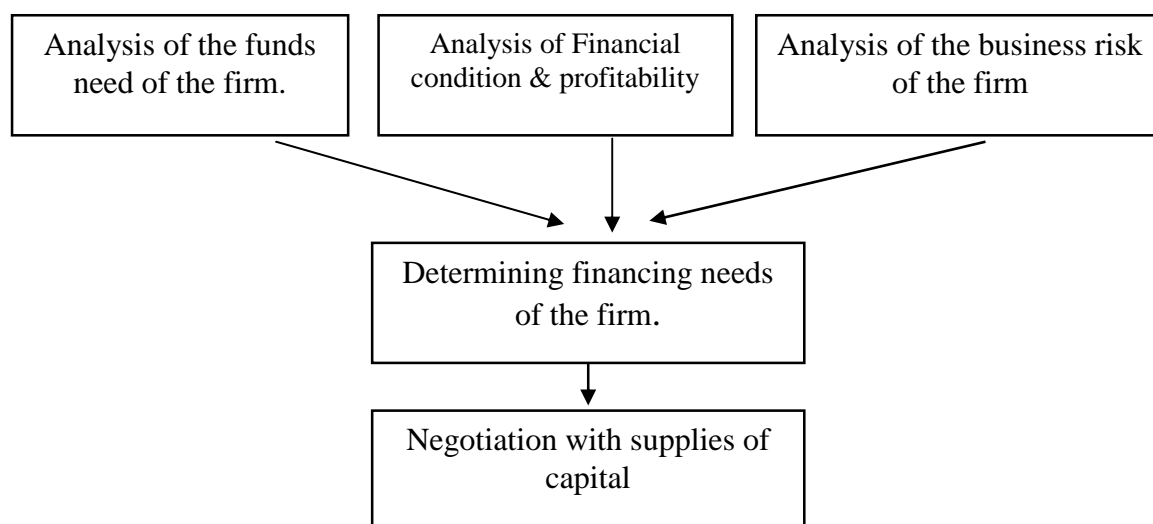
In the word of Kennedy and Medullar “the analysis and interpretation of financial statements is to understand the significance and meaning of the financial statements data so that a forecast may be made of the prospects for future earnings ability to pay interest and debt maturities and probability of sound dividend policies.” The most important objectives of the interpretation of financial statements is to understand the significance and meaning of financial statements data to know the strength and weakness of the business undertaking so that a forecast may be made of the future prospects of the business undertaking.

Financial analysis is performed by both internal management and external groups. The type of financial analysis varies according to the specific interest of the party involved. The firm's management would perform such analysis in order to

their overall current performance identify problem/opportunity areas develop budgets and implement strategies for futures. The external grows (such as creditors, lender, bondholders, investor, shareholders, regulators etc.) also performs financial analysis in deciding whether to invest in a particular firm whether to extend credit etc.

Generally three types of analysis should be use in determining the financial needs of the firm, which can be stated below.

Figure No.1: Framework for Financial Analysis (Van; 1984: 102)



Objectives of Financial analysis

Financial analysis is helpful in assessing the financial position and profitability of a concern. Some of the major objectives of analysis of financial statements are to assess:-

1. The present and future earning capacity or probability of the concern.
2. The operational efficiency of the concern as a whole and its various parts or departments.
3. The short term and long term slovenly of the concern for the benefit of the bondholders and trade creditors.
4. The comparative study in regard to one firm with another or one department with another department.

5. The possibility of departments in the future by making forecasts and preparing budgets.
6. The financial stability of a business firm.
7. The real meaning and significance of financial data.
8. The long-term liquidity of its funds.
9. The financial performance of the firm.
10. In making future plans.

2.2.8 Techniques and tools of financial statement analysis

The purpose of financial analysis is to suggest questions or area for further investigation rather than provide answer. According to Mr. W.H. Beaver, “there are two board purposes of financial statement analysis: (1) Solvency determination, and (2) profitability evaluation. Solvency determination involves determination of the assessment of profitability that and undertaking will fail. By the use of trend percentage technique, it is possible to predict the failure of a business. The ratios of failure firms implied substantially higher probability of failure that the population as a whole, and this higher probability of failure was evident in the ratio data five years before failure.”

In analyzing the financial statements the analyst has a number of tools to employ. One can choose the best to suit his need. These tools are:

1. Comparative financial statements
2. Common size financial statements
3. Trend percentage analysis
4. Cash flows and funds flow analysis
5. Net working capital analysis
6. Ratio analysis
7. Correlation analysis

2.2.9 Comparative financial analysis

The change in the financial data over a period can be best understood if the statements containing data for a period of two or more years are placed side by side in adjustment columns. Such statements are called comparative financial statements. By comparing the change in various items period by period, the analysts/researcher will be able to get some valuable clues as to the growth and other important trends relating to the business. A study of the financial position of a company and the result of its operation for a period is more meaningful if the analysts has available the statements of financial position and income statements for several period when comparison is made.

There are two types of analysis, called *horizontal* and *vertical* which forms the 'back bone' of financial statement. (*Nagarathnam; 1980: 146*)

Horizontal statement is a statement containing the balance figures of successive periods. The current year's figures are compared with the standard as base year. Usually the statements will contain figures for two years and in one column, the figure for the current year. The next column will show the rupee change in percentage. This type of analysis is considered as the type of analysis because the analysis of change in the statement will give the management considerable insight into the levels and areas of strength or weakness.

Vertical statement is a static type of analysis which contain each item in the balance sheet expressed as a percentage of total assets and in the income statement the net sales is used as the base for manufacturing organization and total income for service organization. This deals with the study of the qualitative relationships of the various items in the statements at a particular data. These statements are useful in analysis and comparing several companies/firms in same group or divisions within company/firms.

2.2.9.1 Comparative Balance Sheets

A comparative balance sheet shows the assets, liabilities and owners' equity of a business for two or more dates with increases and decreases in the absolute data in terms of rupees and percentages. This facilitates the comparison of figures of two or more periods and provides necessary information, which may be useful in forming an opinion regarding the financial condition as well as progressive outlook of the concern. The change in the balance sheet items consist of the result of the profit and loss, acquisition of assets, change in current assets, conversion of liabilities into another form, payment of liabilities and issue of shares etc. comparative balance sheet facilitates easy comparison of the trends of the business firm.

2.2.9.2 Comparative Income Statement

This statement discloses the net profit or net loss resulting from the operation of business. The changes in the data will be shown in terms of rupees and percentages which help in deriving meaningful conclusions as it is very easy to ascertain the changes in sales volume, administrative expenses, selling and distribution expenses, cost of sales etc.

Thus comparative financial statements are very useful for analysis because they not only contain certain data but also information necessary for showing the financial and operative trends for a period of years. The nature and trends of these changes indicate the direction to which the financial position and operating results the business move. But the comparison will have no use or will be misleading if the data contained in the statement do not reflect the consistent application of accounting principle.

2.2.9.3 Common Size Statement

The common-size statements indicate the relationship of various items with some common items (expressed in percentage of common items). Generally two common-size statements are prepared while analyzing the firm's "condition & operation i.e. common-size balance sheet & common-size income statements.

Common-size balance sheet discloses the relationship of each asset to total assets and each liability and capital item to total liabilities & capital in order to find out the proportion of a group or sub-group with a single item in the group represent in financial statement analysis of common-size balance sheet is used. Comparison of the common-size balance sheet of a single enterprise over the past years is very useful as the changing proportions in the components within the group; of the trends are to be correctly interpreted, it is necessary to determine the normal percentage of individual assets to the total assets.

Common-size income statement is prepared with a view to compare the various items in the statement to the total amount of sales or total income. Items such as cost of goods sold, selling & administrative expenses and also items of income are reduced to percentage by taking the sales figure as 100%. But for non-manufacturing organization (such as bank) takes the whole income as a base (i.e.100%). The percentage so calculated can be easily compared with the corresponding percentage in other periods and meaningful conclusion can be drawn.

2.2.9.4 Trend Percentage Analysis

To overcome the major limitations of common-size statement (i.e. absence of basic standard to indicate whether the proportion of an item is normal or abnormal) trend analysis is made as a useful technique of financial statement analysis changes in financial statements between the periods can be easily studied by establishing a base year and expressing other years in terms of the base year.

The trend percentage statement is an analytical device for condensing the absolute rupee data by comparative statement. It also indicates the degree of increase or decrease but they can not indicate cause for changes. Particularly the figure of base year is taken as 100. The trend percentages show the relationship of each item with it's preceding year's percentages. These percentages can also be presented in the form of index numbers showing relative change in the financial data of certain period. This will exhibit the direction (i.e. upward or downward trend) to which the concern is proceeding. These trend ratios may be compared with industry in order to know the strong and weak points of the firm. Trends may be favorable and unfavorable too. Favorable trends are increase in sales, accompanied by a decrease in the cost of goods sold and selling expenses and increase in current assets with corresponding decrease in current liabilities and increase in deposit collection, increase in loan investment etc for banking organizations. Similarly in favorable trends include an upward trend in sales. It should be noted that the trend percentages are computed only for the items that have some relationship and not for all items.

In interpreting the trend, the analyst should consider the 'profitableness of the change' compare the trend data for the particular business with that of business in general and of the industry involved and determine to what extent, changes are the result of price level changes. If the base year is not typical or representative of the items in the statement, variations in the subsequent period will affect the comparability. In order that the trend percentage may be reliable, it is necessary to study the rupee variations and also the relationship of the items after changes have taken place before arriving at the conclusion whether the trends favorable and unfavorable. The most important value of trend analysis is that it can disclose to the analyst a better understanding of management's policies and motives, which are the causes for the change. The noted point is that though the trends are important when percentage of various relative items are compared but undue

emphasis can not be laid when there is a small number in the base year. In this case, Mr. Myer has given in fine example:

“In a college it was announced one morning that during the night 33.33% of the female students has eloped. However the college had only three female students.”

Therefore it is always desirable that when comparison is made, regard should be had both to absolute and relative changes. The trend may be prepared to show the graphical history of a concern by slotting curves of the trend ratios for several years. The trend percentage can be represented in the following ways. (*Nagaratnam; 1980:150*)

1. Horizontal manner: - When the percentage of each year appears are after another.
2. Vertical manner:- When the percentage of each year appears are below the other.
3. By a chart containing inventory and sales for some year in rupees.
4. One semi-logarithmic scale showing the inventory and sales for some years in rupees.
5. Showing the trends of average selling prices using as the trend of X as index.

Limitations of the trend percentages are (*Ibid; 151*):-

1. In respect of the variation of the least significant factors in the balance sheet undue emphasis is attached. This will not be of much help in measuring the changes precisely.
2. If the items in the base year selected are not normal, representative and much emphasis is made for the same in the matter of measurement of the changes with the item contained in the balance sheets of subsequent years, the result will not be reliable.

3. If the balance sheet changes are grouped together instead of leaving them as unrelated items, in the preparation of funds statement, the net inflow of funds can not be considered to be precisely prepared.
4. If the changes in the assets are shown as net instead of as gross, it will be easy to ascertain the increase in the assets & depreciation separately.

To make the trend analysis meaningful while analyzing financial statements following precautions may be taken (*Jain & Narang; 1991:VI/14*):

- I. The accounting principles must be followed constantly over the period for which the analysis made. This is necessary to maintain consistence and comparability.
- II. The base year selected should be normal and representative year.
- III. Trend percentage should be calculated only for those items, which have logical relationship with one another.
- IV. Trend percentage should be carefully studied after considering the absolute figures on which these are based. Otherwise, they may give misleading conclusions.
- V. To make the comparison meaningful, trend percentages of the current year should be adjusted in the light of price level changes as compared to base year.

2.2.9.5 Net working capital analysis:

The term working capital refers to the investment by a firm in short-term assets such as cash, marketable securities, account receivable and inventories. Net working capital refers to the current assets less current liabilities. A company's profitability is in one way determined by the management of its working capital. When there is variation of working capital to sales without a corresponding change in its production, the profit are affected. When the flow of funds caused by the changes in the working capital generated by various processes in the business in

interrupted, the working turnover decreases as well as the return on investment. In this sense, planning and controlling working capital position is the most important function of the management. In fact, the magnitude of working capital is a measure of the safety margin that exists of the protection of short-term creditors. Working capital may also be viewed as funds available for acquisition of non-current assets as well as to repay non-current liabilities. Any transaction that results in increase in working capital is a source of WC; any transaction that causes the net decrease in working capital is an application of WC.

The magnitude of working capital depends upon the nature of organization and its size. Insufficient working capital and overworking capital is not favorable for the firm. Therefore, optimum working capital must be required for smooth running of the organization. There are three approaches regarding investment and financing of current assets level.

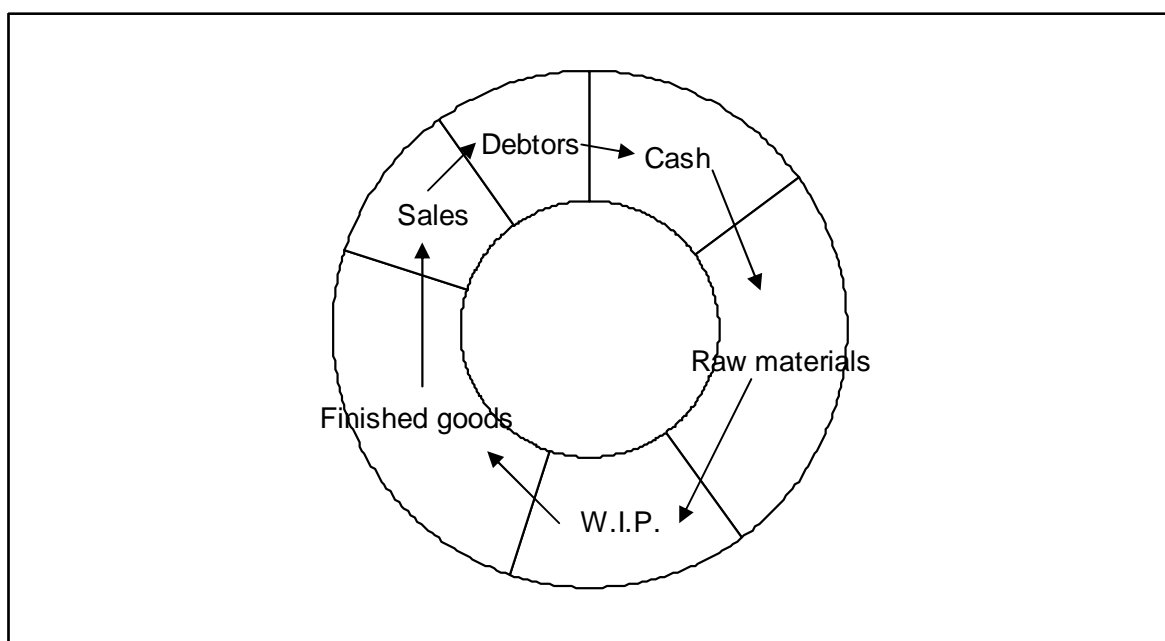
- (1) Conservative working capital policy
- (2) Moderate policy
- (3) Aggressive policy.

A *conservative policy* is that which advocates holding of sufficiently large of assets to be financed by high level of long term sources. The *moderate approach* tries to stress a balance between two extreme approaches. The idea is to finance each asset with a financing instrument of approximately same maturity. Under this policy, long-term & short-term financing, respectively, finances permanent working capital and fluctuating working capital. Similarly, *aggressive approach* stress in keeping low level of current assets as far as possible, which says that it should be financed by maximum level of short-term financing sources.

Additional working capital will be required if the volume of sales/transactions of a business expands. Working capital depends upon the period of time required for converting amounts receivable into cash. If less time is required for conversion,

the lower will be the amount of working capital required. Working capital has a certain cycle. The following diagram illustrates the several current assets forming the working capital cycle, which is basically applicable to the manufacturing organization.

Figure No: 2 Working capital cycle (*Nagaratnam; 1980:452*)



2.2.9.6 Funds flow analysis

The financial statements fail to show how the net income for a period is disclosed of and the effect of flow of funds through the business. They do not give anything like a complete report of the financial activities of all resources provided during the period and the uses to which they are put. The funds flow statement (analysis) overcomes such limitation of financial statements.

Funds flow statement (analysis) is a widely used tool in the hands of financial executives for analyzing the financial performances of a concern. The word 'fund' refers to the net working capital i.e. excess of current assets over current liabilities. Funds keep on moving in a business which itself is based on a going concern concept. When the funds move in-ward or out-ward, the cause a flow or rotation of fund. "The flow of funds refers to transfer of economic values from one asset to

another, from one equity to another, from assets to equity or vice versa or a combination of any of these." (*Pillai and Bhagavatgi; 1994:1403*)

The funds flow statement is prepared to indicate the increase in the cash resources of a business during a period. It helps to enable the management to know the movement in liquid assets between two dates. It shows the ebb and flow of fund into and out of the business. This statement gives a clear picture of what has become of the net profit and of the fund obtained from other sources. It is a means of analyzing in detail the items contained in the balance sheet by recast of increase and decrease of certain figures not found in balance sheet and linking in the analysis. Funds flow statement serves as an indication of the highlighting of the changes that have taken place during the period in the financial statement of the concern. It shows the various means by which these resources were employed. "Funds flow statement is a report on movement of funds explaining where from working capital originates and where it goes during an accounting period." (*Ibid...1403*) It is a useful tool in the financial manager's analytical kit. "Funds statement is a method by which we study the net funds flow between two points in a time." (*Van; 2000:728*) Funds flow statement is called by a variety of names, such as statement of source and application funds, summary of financial operation; where got-where gone statement; Analysis of working capital changes, statement of funds supplied and applied, funds received and disbursed etc.

Funds flow statement summarizes the financial operations for the year indicating by what means new financing was obtained and for what purpose it was utilized. An analyst will get the answer of the following question through the funds flow analysis.

1. Where did the funds come from?
2. What was done with them?
3. What happened to the various asset items during the period?
4. Why did working capital decrease although earnings were favorable?

5. Why were dividends not larger?
6. Is the concern solvent?
7. Where did the funds for replacement or expansion come from?
8. What kinds of financial decisions were made during the period?

Funds flow statement helps the reader of the financial statement to understand not only the financial stability of the concern but also the successful implementation of the financial policies of the management. The high skill on the part of the management with which the management decisions are arrived at can be reflected in the smooth flow of funds in and out of business. Funds flow is equally important to the internal and external parties. It is employed by the management in establishing and reviewing cash budgets. They help the management in evaluating of alternative financing plans and of assessing the long-range forecast of cash requirements and availability. Similarly, outside investors are interested in the flow of fund to enable them to appraise the company's performance in using that have been supplied by them. They are more interested on the capacity of the company in generating current funds in it's normal operation of the business and in the company's financing policies by the employment of the methods of financing in the past. The creditors are equally interested the flow of fund in assessing the degree of risk that may be involved in granting credit to the business.

Funds flow statement contains two main groups of items one the means by which resources are acquire and the other their disposition or utilization. These two sectors of items will be equal in amount since the resources, which are provided by business operations are necessarily utilized in some way.

The following are the sources from which funds come. These are called sources of funds:

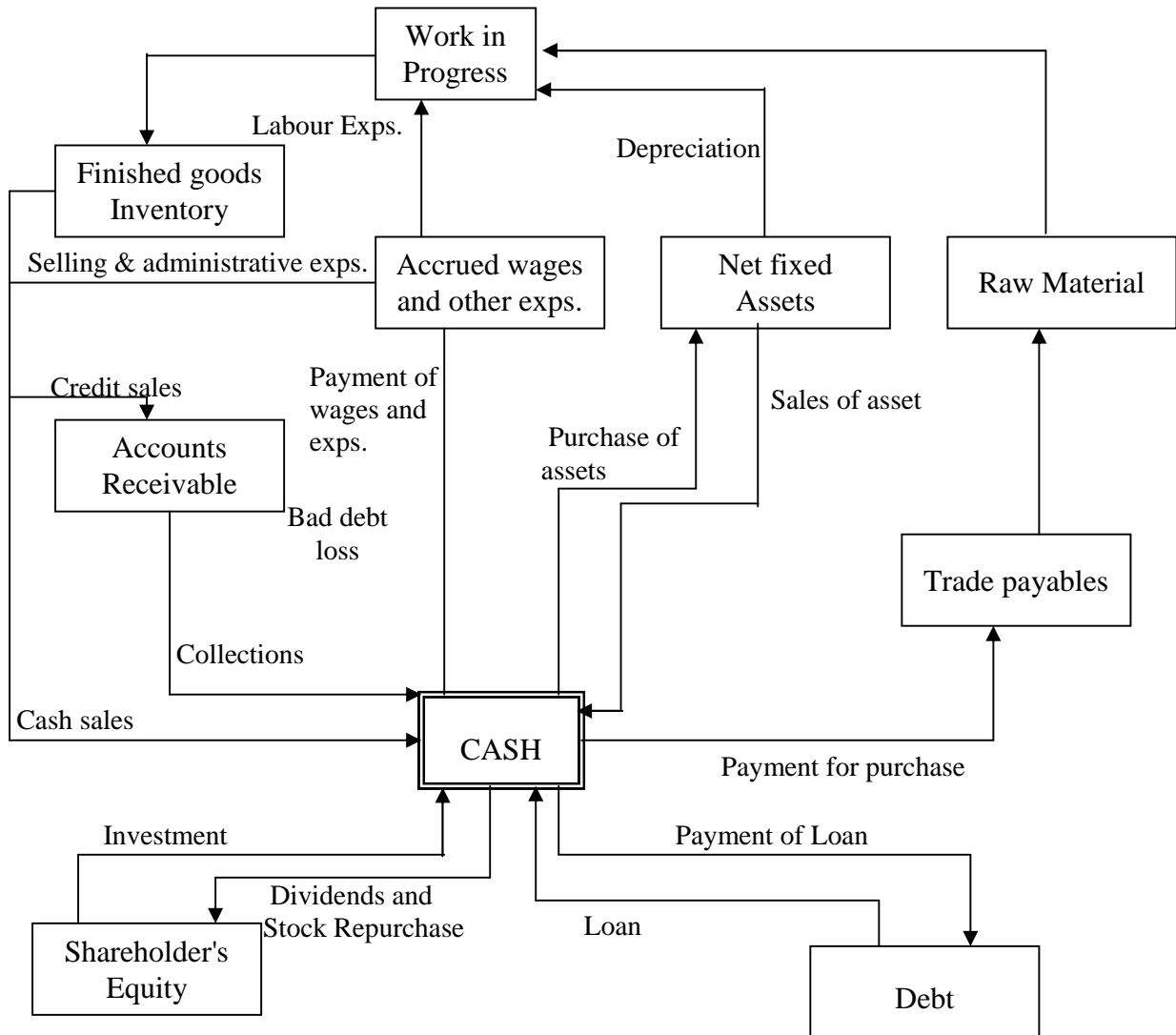
1. Funds from operation/profit from operation
2. Income from sale of investment
3. Issue of share and debenture
4. Raising of loan
5. Receipt of interest of non-trade investment dividend refund of tax
6. Sale of fixed assets, long-term investments and other non-current assets
7. Decrease in working capital.

The following are the various purposes for which funds can be used. These are called application a uses of fund:

1. Funds lost in operation/loss from operation
2. Repayment of long-term loan
3. Redemption of preference share and debenture
4. Purchase of long-term investment
5. Purchase of fixed assets
6. Payment of cash dividends, income tax etc.
7. Drawings in case of proprietary or partnership firm
8. Loss on cash by embezzlement
9. Increase in working capital.

The followings figures shows how the fund flows in a certain firm (specially for the manufacturing firm)

Figure No. 3: Funds flow cycle within the firm. (Van; 2000:729)



The limitation of the funds flow statement can be maintained in the following points:-

1. The statement lacks originality because it is only rearrangement of data appearing in accounts books.
2. It indicates only the past position and not future.
3. It indicates fund flow in summary form and it does not show various changes which takes place continuously.
4. When both the aspects of a transaction are non-current, even then they are not included in this statement.
5. It is not an ideal tool for financial analysis.

2.2.9.7 Cash flow analysis (Statement)

Funds statements fail to explain the change in cash balance. The movement of cash is of vital importance to the management, for if the in flow's of cash are not sufficient to meet the out flows, the firm will not be able to meet it's current obligation. Many a time management is posed with the paradox of huge profit and yet impossible to pay dividends or even taxes. For ex. if credit sales remain uncollected, profit may good but the cash position of the firm will be bad. Therefore the management is interested to know about the movement of cash and the availability of cash. For this cash flow analysis provides this information.

Cash flow statement concentrates on transaction that has direct impact on cash. It deals with the inflow and out flow of cash between two balance sheet dates. It explains the changes in cash position between the two periods. In fact, cash flow statement is of recording systematically all inflows and outflows of cash of the accounting period. Thus it shows the sources (inflow) of cash receipts and the purposes for which payment (outflow) are made. It summaries the causes of changes in cash position between dates of the two balance sheet. This statement analyses changes in non-current account to determine the flow of cash. "The projected cash flow statements prepared month wise or so (which are constructed like the funds statement) can be useful in presenting information of excess cash in some months and shortage of cash in others." (*Perry; 1961:45-50*)

Cash in the lifeblood of a business enterprise. It is the fuel that keeps a business alive. Without cash no activities can be taken place. So a business must have an adequate amount of cash to operate. The decision makers must pay close attention to the firm's cash position and events & transaction that affect/cause cash position to change. The management of cash inflows and outflows accurately and there is no perfect coincidence between the inflows and outflows of cash giving rise to either cash outflows exceeding inflows or cash inflows exceeding cash outflows. Thus, cash flow statement is one important tool of cash management

because it throws light on cash inflows and cash outflows of a particular period. Cash flow analysis is equally useful to the investor, creditor & management too. Investor will value higher to the company whose regular operating cash flow is more than uses, creditor decide whether a company will have enough cash to pay the debts as they mature, and management evaluate whether the company has ability to meet unexpected obligation and ability to take advantage of new business opportunities that may arise. In general, cash flow analysis (statement) attempts to answers of the following questions: (*Munakarmi; 2002:505*)

1. If a company operates at a profit, why is it continually short of cash?
2. How can a company operate at a loss and still generate huge inflow of cash from operations?
3. How was the company's growth and expansion financed?
4. Did the company acquire and long-term investment or other income producing assets?
5. Was financing obtained during the period through issuance of debt or equity securities? If so, what were the amounts of cash obtained?
6. Did the company use cash to retire any long-term debt or equity securities during the period?
7. Are the company incomes producing activities using more cash than they are generating?
8. Do operating activities consistently generate enough cash to assure prompt payment of operating expenses, maturing liabilities, interest obligations and dividends?

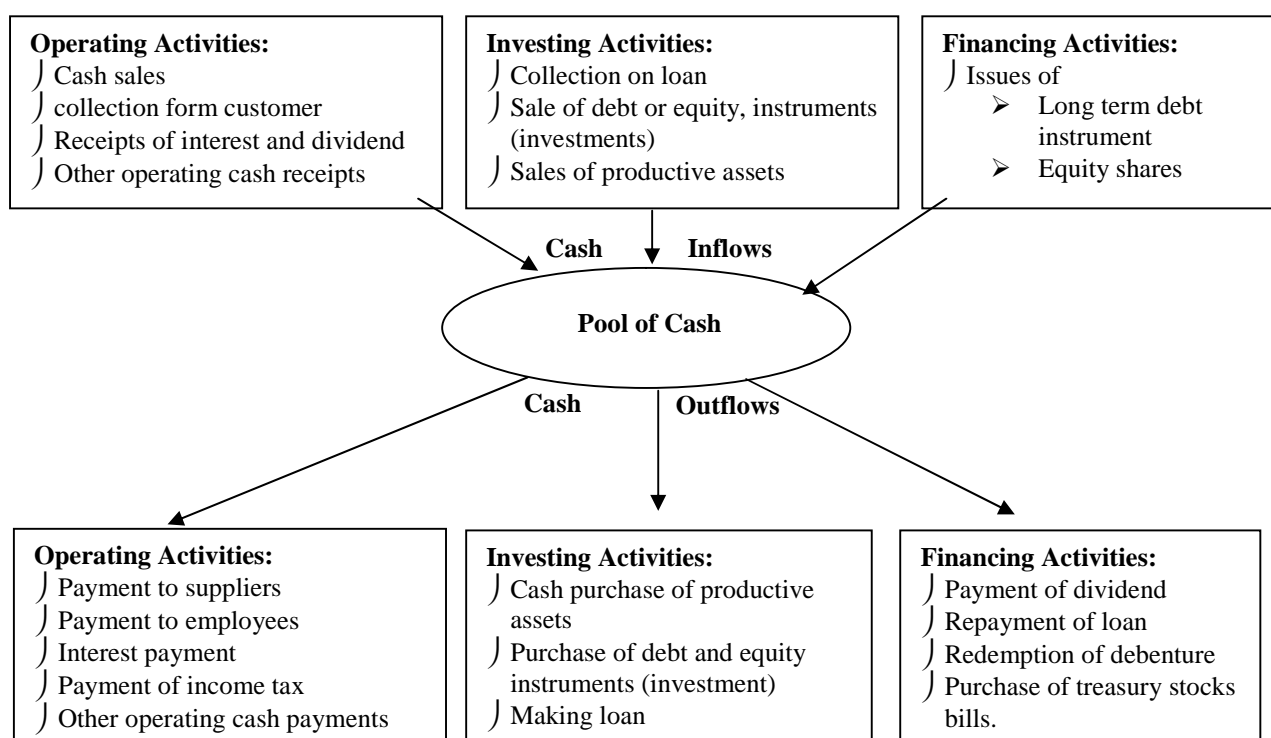
In this way the primary purpose of the cash flow analysis is to provide the information regarding a firm's cash inflow and outflow during accounting period.

The analysis should be informative regarding cash flows from the company's operating, investing and financing activities.

The flow of cash can be classified in terms of operating, investing and financing activities in the following manner.

Figure No. 4: Pull and Push factors of cash within the firm

(Munakarmi; 2002:512)



This information in a source and use of fund statement form (i.e. inflow and outflow of cash statement form).

2.2.9.8 Ratio Analysis

To evaluate the financial condition & performance of a firm, the financial analyst needs certain yardsticks. The yardstick frequently used is a ratio, or index relating two pieces of financial data to each other. Analysis and interpretation of various ratios should give experienced, skilled analysts a better understanding of the financial condition & performance of the firm that they would obtain from analysis of the financial data alone. In fact, "the term 'ratio' refers to numerical or quantitative relationship between two items/variables. The relationship can be

expressed as (1) percentages (2) fractions and (3) proportion of numbers.” (*Khan & Jain; 2000:42*)

The analysis of financial ratio involves two types of comparisons. First, the analyst can compare a present ratio with past and expected future ratios for the same company. These ratios can be computed for projected, or pro-forma, statement and compared with present & past ratios. In the comparisons over time, it is bet to compare not only financial ratios but also the raw figures. Secondly, comparisons with others involve comparing the ratio of one firm with those of similar firms or with industry averages at the same point in time. Such comparisons give insight into the relative financial condition and performance of the firm.

Ratio is used as an index of yardstick for evaluating the financial position and performance of the firm. It is a technique of analysis and interpretation of the firm. It is a technique of analysis and interpretation of financial statement too. It helps in making decision as it helps establishing relationship between various ratios and interpret thereon. It helps analyst to make quantitative judgment about the financial position and performance of the firm. The rationale is of ratio analysis in the fact that it makes related information comparable. A single figure by itself has no meaning but when expressed in terms of a related figure, it yields significant inferences. The ratio analysis, thus, as a quantitative tool, enables analysts to draw quantitative answer to questions such as: Are the net profit adequate? Are the assets being efficiently, is the firm solvent? Can the firm meet it's current obligations? And so on. Further more ratios are more of a diagnostic tool that helps us to identify problems areas and opportunities within a company.

Although the number of financial ratios that might be computed increases geometrically with the amount of financial data, we concentrate only on the more important ratio as per the need of study/analysis. Computing unneeded ratios add both complexity and confusion to the problem. Basically ratios are compute with

the help of income statement and balance sheet. In the broad category ratios can be classified as:

- Liquidity ratios.
- Leverage ratios.
- Profitability ratios.
- Activity ratios.

Liquidity ratios are used to judge a firm's ability to meet short-term obligations. From them, much sight can be obtained into the present cash solvency of a firm and it's ability to remain solvent in the event of adversities. Essentially, we wish to compare short-term obligations with the short-term resources available to meet these obligations. The importance of adequate liquidity in the sense of the ability of a firm to meet current/short-term obligation when they become due for payment can hardly be overstressed. In fact liquidity is a prerequisite for the very survival of a firm. The short-term creditors of the firm are interested in the short-term solvency or liquidity of a firm. But liquidity implies, from the viewpoint of utilization of the funds of the firm that funds are idle or they earn very little. A proper balance between the two contradictory requirements, that is, liquidity and profitability is required for efficient financial management. Thus, liquidity ratios measures the ability of a firm to meet it's short-term obligation and reflect the short-term financial strength/solvency of a firm. The ratios, which indicate the liquidity of a firm are: (i) Net working capital (ii) Current ratios (iii) Acid test/quick ratios (iv) Super quick ratios (v) Turnover ratios and (vi) Defensive interval ratios etc.

Note 1:- The non-manufacturing organization, like Banking, Insurance co. etc, do not apply the ratios relating to inventories and sales since they provide services not goods.

Leverage/capital structure ratios are the second category of financial ratios. The long-term creditors would judge the soundness of firm on the basis of the

long-term financial strength measured in terms of its ability to pay the interest regularly as well as repay the installment of the principal on due date or in lump sum at maturity. The long-term solvency of a firm can be examined by using leverage/capital structure ratios. In fact, leverage/capital structure ratios refer to the financial ratios which throw light in the long-term creditors with regard to: (i) Ability to repay the principal when due and (ii) Regular payment of the interest. There are two different, but mutually dependent and inter-related, types of leverage ratios. First, ratios which are based on the relationship between borrowed funds and owner's capital, which are:- (a) Debt equity ratio (b) Debt asset ratio (c) Equity assets ratio etc. second type of capital structure ratios, popularly called coverage ratios, which are (a) Interest converge ratio (b) Dividend coverage ratio (c) Total fixed changes coverage ratio (d) Cash flow coverage ratios (e) Debt services coverage ratios etc.

Profitability ratio is related to profit of the business. Profit is essential for the survival of the business. So it is regarded as the engine that drives the business and indicates economic progress. Profitability ratios are calculated to measure the overall efficiency of the business. The management of the firm is naturally eager to measure its operating efficiency. Similarly the owners invest their funds in the expectation of reasonable return. The operating efficiency of a firm and its ability to ensure adequate return to its shareholders depends ultimately on the profit earned by it. In fact the profitability ratios are designed to provide answers to questions such as: (i) Is the profit earned by the firm adequate? (ii) What rate of return does it represent? (iii) What is the rate of profit for various divisions and segments of the firm, (iv) What is the earning per share? (v) What was the amount paid in dividends? (vi) What is the rate of return to equity holders? and so on. Therefore the profitability ratios are calculated to enlighten the end results of business activities, which is the sole criterion of the overall efficiency of the business concern. Profitability ratio can be determined on the basis of either sales

or investments. The profitability ratios in relation to sales are: (a) Profit margin (gross and net), (b) Expenses ratio and in relation to investment is measured by (a) Return on assets (b) Return on capital employed and (c) Return on shareholder's equity etc.

Activity ratios are concerned with measuring the efficiency in assets management. These ratios are also called efficiency performance or assets utilization ratios. The efficiency with which the assets are used would be reflected in the speed and rapidity with which assets are converted into sales.

Turnover is the primary mode for measuring the extent of efficient employment of assets by relating the assets to sales. The greater rate of turnover or conversion, the more efficient is the utilization/management, other things being equal. Activity ratios are very important for a concern to judge how well facilities at the disposal of the concern are being used or to measure the effectiveness with which a concern uses its resources at its disposal. Some of the important activities ratios are (i) Capital turnover ratio (ii) Fixed assets turnover ratio (iii) Working capital turnover ratio (iv) Debtor turnover ratio (v) Creditor turnover ratio (vi) Stock turnover ratio (vii) Total assets turnover ratio.

It is mostly noted that the activities ratio (ratios relating to sales) are basically applicable to manufacturing organization i.e. it is not applicable to service organization like banking sector.

The most applicable ratios for financial analysis of a banking organization are given below. (*Joshi; 2058:108*)

Ratios from profit & loss Account

- 1) Total operating income to total assets
- 2) Total operating expenses to total assets
- 3) Net operating income to total assets
- 4) Return on assets
- 5) Total operating exps. to total operating income
- 6) Net income to total operating income
- 7) Interest of deposit to total exps.
- 8) Interest of borrowing to total exps.
- 9) Interest income on loan to total income

Ratios from Balance sheet

1. Current Ratios
2. Debt equity ratios
3. Fixed assets ratio
4. shareholder's equity to total assets
5. Return on assets.

A banker is interested to know the following efficiency aspect of the borrower's business.

- a) Efficiency in operational management
- b) Efficiency in Financial management
- c) Efficiency of debt service management

Usefulness of Ratio analysis

Ratios are exceptionally useful tools with which over can infer the financial performance of the enterprise over a period of time, with the help of ratio analysis conclusions can be drawn regarding several aspects such as financial health, profitability and operational efficiency of the undertaking. It facilitates the management to know whether the firm's financial position is improving or deteriorating or it is constant over the years by setting a trend with the help of ratios. Further, the ratio analysis plays a very important role in the interpretation of the financial statement correctly and to make the figures comparable and more meaningful. Following are the important uses of ratio analysis. (*Munakarmi; 2002:485*)

1. Ratio analysis simplifies the financial statements. It tells the whole story of changes in financial condition of the business.
2. Ratio analysis provides data for inter-firm comparisons. It highlights the factors in relation to success or failure of activities.
3. Ratio analysis helps in planning and forecasting. Ratio can assist management in its basic functions of forecasting, planning, coordinative, control and communications.
4. Ratio analysis may be used as measure of efficiency for inter-firm and intra-firm comparisons.
5. Ratio acts as an index of the efficiency of the enterprise. They serve as an instrument of management control.

6. Ratios analysis is an effective instrument which, when properly used, is useful to assess important characteristics of business like liquidity, solvency, profitability etc.

Limitation of Ratio analysis

In deed, ratios are only the means to reach conclusions and not conclusions in themselves. They are clues, not bases, for immediate conclusions. The specific limitations of ratio analysis are:-

1. Ratios are simply means and not end.
2. Ratios are tools of quantitative analysis only and it ignores the qualitative analysis. Which is most needed factor to draw conclusions?
3. Price level changes and current economic conditions are ignored.
4. Ratio may be linked to railroads; they tell the analyst to "stop, look and listen."
5. Unless adequate details of accounts are given specially in relation to consistent application of generally accepted accounting principles, the ratios obtained cannot be relied upon.
6. Ratios do not make decisions. They do not purport precise problem nor indicate causes. They may aid in decision making by highlighting areas which are problems or which require further investigation.
7. Ratios are more useful than absolute amount because the claim that 'figures speak for themselves' is often quite unjustified. It may be necessary to translate them into a language understandable to other or so as to arrange them that they speak more loudly. The object of ratios is to measure facts and probabilities so as to draw out their inner meaning, which is not evident from absolute accounts alone.
8. All types of ratios are not applicable to analyze the all type of organization.
9. It is a guide rather than solution to present the problems and future plans.

10. Plan is not an exact indicator of future. A particular ratio is not a sure indicator of bad or good management etc.

2.3 Review of related study

Review or related study is also important part of the study. In this section, an attempt is made to present review of related study on the basis of several past studies.

In the researcher's knowledge, there are many research studies related to financial performance analysis of different financial institution/bank. But a few researchers have been made about the financial performance analysis of Agricultural Development Bank, Nepal. Therefore the literature relating to this study was received and views expressed by the various researchers have been presented in this section.

(a)Mr. Rajib Raj Joshi (2001) reports on the financial performance of Nepal Arab Bank Limited (NABIL) and Nepal Grindlays Bank Limited (NGBL) in the following words. (*Joshi; 2001:69*)

1. The liquidity analysis reveals that overall liquidity position of NABIL is better than that of NGBL.
2. The activity ratio analysis reveals that NGBL is more efficient than NABIL in managing and utilizing its resources.
3. The overall profitability of NGBL is better than that of NABIL because it pays less interest to its depositors than it earns interest on deposits.
4. The average price-earning ratio of NABIL is higher which reveals that NABIL was higher market price per share over earning per share and the investor will prefer to invest in stock (shares) of NABIL because they will recover their investment quickly.
5. The stock of NABIL is highly priced than that of NGBL since it has higher book value per share.

6. Average dividend payout ratio indicates that NGBL pays more dividend to its shareholders than NABIL where as NABIL retains more earning.

(b) An another research conducted by Mr. Prem Bahadur Mungmen, on the topic of financial performance of Purwanchal Grameen Bikash Bank Ltd. pointed out the following results and findings. (*Mungmen; 2004:112*) Borrowing is the main source of fund. Although the main resources of fund are used in loan disbursement, it is used for the recovery of losses.

1. Financial ratio indicates poor financial position over the period of 2051 to 2059 B.S.
2. Trend of operating expenses is increasing day by day in comparisons with operating profit.
3. The growth of net loss is negative. It is the sign of gradually improvement in financial performance.
4. Loan has not been timely recovered from clients.
5. The relationship between deposit and investment is not in acceptable condition.
6. Overdue loan has increased year to year.
7. Share capital remains same during the study periods.
8. Loan disbursement by the bank quite small in amount, it is not practicable to go legal action against the defaulters.
9. The PGBBL is going to break even level in the next coming year. Its activities are also expanding day to day.

(c) Similarly a research study carried out by Dipak babu mainly, about comparative financial performance to Nepal Bangladesh Bank (NBB) and Bank of Kathmandu (BOK) limited carried out following conclusion. (*Mainly; 2001:96*)

1. NBB is more consistent in maintaining over all liquidity than BOK Ltd.
2. The capacity of providing long-term loan and advance is greater in NBB.
3. Return on net worth of NBB is significantly higher than BOK Ltd.

(d) An another research carried out by Mr. Bhab Nath Ghimire about financial performance on Nepal insurance company limited concluded as follows. (*Ghimire; 2002:87*)

1. The current assets are sufficient.
2. Co. has only ownership capital i.e. no creditor ship capital has been used.
3. Its net worth is slightly poor.
4. The profitability position is satisfactory to some extent any because the company has not earned sufficient profit from it's underwriting function.

(e) Similarly, another researcher Mr. Yadav Pd. Pokharel has measured the financial performance of Agricultural Development Bank Nepal from F.Y. 2041 to 2052 B.S. On his research work about 'Financial performance of Agricultural Development Bank Nepal major tools for measuring it's performance were funds flow analysis, ratio and trend analysis. The major findings were: (*Pokharel; 1998:73-79*)

1. The funds flow analysis shows the precaution care of fund in the bank for future growth of the bank.
2. The liquidity position of the bank over the 11 years for 2041 to 2052 B.S. is quite poor.
3. The debt equity ratio is unbalanced since the rising tendency of the ratio is the due to rapid yearly increase in borrowing but equity is increasing very slowly.
4. The over due loan and interest receivable amount are increasing every year.
5. Over all profitability position of the bank over 11 years from fy 2041 to 2052 B.S. is very weak. The bank has been facing the problem of loss during the periods.
6. Total trend analysis of loan activities of the bank shows the mixed result. Every year loan disbursement, collection, interest collection have been

increased but on the other side overdue and interest receivable have also been increasing which shows the inactive position on of ADBN.

2.4 Uses of Analytical Tolls:

The performance measurement of business is more difficult and complex. With regard to the financial performance of firm depend on effectiveness is capital management, efficiency and profitability in operation, risk and uncertainty in competition etc. The collected data are analyzed by using various financial tools, out of these are given and defined below:

(1)Financial Tools:

- (i) Funds flow analysis
- (ii) Ratios analysis

(2)Statistical Tools:

- (i) Trend percentage analysis
- (ii) Trend least square method analysis
- (iii) Simple correlation analysis (coefficient of determinants)

2.4.1 I Funds flow analysis:

A statement of sources as the funds flow statement. It is technical device designed to highlight the changes in the financial position of the business enterprises. The funds are detected from five years Balance sheet from FY 2064/65 B.S. to 2068/69 B.S. for the purpose of funds flow analysis.

- a. Sources of fund: During the study periods of FY 2064/65 B.S. to 2068/69 B.S. fourteen different sources of fund have been available in different years of FORWARD. They are:
1. Increase in capital
 2. Increase in reserves & fund
 3. Operating income/profit
 4. Increase in borrowing
 5. Increase in deposits

6. Increase in other liabilities and provisions
 7. Increase in fixed assets
 8. Decrease in investment
 9. Decrease in interest receivable
 10. Decrease in account receivable
 11. Decrease in other assets
 12. Decrease in cash and bank balance
 13. Plan Nepal & RMDC subsidy
 14. Total uses of fund
- b. Application of fund: During the fiscal year 2064/65 to 2068/69 B.S. total sources of funds of FORWARD have been applied in twelve different uses, They are:
1. Increase in cash and bank balance
 2. Increase in investment
 3. Increase in loan outstanding
 4. Increase in interest receivable
 5. Increase in account receivable
 6. Increase in other assets
 7. Increase in fixed assets
 8. Increase in reserves
 9. Decrease in borrowing
 10. Decrease in other liabilities and provisions
 11. Operating loss
 12. Total uses of fund

2.4.1. II Ratio Analysis

An arithmetical relationship between two figures is known as ratio. The ratio is used as an idea or yards stick for evaluating the financial position and performance of a firm. "A ratio helps to the researcher to make qualitative judgment about the firm's financial position and performance." Various tools are used to analysis the performance of the firm. Among the available various

financial tools and techniques ratio analysis is a powerful tools and techniques are created from the figures of different account consisting in balance sheet and income statement. It can be grouped into following classification.

- a) Liquidity Ratio
- b) Leverage Ratio
- c) Activity Ratio
- d) Profitability Ratio

2.4.1.II (a) Liquidity Ratio:-

The ability of a firm to meet its obligation in the short term is known as liquidity. On other words, Liquidity ratios measure the firm's ability to meet current obligations. These examine the adequacy of funds. The solvency of the firms ability to pay its obligation when due. If a firm has sufficient net working capital deemed to have sufficient liquidity. There are four reasons in order to measure the liquidity position of FORWARD the following are considered.

- i. Current ratio
- ii. Working capital to current assets ratio
- iii. Cash and bank balance to total deposits ratio
- iv. Cash and bank balance to current assets ratio

2.4.1. II.a.i Current Ratio

The current ratio is a ratio of the firm's total current assets to its total current liabilities. A low ratio is an indicator that a firm may not be able to pay its future bills on time, particularly if conditions change, causing a slowdown in cash collections. A high ratio may indicate an excessive amount of current assets and management's failure to utilize the firm's resources properly. It is calculated by the following way.

$$\text{Correct ratio} = \frac{\text{Currect ratio}}{\text{Currect Laibailities}}$$

2.4.1. II.a.ii Working capital to current assets ratio:

It shows the portion of the working capital on the assets. This ratio is calculated in percentage, in mathematically, it can be written as follows:

$$\text{Working capital to current} = \frac{\text{Working capital}}{\text{Current asset}} \times 100\%$$

2.4.1.II.a.iii Cash and bank balance to total deposit ratio:

This ratio shows the ability of banks immediate funds to cover their deposit. Dividing cash and bank balance it is calculated it by total deposits. The ratio can be expressed as:

$$\text{Cash and bank balance to total deposit ratio} = \frac{\text{Cash and bank balance}}{\text{Total deposit}} \times 100\%$$

2.4.1.II.a.iv. Cash and bank balance to current assets ratio:

The cash and bank balance to current assets ratio is also one measure of liquidity. It is the most liquid form of the current assets. It shows the percentage of readily available fund within the banks. Dividing the cash and bank balance by the current assets can derive it. This can be done by the following expression:

$$\text{Cash and bank balance to current asset ratio} = \frac{\text{Cash and bank balance}}{\text{Current assets}} \times 100\%$$

2.4.1. II.b. Leverage Ratio:

Leverage ratios show the proportions of debt and equity in financing the firm's assets. The short-term creditors, like debentures holders, financial institutions etc, are more concerned with the firm's long-term financial strength. In fact a firm should have a strong short as well as long-term financial position. To judge the long-term financial position of the firm financial leverage or capital structure, ratios are calculated; these ratios indicate mix of funds provided by owners and lenders. As a general rule, there should be an appropriate mix of debt and owner's equity in financing the firm's assets.

The manner in which assets are financed has a number of implications. First between debt and equity: debt is more risky firm's point of view. The firm has a legal obligation to pay interest to debt holders, irrespective of the profits made or losses incurred by the firm. If the firms fail to pay to debt holders in time, they can take legal action against to get payments and in extreme cases, can force the firm into liquidation. Second, employment of debt is advantageous for shareholders in two ways (a) They can return control of the firm with a limited stake and (b) Their earning will be magnified, when the firm earns a rate of return on the total capital employed higher than the interest rate in the borrowed funds. The process of magnifying the shareholders return through the employment of debt is called financial leverage or trading on equity. However leverage can work in opposite direction as well, if the cost of debt is higher than the firm's overall rate of return, the earning of shareholders will be reduced. In addition, there is threat of insolvency. Third, a highly debt-burdened firm will find difficult in raising funds from creditors and owners in future. Creditors treat the owners/equity as a margin safety; if equity base is thin; the creditors risk will be high. Thus Leverage ratios are calculated to measure the financial risk and the firm's ability of using debt to shareholders advantage.

In short cut, leverage refers to the ratio of debt to equity in the capital structure of the firm. Leverage ratio gives the important information interested creditors, investors, moneylenders, social investigators. The different leverage ratios are maintained to measure the financial risk and the firm ability of using debt for the benefits of the shareholders. These ratios are used to measure the proportion of outsider's fund and owner's capital used by the firm. The following ratios are estimated in order to evaluate the capital structure of the FORWARD to the desired objectives.

- i. Debt-equity Ratio
- ii. Debt-assets Ratio

- iii. Debt to capital Ratio
- iv. Net fixed assets to equity Ratio
- v. Interest coverage Ratio
- vi. Current asset to equity

2.4.1. II.b.i Debt-Equity Ratio

This ratio has been calculated to measure the relative proportions of outsider's fund and shareholders fund invested in the firm. This ratio shows a favorable or unfavorable financial position of the concern depending upon the nature of institutions. Debt and equity have their own identical features. More debt in capital structure also produces higher financial risk because it has fixed claim and fixed maturity. But in contrast, equity capital is more flexible and residual claim on the earnings of the firm.

The difference between equity and refers to margin of safety, which is crucial to the lenders in providing loans. The ratio can be computed as below

$$\text{Debt-Equity ratio} = \frac{\text{Total debts}}{\text{Share holders equity}}$$

2.4.1. II.b.ii Debt-Assets Ratio

It measures the contribution of creditors to own the assets of the company. This ratio is computed by applying the following formula.

$$\text{Debt to asset ratio} = \frac{\text{Total debts}}{\text{Total assets}} \times 100\%$$

2.4.1.II.b.iii Debt to Total Capital Ratio

It is relationship between long-term debt and total capital. Total capital includes owner's equity as well as borrowed capital. A high ratio shows the large share of financing by the borrower as compare to that of total capital. Creditors

would suffer here in times of distress than the owner. That is why creditors prefer low debt capital ratio. It is calculated in following way.

$$\text{Debt to Total Capital Ratio} = \frac{\text{Total debts}}{\text{Total capital}} \times 100\%$$

2.4.1.II.b.iv Net Fixed Assets to Equity

This ratio shows how much of shareholder's fund is being invested in fixed assets. It is calculated by using the formula.

$$\text{Fixed assets to equity ratio} = \frac{\text{Total Net Fixed Assets}}{\text{Shareholders Equity}} \times 100\%$$

2.4.1.II.b.v Interest Coverage Ratio

It reveals the ability for payment of interest on borrowed capital. This ratio measures the debt servicing capacity of a firm. It is computed by dividing net profit before interest and tax by interest. A high ratio is sign of low burden of borrowing of the business and lower utilization of borrowing capacity. From the point of the view of the creditors, the larger the coverage, the greater the ability of the firm is to make the payment of interest to creditor mathematically.

$$\text{Interest coverage ratio} = \frac{\text{NIBT} + \text{Interest}}{\text{Interest}}$$

2.4.1.II.b.vi Current Assets to Equity Ratio

It ratios reveals that how much of shareholders fund is being deployed in current assets. If the deployment is too small, working capital may be inadequate.

$$\text{Current assets to equity ratio} = \frac{\text{Total current assets}}{\text{Shareholders equity}}$$

2.4.1. II.c Activity ratios:

Activity ratios reflect the firm's efficiency in utilization its assets and profitability ratios measure overall performance and effective of the firm. This

ratio is called efficiency or turnover ratio. This ratio measures the degree of effectiveness in use of funds by enterprise. Out of several activity ratios the following ratios are calculated for the financial performance of the FORWARD.

- i. Loans outstanding to collection ratio.
- ii. Loans collection to disbursement ratio
- iii. Loans outstanding to disbursement ratio.
- iv. Loans outstanding to equity ratio
- v. Administrative expenses to loans outstanding ratio
- vi. Investment to total deposit ratio
- vii. Over due loan ratio
- viii. Loans collection rate ratio

2.4.1. II.c.i. Loans outstanding to collection ratio

It shows the relationship between loans outstanding and collection. It shows the efficiency of a financial activities institution in realization of the loans disbursed by it. It is expressed in mathematically:

$$\text{Loans outstanding to collection ratio} = \frac{\text{Loans outstanding}}{\text{Loans collected}} \times 100\%$$

2.4.1.II.c.i. Loans collection to disbursement ratio

It indicates that how efficiency has been gain from loan disbursement. This ratio is calculated by using following formula:

$$\text{Loans collection of disbursement ratio} = \frac{\text{Loans collected}}{\text{Loan disbursement}} \times 100\%$$

2.4.1.II.c.iii Loans outstanding to disbursement ratio

It measures what percentage of loans outstanding has remained yet in clients. It shows the effectiveness and efficiency to operate loans disbursement activities. Higher ratio is not good for the Bank. It is computed by the following way.

$$\text{Loans outstanding to disbursement ratio} = \frac{\text{Loans outstanding}}{\text{Loan disbursement}} \times 100\%$$

2.4.1.II.c.iv. Loans outstanding to equity ratio

It shows the relationship between loans outstanding and equity ratio. It is calculated by dividing loans outstanding by equity ratio.

$$\text{Loans outstanding to equity ratio} = \frac{\text{Loans outstanding}}{\text{Equity ratio}} \times 100\%$$

2.4.1.II.c.v. Administrative expenses to loan outstanding ratio

It shows the relationship between administrative expenses to loan outstanding. It is computed by dividing administrative expenses by loans outstanding.

$$\text{Administrative expenses to loans outstanding} = \frac{\text{Administrative ex.}}{\text{Loans outstanding}} \times 100\%$$

2.4.1.II.c.vi Investment to total deposit ratio

It reveals that how portion of the deposit is invested in investment. The bank collects the deposit from the clients by paying the fixed rate of interest. It invests the deposit for buying shares and investment in other profitable sectors. If the bank can be increase in the investment proper sectors, it earns profit, which is used for the payment of the interest on deposits. When the bank has a higher ratio of its then it shows the effectiveness and efficiency its activities. It is calculated by dividing the investment by the total deposit ratio. Mathematically:

$$\text{Investment to total deposit ratio} = \frac{\text{Investment}}{\text{Total deposit ratio}} \times 100\%$$

2.4.1.II.c.vii Loans outstanding to total deposit ratio

This ratio reveals what portion of deposit has been carried by the loan outstanding. This ratio is computed by dividing loans outstanding by total deposit ratio. Mathematically.

$$\text{Loan outstanding to total deposit ratio} = \frac{\text{Loans outstanding}}{\text{Total deposit}} \times 100\%$$

2.4.1.II.c.viii Over due loans ratio

This ratio shows what percentage of the over due loan are on loan outstanding. It is computed by using the following formula:

$$\text{Over due loans ratio} = \frac{\text{Over due loans}}{\text{Loans outstanding}} \times 100\%$$

2.4.1.II.c.ix Loans collection rate ratio

This ratio measures the efficiency of the financial institution. It is calculated by the following formula:

$$\text{Loan collection ratio} = \frac{\text{Total loans collection}}{\text{Total collection of loan+overdue+Interest receivable}}$$

2.4.1. II.d. Profitability Ratio:

Profitability ratios indicate the overall efficiency of the business concerns. A company should earn profits to survive and grow over a long period of time profit are essential, but it would be wrong to assume that every action initiated by management of a company should be aimed at maximizing profits, irrespective of social consequences. It is unfortunate that the word profit it looked upon as a term of abuse since some firms always want to maximize profits at the cost of employees, customers and society. Except such infrequent cases, it is a fact that the sufficient profit must be earned to sustain the operations of the business to be able to obtain funds from investors for expansion and growth and to contribute towards the social overheads for the welfare of the society.

Profit is the difference between revenues and expenses over a period of time. Profit is the ultimate output of a company and it will have no future if it fails to make sufficient profits. Therefore financial manager should continuously evaluate the efficiency of its company in term of profits the profitability ratios are calculated to measure the operating efficiency of the company. Besides management of the firm or company, creditors and owners are also interested in

the profitability of the firm. Creditors want to get interest and repayment of principle regularly. Owners want to get a reasonable return on their investment. This possible only when the company earns enough profits.

Generally, profitability position of FORWARD is evaluated on the basis of following ratio analysis.

- i. Net profit to total assets ratio
- ii. Net profit to total deposit ratio
- iii. Operating ratio
- iv. Interest earned to total assets ratio
- v. Return on equity ratio

2.4.1.II.d.i. Net profit to total assets ratio

This ratio indicates whether the total asset of the business has been properly used or not. It helps also to measure the profitability of a firm. It is expressed symbolically as follows:

$$\text{Net profit asset ratio} = \frac{\text{Net profit}}{\text{Total assets}} \times 100\%$$

2.4.1.II.d.ii. Net profit to total deposit ratio

Deposits are mobilized for investment. Loans and advances to the public in generating revenue. This ratio measures the percentage of profit earned from the utilization of the total deposits. It is calculated as follows:

$$\text{Net profit to total deposit ratio} = \frac{\text{Net profit}}{\text{Total deposits}} \times 100\%$$

2.4.1.II.d.iii Operating ratio

This ratio shows the changes in the net profit margin. It is calculated by dividing operating expenses by operating revenue.

$$\text{Operating Ratio} = \frac{\text{Operating expenses}}{\text{Operating revenue}} \times 100\%$$

2.4.1.II.d.iv. Interest earned to total assets ratio

It is calculated to find out the percentage of interest earned by the total assets of the firm. The following formula is employed for this purpose.

$$\text{Interest earned to total assets ratio} = \frac{\text{Interest earned}}{\text{Total assets}} \times 100\%$$

2.4.1.II.d.v. Return on equity ratio

It reveals the earning power on shareholders' book investment i.e. net worth. It is computed by dividing net profit after tax by net worth.

$$\text{Return on equity} = \frac{\text{Net profit after tax}}{\text{Net worth}} \times 100\%$$

2.4.2.I. Trend Percentage Analysis:

It shows the financial performance trend. It is calculated by using selected as the base year and is set to 100%. All other years are represented as a percentage of the base year. An index number can be calculated by the following formula for trend analysis

$$\text{Index percentage} = \frac{\text{Index yearly amount}}{\text{Base year amount}} \times 100\%$$

The general tendency of the time series data to increase during a long period of time is called trend. Trend analysis indicates the direction change. It is always desirable to express

the trend on absolute terms as well as relative terms. The index percentage can be plotted on a graph in various ways to facilitate the study of trends in a firm.

2.4.2.II. Simple correlation analysis (coefficient of determinant)

Correlation analysis reveals the degree of relationship between two or more than two variables. Relationship between two variables is called simple correlation and can be positive or negative.

Coefficient of correlation is calculated when it is believed that there is a cause and effect relationship. One of the variables will be the causal variable and another will be the effect. When there is a change in the causal variable, there will be a corresponding change in the dependent variable.

Degree of correlation or coefficient of correlation will lie in between 0 to +1. When the value is nearer to one, the relationship is strong. Similarly, when the coefficient of correlation is nearer to '0', the relationship is weak and hence a cause and effect relationship doesn't exist.

In statistical analysis, instead of using the coefficient of correlation 'r', there is a tendency of using the coefficient of determination. It is very simple when $r^2 = 0.9$, then the coefficient of determination is $(0.9)^2 = 0.81$. It means 81% change in the dependent variable is explained by a change in the independent variable. The remaining 19% change is unexplained. It means the change is caused by other variables not included in the model. Researchers must calculate to find out the 'r' as follows:

$$R_{xy} \text{ (coefficient correlation)} = \frac{\sum xy - \frac{\sum x \cdot \sum y}{N}}{\sqrt{\sum x^2 - \frac{(\sum x)^2}{N}} \sqrt{\sum y^2 - \frac{(\sum y)^2}{N}}}$$

Where $x = X - \bar{X}$ $Y = Y - \bar{Y}$

$$\text{Or } R = \frac{\sum xy - \frac{\sum x \cdot \sum y}{N}}{\sqrt{\sum x^2 - \frac{(\sum x)^2}{N}} \sqrt{\sum y^2 - \frac{(\sum y)^2}{N}}}$$

The above formula is called Karl Pearson's correlation coefficient, which is one of the widely used mathematical methods of calculating the correlation coefficient between two variables.

CHAPTER – THREE

RESEARCH METHODOLOGY

3.1 Introduction:

The main target of the research is to explain the financial performance of FORWARD to judge its performance FY 2064-65 to 2068-69 BS. Research methodology is the process by which the objectives of the study can be derived. It provides the instruction regarding the methods and process associated with the overall study of financial performance.

The term ‘research’ is meant any inquiry or investigation regarding any phenomena or event in order to discover facts. “A scientific is systematic, controlled, empirical and critical investigation of hypothetical propositions about the presumed relations among natural phenomena.”⁴⁷ A research has specified its procedures and some it’s essential characteristics. It is a process of investigation, which involves a series of well throughout activity of gathering, recording, analyzing and interpreting the data with the purpose of finding to the problem.

In fact, research may involve a scientific study or experimentation, and result in discovery or investigation, which would aid either scientific development or decision making. It may be concern with general abstract or concrete subjects. The research that involves scientific analysis would result in the formation of new theories, the discovery of new techniques, a modification of old concepts or a knocking -off an existing theory, concept or techniques. Thus, “research is the manipulation of things, concepts or symbols for the purpose of generalizing to extend, correct or verify knowledge, whether that knowledge aids in construction of theory or in the practice of an art.”⁴⁸

Research is the original construction to the existing stock of knowledge making for its advancement. It is the pursuit of truth with the help of the study

observation, comparisons and experiment. “Research is careful investigation or inquiry especially through search for new facts in any branch of knowledge.”⁴⁹

Research is not only to solve the problem but also it will build some ideas of knowledge, thus it is as knowledge building process. The main purpose of research is to discover answer to questions through the application of scientific procedures. The aim of research is to find the truth which is hidden and which has not been discovered as yet. Therefore, “research is a systematized effort to gain new knowledge.”⁵⁰

The research methodology may be defined as a science of studying how research is done scientifically. It tells about various steps that are generally adopted by a research in studying his research problem along with the logic behind him. “Methodology is a way to systematically solve the research problem.”⁵¹ Research methodology has many dimensions and research methods do consists a part of the research methodology. Thus, the scope of research methodology is wider than that of research methods. In fact, research methodology refers to all those technique/methods that are used for conclusion of research. It refers to the methods/technique the researcher use in performing research operation. Thus, all those methods, which are used by the researcher during the course of studying his research problems terms as research methods.

Methodology is the development phase of research methods. By research methodology, we mean design research logic behind application of tools and technique. In deed, Research methodology tries to give the answer of the following questions.

1. Why the research study has been undertaken?
2. How the research problems have been defined?
3. In what way and why the hypothesis has been formulated?
4. What data have been collected?
5. What particular technique of analyzing data has been adopted?

From the above description, the procedure by which research goes about their work of describing and explaining the phenomena are called research methodology. The rationale behind his study is to analyze and interpret the financial performance of Agricultural Development Bank, Nepal during the period of 5 years from 2064/65 B.S. to 2068/69 B.S.

3.2 Research Design:

It is devising the plan for the research. It describes the general framework for collecting, analysis and evaluating data after identify: (i) what the researcher wants to know and (ii) what has to be dealt with in order to obtain required information.

The basic aim of this study is to evaluate the situation and to provide constructive suggestions for better mobilization and utilization sources and resources and other aspect of financial management of FORWARD. Evaluation has been done on the basis of profit and loss A/C and balance sheet by using financial tools and statistical tools.

Research design refers to the framework of the study. It is the blue print for any kinds of studies. "Research design is the arrangement of condition and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure."⁵² In fact the research design is the conceptual structure within which research is conducted; it constitutes the blueprint for the collection, measurements and analysis of data. The research design tries to the answer of the following questions.⁵³

1. What is the study about?
2. Why is the study made?
3. Where will the study be carried out?
4. What type of data is required?
5. Where can the required data be found?
6. What will be the sample design?

7. What techniques of data collection will be used?
8. How will the data be analyzed?
9. In what style will the report be prepared?

The basic aim of this study is to examine and assess the financial performance of FORWARD through the collection, evaluation, verification and analysis of data systematically for the improvement and exploration of certain facts. Evaluation has been done on the basis of its five years performance from 2064/65 B.S. to 2068/69 B.S. To measure its performance, income statement, balance sheet, cash flow statement is primarily required. The statements have been obtained from the 5 years annual audit report of FORWARD. Most of the relevant information's have been taken from the web site of Nepal Rastra Bank, annual report of FORWARD, census bureau of statistics etc. This study totally depends upon the secondary data.

The obtained data, at first, arranged and classified so that it is easy to analyze. The data have been analyzed using various tools and techniques such as common-size statement, relevant ratio, cash flow analysis, and trend analysis as well as statistical tools such as means, standard deviation, correlation analysis etc. These tools help to display the clear financial performance of the FORWARD. This study represents historical and exploratory as well as descriptive.

In this study, ratio analysis is the process of determining and interpreting numerical relationships based on financial statements. Cash flow analysis is a more informative tool regarding a bank's cash flows (inflows & outflows) from its operating, investing and financing activities. Similarly, trend analysis makes it easy to understand the change in old items on the group of items over a period of time. The correlation analysis shows the relationship between certain variables. To draw the conclusion regarding the data, the common-size statement shows the percentage change as increase and decrease in amount of statements over a period

of time. So the structure of research has been designed to obtain the objectives, which are mentioned in this study.

3.3 Nature and sources of data:

This study is based upon the secondary data published in the form of annual report about profit & loss A/C, balance sheet and concerned notes of FORWARD for five years from FY 2064/65 BS to 2068/69 BS.

3.4. Population and sample of the study:

The population of the study is the totality of all observations that have been selected for the study. Thus, in the case of FORWARD if the researcher studies the past whole life of FORWARD is called population study. It is quite difficult to analysis all the data of population. So the sample has been selected for the study, which starts from FY 2064/65 BS to 2068/69 BS.

The term 'population pr universe' for research means all the members of any well defined class of the people, events or objects. The study of 'population or universe' is difficult matter in all kinds of research. But also it is must necessary to study all the population in same kind of research. Thus population, in must studies, usually consists of a large group of people. Because of its large size it is fairly difficult to collect detailed information from each member of population. For this, a sub group of member is chosen which is believed to be representative of the population and this sub groups called sample and the process of selection of such sub group is called sampling. Good sampling techniques or methods can save the researcher's time and money.

There are so many statements, which help to indicate the financial strength and firm's conditions. Not only numerical data but also show abstract phenomena are used to analyze the financial position. It is very difficult to study such all statements and abstracts phenomena. Besides this there are many tools and

techniques to analyze the bank's financial performance. Thus, this study is made by using judgmental or purposive sampling. Only the required statements like income statement, balance sheet and cash flow statements have been taken for analyzing financial performance of the selected micro finance bank or institutions (FORWARD). Only recent past five year such statements have been collected and used for analyzing bank's financial performance. Similarly, some of the popular and well accepted tools and techniques have been used to analyze and interpret the financial condition and performance of bank, i.e. comparative financial analysis, common-size statements, funds flow and cash flow analysis, trend analysis, ratio analysis, correlation analysis etc. It has been fully tried to avoid the possible sampling error in this study so that the required objective can be achieved.

3.5 Sources of data:

The collection of data is considered as an integral part of research activity. The sources of information are generally classified primary and secondary. Data collected by the researcher or through agent for the first time from related field and possessing original character are known as primary source. On the other hand, data collected by some one else, used already and are made available to others in the form of published statistics are known as secondary data. Once primary data have been used, it loses it's primary characteristics (originality) and becomes secondary.

This study basically depends upon the secondary data. The major secondary sources of data, for this study, are the annual reports published by the FORWARD. Some of the journals, economic survey reports, and banking news have been taken into consideration for this study. Along with above, staffs of the agricultural development bank are the primary source of information.

3.6 Data collection procedures:

This study is basically depends upon the secondary sources of data. The annual audit reports and monthly journals published by the FORWARD publication of Nepal Rastra Bank, Economic survey reports are taken as the secondary sources of data. Some of the related information has been taken through the web site of related organization.

Although, while collecting data from secondary sources, there exist less problem in comparison to the collection of data from primary sources since the secondary data have been collected under a given set of definition of various term and units used. However, before using secondary data for statistical investigation under study, it must be subjected to careful editing and scrutiny with respect of their reliability, suitability and adequacy. Therefore "in order to arrive at best conclusion free from limitation and inadequacies, the published data i.e. the secondary data must be subjected to through scrutiny and editing before it accepted for use."⁵⁴

Thus the applicability of secondary data for this analysis has been tested in the following manner.

- ❖ Test of reliability
- ❖ Test of suitability
- ❖ Test of adequacy

The necessary data has been collected from more reliable sources. Annual report published by FORWARD is the main source of the secondary data for this analysis. While testing reliability of data, the following matters have been kept in mind.

- The reliability, integrity and experience of the selecting org.
- The reliability of source of information and
- The method used for the collection and analysis of data.

A mere reliable data may not sufficient for the purpose of the analysis/study. The available data must be suitable as per the objectives, nature and scope of the analysis/study. To analyze the financial performance of concern bank (FORWARD), some important financial statement like profit and loss account, profit and loss appropriation account, balance sheet and cash flow statements have been taken as a suitable data.

Even if the secondary data are reliable and suitable in terms of various aspect, it may not be adequate enough for the purpose of given study. To reach in the best conclusion, adequate data must be needed. In this study, past five years data (income statement, balance sheet) have been collected, arranged and tabulated for the analysis.

3.7 Data processing procedures:

The data collected from the above sources of the bank are classified, tabulated and analyzed. Financial ratios are basically used for interpretation.

3.8 Data analysis tools:

There are a number of tools and techniques can be used to analyze the bank's financial performance. All of the tools and techniques may not applicable at a time due to the nature, objectives, scope and availability of time and cost. Thus some of well accepted and important financial and statistical tools have been used to measure the financial performance of forum for rural women ardency development (FORWARD). These tools and techniques are as follows:-

Financial tools

1. Comparative and common-size financial statement
2. Ratio analysis
3. Net working capital analysis
4. Funds flow analysis
5. Cash flow analysis

Statistical tools

1. Trend percentage analysis
2. Mean
3. Standard deviation
4. Correlation analysis

The *comparative financial statement* is popular and well-accepted Tools for financial analysis which reflect the change in the financial data over a periodical and will best understand if the statements containing data for a period two or more years placed side by side in adjustment columns. Similarly the *common-size financial statements* indicate the relationship of various items with some items (expressed in percentage of common item). The percentage so calculated can be easily compared with the corresponding percentage in other periods meaningful conclusion can be drawn.

Ratio analysis, a well-accepted yardsticks financial analysis, is the analysis of numerical/quantitative relationship between two variable/items. With the help of ratio analysis conclusion can be drawn regarding several aspect such as financial health, profitability and operational efficiency of the undertaking. It plays a vital role in interpretation of the financial statement correctly and to make the figures comparable and more meaningful. Ratio analysis facilitate the management whether the firm's/bank's financial position is improving or deteriorating or it is constant over the year.

Net working capital analysis deals about the liquidity position of the firm/bank. The term net working capital refers to the current assets less current liabilities the magnitude of working capital is a measure of the safety margin that exists for protection of short term creditors. Thus working capital analysis helps to determine the optimal level of working capital for smooth running of the

organization/bank without any deficiencies. Similarly, *fund flow analysis* gives a clear picture of the various sources of fund and their application in various sectors.

Cash flow analysis deals with inflow and outflow of cash between two dates. It explains the changes in cash position between the periods. It shows the causes of changes in cash position of the two balance sheet data.

Statistical method/tools are the mathematical techniques used to facilitate the analysis and interpretation of numerical data secured from groups of individuals or groups of observation from single individual. The statistical analysis is one particular language, which describes the data in a simple way. By using statistical analysis it is possible to talk about the relations and differences of variables. "With the help of statistical analysis of data, the results can be presented in brief and precise language and complex and complicated problems can be studied in very simple way."⁵⁵ It becomes possible to convert abstract problems into figures and complex data in the forms of tables. Generally, a satisfactory statistical tools/unit should have four qualities which are: (1) Appropriateness (2) Clarity (3) Measurability (4) Comparability. The popular and well-accepted statistical tools are: average/mean, standard deviation, trend percentage analysis, co-efficient of variation, correlation analysis etc.

Mean/average is the measures, which condense a huge data in to a single value, which represent the entire data and generally located at the central part. "Mean/average is a single value that represents a group of single value."⁵⁶ Average is the typical values around which other items of the distribution congregate. They are the values which lie between the two extreme observations of distribution and give us an idea about the concentration of the values in the central part of observation. Measures of central tendency are also called measure of location since they enable us to locate the position or place of the distribution. "Average provides us the gist and a bird's eye of the huge mass of unwieldy numerical data."⁵⁷ There are five types of average commonly used in business statistics,

which are: (i) Arithmetic mean (ii) Median (iii) Mode (iv) Geometric-mean (v) Harmonic mean. Average is more helpful to:

1. Describe the distribution in concise manner
2. Facilitate comparison of various distribution
3. Establish relationship among variables
4. Take necessary decisions.

Among the different types of average, geometric mean has been primarily used in this study. Because it is used to find the average percent increase in variable like profit, expenses and other economic or business series. The application of geometric mean is the construction of index number, in averaging ratio, percentage, or rate if increase and decrease. In case of computing average rate of growth of population or rate of profit etc. geometric mean is most appropriate method to obtain average. Most of the economic activities are involved in the banking organization. So, geometric mean is more applicable in this study.

Standard deviation is the most popular and most useful measure of dispersion and gives uniform, correct and stable results. The chief characteristic of standard deviation is that it is based on mean, which gives uniform and dependable results. A standard deviation is always a positive number and is superior to other absolute measure of dispersion because it is used for further mathematical treatment. It is the positive square root of the average of the squared deviation of the observation from the arithmetic mean of distance of the observation from arithmetic mean of the distribution. "Standard deviation is the square root of the average of the square distance of the observation from the mean."⁵⁸ It is rigidly defined and base on all observations. The requiring of the deviation removes the drawback of ignoring the signs of deviation in comparisons of sampling. In this study, sample standard deviation has been used which is denoted by sign's' instead of sign.

The standard deviation measures the absolute dispersion or variability of a distribution. The greater the amount of dispersion or variability the greater the standard deviation, for the greater will be the magnitude of the deviation of the values from their mean. A small standard deviation means a high degree of uniformity of the observation as well as homogeneity of a series; a large standard deviation means just the opposite. Thus if we have two or more comparable series with identical or nearly identical means, it is the distribution with the smallest standard deviation that has the most representative mean. Hence standard deviation is extremely useful in judging the representative of mean.

Trend percentage analysis, as another statistical tool of financial analysis, reflects the changes in financial statements between the periods. These can be easily studied by establishing a base year and expressing other year in terms of the base year. The trend percentage can be also presented in the form of index numbers showing relative change in the financial data of certain period.

Correlation is the measure of relationship between two or more characteristics of a population or a sample. It is simply measure the changes between the phenomenon's. If two quantities vary in the related manner so that a movement an increase or decrease in one tend to accompanied by a movement in the same or opposite direction in the other they are called correlated. If the relationship is direct they are called positively correlated and if the relationship is inverse they are called negatively correlated. In fact "The correlation analysis refers to the techniques used in measuring the closeness of the relationship between the variables."⁵⁹ It is a statistical device which helps us in analyzing the co-variation two or more variables. Correlation analysis contributes to the understanding of economic behavior, aids in locating the critically important variables on which disturbances spread and suggest to him/her the paths through which establishing forces may become effect. The effect of correlation is to reduce the range of uncertainty of our prediction.

"The correlation is a statistical tool which studies the relationship between two variables and correlation analysis involves various methods and techniques used for studying and measuring the extent of the relationship between the two variables."⁶⁰ Two variables are said to be correlating if the change in variable results in a corresponding change in other variable. Correlation analysis enables us to have an idea about the degree and direction of the relationship between the two variables under study, correlation analysis is used in conjunction with regression analysis to measure how well the regression line explains the variation of dependent variables. Correlation can be used by itself, however, to measure the degree of association between two variables. Thus, "Correlation analysis is the statistical tool that we can use to describe the degree to which one variable is linearly related to another."⁶¹

The problem of analyzing the relation between different series should be broken down into three steps:

-) Determining whether a relation exists and, if it does measuring it.
-) Testing whether it is significant.
-) Establishing the cause and effect relation, if any

The significance of the correlation can be highlighted in the following points.

1. With the help of correlation analysis we can measure in one figure the degree of relationship existing between the variables.
2. Once we know that two variables are closely related, we can estimate the value of one variable given the value of another.
3. With the help of correlation some of the guess work can be removed from decisions when the relationship between a variable to be estimated and the one or more other variables on which it depends are close and reasonably invariant.

4. Progressive development in the methods of science and philosophy has been characterized by increase in the knowledge of relationship or correlations.
5. The effect of correlation is to reduce the range of uncertainty. The predication based on correlation analysis is likely to be moved variable and near to reality.

There are several types of correlation. But mostly/widely used correlation are (i) positive and negative (ii) simple, partial & multiple and (iii) linear and non-linear. Among them the linear correlation is popularly used to analysis the economic and financial activities. A mathematical method for measuring the intensity or the magnitude of linear relationship between two variable series was suggested by Karl Pearson (1867-1936), a great British Biometrician and statistician and is by the most widely used method in practice. It is popularly known as Pearson co-efficient of correlation and it is denoted by the symbol r . Simple r is a numerical measure of linear relationship between the variable, say x and y , and it is defined as the ratio of the covariance between x and y . written as $\text{cov}(x,y)$, to the product of the standard deviation of x and y , symbolically.

$$r = \frac{\text{Cov.}(x,y)}{\sigma_x \cdot \sigma_y}$$

Where, r =person's co-efficient of correlation

$\text{cov.}(x,y)$ = Co-variance between the variable x and y .

σ_x = standard deviation of variable x

σ_y = standard deviation of variable y

Interpretation of r

The coefficient of correlation measures the degree of relationship between two sets of figures. As the reliability of estimates depends upon the closeness of the relationship it is imperative that almost care be taken while interpreting the value

of coefficient of correlation other wise fallacious conclusions can be drawn. The full significance of r will only be grasped after working out a number of correlation problems and seeing the kinds of data that give rise to various value of r . The value of r exist between +1 & -1 i.e. $+1 \leq r \leq -1$. Following general rules are given which would help in interpreting.

1. $r = +1$ implies that there is perfect positive correlation between the variables.
2. If $r = -1$, there is perfect negative correlation between the variables.
3. If $r = 0$, the variables are uncorrelated. In each word, there is no linear relationship between the variables.
4. The closer r is to +1 or -1, the closer the relationship between the variables and the closer r is to 0, and the less close the relationship. The full interpretation of r depends upon circumstances, one of which is the size of the sample, when estimating the value of one variable from the value of another, the higher the value of r the better the estimate.
5. The closeness of the relationship is not proportional to r . If the value of r is 0.8, it does not indicate a relationship twice as close as of 0.4. It is, in fact, very much closer.

The significance of the correlation must be tested. The value of correlation has no meaning if it is not significant. The probable error of the coefficient of correlation helps in interpreting it's value. With the help of probable error, it is possible to determine the reliability of the value of the coefficient in so far depends on the conditions of random sampling. The probable error of the correlation coefficient is an amount, which if added to and subtracted from the mean

correlation coefficient, produces amounts within which the chances are even that a coefficient of correlation from a series selected as random will fall.

If r is the observed correlation coefficient is a sample of n pairs of observation then its standard error, usually denoted by S.E. (r) is given by:

$$\text{S.E. } (r) = \frac{1 - r^2}{\sqrt{n}}$$

Probable error of the correlation coefficient is given by:

$$\begin{aligned} \text{P.E. } (r) &= 0.6745 \times \text{S.E. } (r) \\ &= 0.6745 \times \frac{1 - r^2}{\sqrt{n}} \end{aligned}$$

P.E. (r) may be used to test if an observed value of sample correlation coefficient is significant of any correlation in the population. The following guide-lines may be used.

5. if $r < \text{P.E. } (r)$ i.e. if the observed value of r is less than its P.E. then correlation is not at all significant.
6. if $r > 6 \text{ P.E. } (r)$ i.e. if observed value of r is greater than 6 times its P.E. then r is definitely significant.

Coefficient of determination is a much more useful measure of the linear co-variation of two variables. One very convenient and useful way of interpreting the value of coefficient of correlation called coefficient of determination. A more useful and readily comprehensible measure is coefficient of determination, which gives the percentage variation in the dependent variable that is accounted for by independent variables. It gives the ratio of the explained variable to the total variable. The coefficient of determination is given by the square of the correlation coefficient i.e. r^2 . Thus the coefficient of determination,

$$r^2 = \frac{\text{Explained variance}}{\text{Total variance}}$$

If the value of $r = 0.90$, r^2 will be 0.81 and this would mean that 81% of the variation in the dependent variable has been explained by the independence variable. It is much easier to understand the meaning of r^2 than r and, therefore the coefficient of determination should be preferred in presenting the results of correlation analysis. It has been grossly over stated and is used entirely too much. It's square, the coefficient of determination, is a much more useful measure of the linear co variation of two variables. Thus the reader should develop the habit of squaring every correlation coefficient he finds cited or stated before coming to any conclusion about the extent of the linear relationship between the two correlated variables. Thus "The coefficient of determination is the primary way we can measure the extent or strength, of the association that exists between two variables, x and y ."⁶² Some times the correlation may not give the true result because it does not tell us anything about cause and effect relationship. The explanation of the significant degree of correlations may be any one, or a combination of the following reasons:-

1. The correlation may be due to pure chance, especially in a small sample.
2. Both the correlated variables may be influenced by one or more other variable.
3. Both the variables may be mutually influencing each other so that neither can be designated as the cause and the other the effect.

3.9 Limitation of methodology:

For every study certain methodology has been applied. Similarly for this study (financial performance analysis of FORWARD), some specific methodology has been adopted. Financial analysis is a complex topic, which can not be performed in a limit period and at a limit cost. Although financial analysis is only one key tool to analyze the firm's (bank's) financial performance and it's position, again, organization/firm with poor financial analysis could not make a better future planning for it's perpetual growth. Financial analysis is a kind of descriptive

research in which facts are accumulated, processed, analyzed and lastly recommended for better future performance.

This study is based on only past five years data i.e. 2064/65 BS to 2068/69 BS annual report of agricultural development bank has been taken as major sources of data. Only these audit report may not be fully reliable source of data. The collected data has been arranged, processed and silently manipulated to make easily for analyzing. Further a detailed analysis of bank financial and operating data sometimes can not be made by a external analysis because only condensed bank statements are available. Therefore, the best analysis of financial performance of the bank basically depends upon the fact finding of the data. There are a number of tools for analyzing the financial performance of the bank. Because of inadequate data and time, only some of the common and well-accepted tools like comparative and common-size financial statement analysis trend percentage analysis, net working capital and funds flow analysis, cash flow analysis, ratio analysis along with some statistical tools mean, standard deviation and correlation have been adopted or analysis of financial performance of the selected bank.

A mere numerical analysis may not give the best result about the financial performance of the bank, some of the abstract phenomenon, which can not be expressed in monetary form, may effect the analyzing the data. Again, the data received from annual report has been taken as same form i.e. time value of money has been fully ignored and it is another limitation of methodology in this study. Similarly, only major two statement (i.e. P/L a/c & B/S) is taken for analyzing the data. There are a number of statements, which reflect the clear financial performance of the bank and it has been fully ignored. Further, this study does not compare with the financial performance of another bank and it compare between bank's past performance and present performance only. Finally, this study fives recommendation to the bank for it's better future performance, which may not fully applicable to the bank in future environments.

CHAPTER-FOUR

PRESENTATION AND ANALYSIS OF DATA

4.1 Introduction:

It is the main part of the study researcher comes to know in the ground of reality about the financial performance of FORWARD where he tests the data with financial and statistics tools. Financial performance is the matter of interest in the inner of the organization. All different stakeholders and concerned parties look into it with different views on their interest. The stakeholders are integrated in creditor is interested to know whether the firm is in position to meet up its obligation like current liabilities on the other hand the long term creditors give interest to know the working capital and fixed assets of it. Especially the financial management is interested in the fact that the resources of the firm are used effectively and most efficiently.

Management should particularly be interested in knowing the financial position of the firm to make their best use and to be able to spot out the financial weakness of the firm to take correct action for future. If financial statement is properly analyzed it shows the financial strength and weakness. The important part of the study is presentation and analysis of data which helps to find out the fact matter about organization so to get fact results researcher uses the modern tools such as funds flow, financial ratio, trend percentage analysis, trend least square method analysis and correction analysis. In conclusion this chapter gives answer the research question and derives certain conclusion.

4.2 Funds flow analysis:

The term funds flow indicates the inflows and outflows of funds during a particular accounting period, generally year. The flow exhibits the movement of funds in both the directions inside the business and outside the business. However

the flow of funds must arise due to external not internal transaction of the business for instance the capitalization of reserves by the issue of bonus shares is an internal transaction. Such transactions are not included in the statement as there is no real addition to the funds of the company. When the term fund is used in the sense of working capital, funds flow will mean inflow and outflow of working capital.

In fact, funds flow analysis reveals about the sources and uses of fund properly. The sources and uses of fund are calculated from balance sheet of the FORWARD on the last day of the FY of five consecutive years 2064/65 BS unto 2068/69 BS. The current year is compared with previous year, increases in amount of any item in the liability side of balance sheet is accounted as uses of fund during the FY.

4.2.1 Sources of fund:

The sources of fund for different years are detected from five year balance sheet for the purpose of funds flow analysis for the bank. The different sources of funds have been available for FORWARD during the study periods of 2064/65 BS to 2068/69 BS. They are as follows:

- a) Share has not issued
- b) Increase in reserve & funds
- c) Increase in borrowings
- d) Increase in deposits liabilities
- e) Increase in other liability and provisions

Table 2**The sources of funds are presented in table No. 1****(Rs.000)**

S.N	Particular	064/65	065/66	066/67	067/68	068/69
1.	Share capital	–	–	–	–	–
2.	Increase in reserve	37077	64596	89882	131167	154982
3.	Increase in deposit	73314	117413	167382	249921	373680
4.	Increase in borrowing	180913	198401	270056	411002	674716
5.	Increase other liabilities	5065	7338	12296	16747	24527
	Total	296369	387748	539616	808837	1227905

Source: Annual report of FORWARD.**4.2.1.2 Increase in reserve:**

The reserve at the period of FY 2064/65 was Rs. 37077 thousand, which has been shown in above table. Now it has been increased to 154982 thousand. Then the reserve has risen to 154982 thousand by increasing 117905 thousand. The reserve has been a permanent source of fund for the FORWARD. There is no any contribution for the source of the fund of the FORWARD. Thus the bank has intended to avoid over capitalization and managed it's operation function by the leverage of borrowing.

4.2.1.3 Increase in deposit:

Deposit includes group saving, personal saving, central fund saving, child saving and other saving. The total deposit amount has been continuously increasing. In this study, every year from the FY 2064/65 to 2068/69 BS its deposit has increases 73314, 117413, 167382, 249921 and 373680 thousand respectively. It is main source of the fund. So its contribution on the total source of fund is 24.73%, 30.28%, 31.01%, 30.89% and 30.43% respectively of the study period. The contribution of the deposit amount in total source of five years period

is 29.46% on the average. The FORWARD has been successful in increasing the resources by acceptance in deposit. Such an increase in deposit is due to faithful of public towards the bank. It reveals that the bank has been popular among the people in rural sector of the eastern region of our country. It is the good symbol for the FORWARD.

4.2.1.4 Increase in borrowings:

Borrowing is the major source of fund; it includes with national and international bank and financial institution for the loan. The main amount of borrowing is Rs 180913, 198401, 270056, 411002 and 674716 thousand respectively of the study period. It contributes on the total sources of fund 61.04%, 51.16%, 50.04%, 50.81% and 54.94% respectively. It covers 53.59% of the total sources of fund on average. It's contribution on total sources and average fund, which has been shown in above figure.

4.2.1.5 Increase in other liabilities:

Other liability includes payable office rent, payable salary, payable auditor, payable member, payable saving interest, payable taxes (office rent tax, Audit tax, salary tax, other tax), payable insurance, provident fund, proposed employee bonus and payable others. It is also increased gradually in study period. It has contribution the total source of fund as 1.70%, 1.89%, 2.27%, 2.07% and 1.99% respectively. Its average contribution on sources of fun is 1.98%.

Increase in other liabilities shows the increase in source of funds. There is not constant source of fund during the study period. So decrease in other liabilities shows the unhealthy economic situation for institute.

4.2.2 Application of funds:

The following are found to be the uses of fund of the FORWARD in different year from FY 2064/65 BS to 2068/69 BS.

- (a) Increase in cash and bank balance
- (b) Increase in investment
- (c) Increase in loan and advance
- (d) Increase in loan loss reserve
- (e) Increase in fixed assets
- (f) Increase in other assets

Table 3

Uses of funds of FORWARD from the FY 2064/65 to 2068/69 BS

(Rs.000)

S.N	Particular	064/65	065/066	066/67	067/68	068/69
6.	Increase in Cash	13	65	513	198	208
7.	Increase in bank balance (current)	2470	3855	7483	8676	25374
8.	Increase in bank (saving & call a/c)	26919	49576	27954	48048	302122
11.	Investment (FD)	26125	26125	14500	17875	31025
9.	Increase loan & advance	235851	302420	476419	709700	800101
10.	Loan loss reserve	(5179)	(7302)	(15371)	(19558)	(29307)
12.	Increase in fixed assets	5740	74663	14159	22500	69546
13.	Increase in other assets	4430	5546	13959	21398	28836
S.N	Total	296369	387748	539616	808837	1227905

Source: Annual report of FORWARD.

4.2.2.1 Increase in cash and bank balance:

The FORWARD has utilized its resources to increase in cash and bank balance. Bank balance of FORWARD includes two types of bank account i. e. bank balance as per current account and bank balance per saving and call account. At the end of FY 2064/65 to 068/69, cash balance is amounted Rs 13, 65, 513, 198

&208 thousand which is in increasing trend, bank balance as per current account is amounted Rs 2470, 3855, 7483, 8676 & 25374 thousand which is also in increasing trend and bank balance as per saving and call account is amounted Rs 26919, 49576, 27954, 48048 & 302122 thousand which is in fluctuating trend. Entirely the cash and bank balance of FORWARD is amounted Rs 29399, 53496, 35950, 56922 & 327704 thousand respectively.

Contribution of cash and bank balance on the application of the fund is 9.91%, 13.79%, 6.66%, 7.03% & 26.68% respectively of the study period. It contributed to the total fund of utilization by 12.81% on average.

The cash and bank balance is the best for liquidity but it is very expensive for financial institution if it keeps balance in excess. The bank could not make any investment for generate of any income. Minimum cash and bank balance shows that total fund utilization by FORWARD as cash and bank balance has not been used properly.

4.2.2.2 Increase in investment:

The FORWARD used its fund by investing in its corresponding area. These are government bonds company share as well as fixed deposit of commercial bank. The amount of investment figure of this bank is amounted Rs 26125, 26125, 14500, 17875 & 31025 thousand respectively during the study year. The figure has shown clearly that in the first two years of the study period i. e. from FY 2064/65 to 65/66, the investment remain constant then it drastically reduce in FY 2066/67 with the comparison of previous two years. Then after, the investment is gradually go on increasing in FY 2067/68 to 2068/69.

The fluctuated condition of the investment reveals that the investment policy of the bank is not satisfactory.

4.2.2.3 Increase in loan and advance (loan outstanding):

It includes General loan, seasonal loan, Centre fund loan, Micro Enterprise loan, foreign employment loan, sanitary construction loan, House construction loan etc. The amount of loan outstanding from the FY 2064/65 to 2068/69 is Rs 235851, 302420, 4764019, 709700 & 800101 respectively which is in increasing trend. It established with a view to upgrade the rural public economic condition. The figure of loan outstanding reveals enlistment in the rural sector. On the other aspect, increasing in loan outstanding is to rise in revenue income of the bank by receiving as interest. Since the bank has not issued the share capital in order to meet up the fund required for loan disbursement because it has adopted the policy of taking the aid of borrowings. However the increase in borrowings is found to be less than the increase in loan outstanding which is the positive way to run the bank only borrowings and loan outstanding relationship.

4.2.2.4 Increase in loan loss reserve:

Reserves of have been changing in this study period. The reserve of FORWARD is in increasing trend from FY 2064/65 to 2068/69 by Rs 5179, 7302, 15371, 19558 & 29307 thousand respectively. These type of increase have happened due to continuous claim in capital reserves. Increasing reserve indicate good performance of the centre.

4.2.2.5 Increase in fixed assets:

Fixed assets of FORWARD include the land, building, furniture and fixture, office equipment, vehicle, computer and miscellaneous etc. The fixed assets of this bank has increased from FY 2064/65 to 2068/69 BS is amounted Rs 5740, 7463, 14159, 22500 and 69546 thousands. So the bank has become able to utilize its fund properly in respect of fixed assets.

4.2.2.6 Increase in other assets:

Other assets of FORWARD include receivables, staff advance, staff cycle facility, stationary stock, provident fund deposit and other receivable. The other assets of this bank has increased from FY 2064/65 to 2068/69 is amounted Rs 4430, 5546, 13959, 21398 & 28836 thousands respectively. So the bank has become sustainable to utilize its fund properly in respect of other asset.

4.3 Ratio analysis:

Ratio analysis is a technique of analysis and interpretation of financial statements. To evaluate the performance of and organization by creation the ratio from the figures of different accounts consisting balance sheet and income statement is known as ratio analysis. "One cannot arrive a definite conclusion about the financial health of an enterprise simple by studying and scanning the absolute figures contained in the conventional from of financial statement viz. revenue statement (i.e. P/L account) and balance sheet. The same is possible only when the absolute figures are analyzed further in term of ratios."⁶³

Ratio analysis is an important tool of financial analysis. A ratio is a statistical two figures tape that measures the relationship between is used as a measuring tape evaluating the financial position and performance of an enterprise and by its help we can make proper qualitative judgment accounting. We are calculating the following ratio in this study.

1. Liquidity ratios
2. Leverage ratios
3. Activity ratios
4. Profitability ratio

4.3.1 Liquidity ratios:

Liquidity ratios measure the firm's ability to meet current obligations. It reflects the short-term financial strength of the firm. It is most important to measure liquidity position of FORWARD. The following ratios are considered:

- i. Current ratio
- ii. Working capital to current ratio
- iii. Cash and bank balance to total deposit
- iv. Cash and bank balance to current assets

4.3.1 (i) Current ratio:

Current assets includes cash and bank balance, short term investment, interest receivable, inventories, sundry debtors, account receivable and other assets accept loans and advance to staff etc. On the other side, current liabilities includes saving and deposit, sundry creditors, other liabilities and provision, employees reserve fund, doubtful debts provided fund and etc. Current ratio is calculated by the following formula:

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

Table 4

Current ratio of FORWARD FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Current assets 1	Current liabilities 2	Ratio = 1/2
2064/65	33832	78379	0.43:1
2065/66	59042	124751	0.47:1
2066/67	49909	179678	0.27:1
2067/68	78320	266668	0.29:1
2068/69	356540	398207	0.89:1

Source: Annual report of FORWARD

The current ratios of FORWARD from FY 2064/65 BS to FY 2068/69 BS have been shown in the table no. 3. It is clear that the current ratios of the five year period are less than 1. So there is adverse effect on operations through the view of current ratio. If the ratio is less than two times difficulty may be created in the payment of current liabilities and daily operations of organization may suffer.

The FORWARD has the current ratios as follows: 0.43:1, 0.47:1, 0.27:1, 0.29:1, and 0.89:1. The ratio for the bank is less than the general standard i.e. 2:1. However, banks are the service tendering organization therefore 1:1 ratio for the bank is also a satisfactory level. But the current ratio of FORWARD is decreased.

4.3.1(ii) Cash and bank balance to total deposit ratio:

Cash and bank balance to total deposit measures the percentage of cash and bank balance maintained by the commercial banks in order to honor the cheques presented by its depositors excluding fixed deposit. The cash and bank balance to total deposit ratios calculated by dividing cash and bank balance by total deposit

Table 5

Cash & Bank and Deposit of FORWARD FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Cash & Bank balance 1	Total Deposit 2	Ratio = $\frac{1}{2}$
2064/65	29399	73314	40.10%
2065/66	53496	117413	45.56%
2066/67	35950	167382	21.47%
2067/68	56922	249921	22.78%
2068/69	327704	373680	87.69%

Source: Annual report of FORWARD

The ratios are found to be 40.10%, 45.56%, 21.47%, 22.78% and 87.69% from FY 2064/65 BS to 2068/69 BS respectively. Higher ratio indicates the sound payment position and vice-versa.

4.3.1 (iii) Cash and bank balance to current assets ratio:

This ratio reflects the portion of cash and bank balance in total of current assets. Cash and bank balance are highly liquid assets than other assets. This ratio measures the ability of bank to payout the total call made on current deposits. This ratio indicates that, if the ratio is higher, there is high margin and if lower, the bank is less liquid.

$$\text{Cash and bank balance to current assets ratio} = \frac{\text{Cash \& bank balance}}{\text{Current assets}} \times 100$$

Table 6
Cash & Bank of FORWARD FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Cash & Bank balance 1	Current assets 2	Ratio = 1/2
2064/65	29399	33832	86.89%
2065/66	53496	59042	90.60%
2066/67	35950	49909	72.03%
2067/68	56922	78320	72.67%
2068/69	327704	356540	91.91%

Source: Annual report of FORWARD

The ratios are found to be 86.89%, 90.60%, 72.03%, 72.67%, and 91.91%. The ratio is in fluctuating trend over the period of study.

4.3.2 Leverage Ratios:

These ratios are also called solvency ratios or capital structure ratios. The use of finance is referred to by financial leverage. The capital structure position of FORWARD has been evaluated with help of the following ratio analysis:

- i. Debt-equity ratio
- ii. Debt-asset ratio
- iii. Debt capital ratio
- iv. Net fixed asset to equity
- v. Increase coverage ratio
- vi. Current assets to equity

4.3.2 (i) Debt-Equity Ratio:

FORWARD has not issued any kinds of share capital. So, this ratio can not be computed due to absence of share capital. This ratio is computed by applying the following formula:

$$\text{Debt-equity ratio} = \frac{\text{Total debt}}{\text{Shareholders equity}}$$

4.3.2 (ii) Debt-Assets Ratio:

This ratio indicates the financial contribution of outsiders and owners on total assets of the firm. It also measures the financial security of outsiders. Generally creditors prefer a low debt ratio whereas, owners prefer high debt ratio in order to magnify their earnings and maintain their concentrated control over the firm. Higher the ratio depicts higher the contribution of debt in total assets consequently higher the risk association. The relationship between total liabilities and total assets is known as debt-asset ratio. It is calculated by the following formula:

$$\text{Debt-Asset ratio} = \frac{\text{Total debt}}{\text{Total assets}} \times 100\%$$

Table 7

Debt-assets ratio of FORWARD FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Total Debt. 1	Total Assets 2	Ratio = 1/2
2064/65	259292	296369	87.48%
2065/66	323152	387748	83.34%
2066/67	449734	539616	83.34%
2067/68	677670	808837	83.78%
2068/69	1072923	1227905	87.37%

Source: Annual report of FORWARD

It is expressed in percentage. Deducting the loss from total assets of the balance sheet has brought total assets. The debt-assets ratio from FY 2064/65 to 2068/69 BS is 87.48%, 83.34%, 83.34%, 83.78% and 87.37% respectively. The total debt-assets ratio for FORWARD is highest at 87.48% in FY 2064/65 and it is lowest in FY 2065/66 and 2066/67 i.e. 83.34% which is same in both FY.

4.3.2 (iii) Net fixed asset to equity ratio:

It is the relationship between net fixed assets to equity. So this ratio can not be computed due to absence of equity. Formula for computing this ratio is as follows,

$$\text{Net fixed assets to equity} = \frac{\text{Net fixed assets}}{\text{Equity}} \times 100\%$$

4.3.2 (iv) Interest coverage ratio:

The ratio also is known as the interest earned ratio. A high ratio is a sign of low burden of borrowing of business and lower utilization of borrowing capacity from the point of the view of the creditors, larger the coverage the greater the ability of the firm to make the payment of interest to creditors.

$$\text{Interest coverage ratio} = \frac{\text{EBIT} + \text{Interest}}{\text{Interest}}$$

Table 8

Interest coverage ratio of FORWARD FY 2064/65 to 2068/69 BS

(Rs.000)

FY	EBIT+Inerest 1	Total interest charge 2	Ratio = $\frac{1}{2}$
2064/65	40958	11684	3.505:1
2065/66	61602	18075	3.408:1
2066/67	77596	26463	2.932:1
2067/68	140490	48641	2.888:1
2068/69	190978	78263	2.440:1

Source: Annual report of FORWARD

In the beginning year of the study period, it is higher value to ratio. It shows the ability to pay the interest. All year have the low ratio. Higher coverage ratio of the FORWARD indicates strong the ability of firm to make the payment of interest creditors.

4.3.2 (v) Current assets to equity ratio:

A current asset to equity has been computed by dividing equity into current assets. The formula for computing this ratio is as follows,

$$\text{Current assets to equity ratio} = \frac{\text{Current assets}}{\text{Equity}}$$

But here in this study, share capital is not available, so it is not possible to compute this ratio.

4.3.3 Activity Ratio:

Activity ratios are also called efficiency or turnover ratios. These ratios reflect that how effectively and efficiently the bank has been using its resources. Higher the activity ratios the better the profitability and use of capital or resources

will be greater the amount of collection from over due loan the amount available for providing loan to public or rural.

- (i) Loan outstanding to collection ratio
- (ii) Loan collection to disbursement ratio
- (iii) Loan outstanding to disbursement ratio
- (iv) Loan outstanding to equity ratio
- (v) Administrative expenses to loan outstanding
- (vi) Investment to total deposit ratio
- (vii) Loan outstanding to total deposit ratio

4.3.3.(i) Loan outstanding to collection ratio:

A relationship between loan outstanding and total collection is represented by this ratio. This ratio is calculated by dividing loan collection into loan outstanding.

$$\text{Loan outstanding to collection ratio} = \frac{\text{Loan outstanding}}{\text{Collection}}$$

Table 9

**Loan outstanding to collection ratio of FORWARD from
FY 2064/65 to 2068/69 BS**

(Rs.000)

FY	Loan outstanding 1	Loan Collection 2	Ratio = $\frac{1}{2}$
2064/65	235851	594670	0.396:1
2065/66	302420	1104273	0.273:1
2066/67	476419	1790011	0.266:1
2067/68	709700	2905406	0.244:1
2068/69	800101	4480505	0.179:1

Source: Annual report of FORWARD.

The ratio is calculated in percentage in realization of the loan disbursement by it. The above ratios are fluctuating that in the all years of the study period. The outstanding loan should collect in time to mobilize the fund again for disbursement. It helps to increase the bank activities. So the Microfinance institution should try to finish the ratio further by timely collection loan.

4.3.3.(ii) Loans collection to disbursement ratio:

The loans collection to disbursement ratio is obtained by dividing loans disbursement to loan collection.

$$\text{Loan collection to disbursement ratio} = \frac{\text{Loan collection}}{\text{Loan disbursement}} \times 100\%$$

Table 10
Loan collection to disbursement ratio of FORWARD
FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Loan collection 1	Loan Disbursement 2	Ratio = 1/2
2064/65	594670	830521	0.72:1
2065/66	1104273	1406693	0.78:1
2066/67	1790011	2266430	0.79:1
2067/68	2905406	3615106	0.80:1
2068/69	4480505	5280606	0.84:1

Source: Annual report of FORWARD

Micro-Financial institutions are generated income on loan disbursed. It can exist and efficiently if the loan disbursements are collected in time so the ratio is significant for financial institutions like FORWARD. Higher ratio is

preferable for financial institution like FORWARD. The loan collection to disbursement ratio for the financial institution should be maintained 85% level. In FY 2064/65, 2065/66 BS the ratios are 94% & 95% which is less than other ratio of the study period. However, all ratios are greater than the expected level 85%.

4.3.3.(iii) Loan outstanding to disbursement ratio:

The ratio shows the relationship between loans outstanding and disbursement. It measures what percentage of the loans outstanding has remained yet in client in comparison with disbursement. It is computed by the following way.

$$\text{Loan outstanding to disbursement} = \frac{\text{Loan outstanding}}{\text{Loan disbursed}} \times 100\%$$

Table 11
Loan standing to disbursement ratio of FORWARD from
FY 2064/65 to 2068/69 BS.

(Rs.000)

FY	Loan outstanding 1	Loan Disbursement 2	Ratio = 1/2
2064/65	235851	830521	28.39%
2065/66	302420	1406693	21.49%
2066/67	476419	2266430	21.02%
2067/68	709700	3615106	19.63%
2068/69	800101	5280606	15.15%

Source: Annual report of FORWARD

Higher ratios are not good for the bank or micro-finance institution. Interest is received from loan, in that view the higher loan outstanding is to source of the interest but there may be doubtful in repayment of the loan. The loan should be repayment in right time. The calculated figure of its ratio 60.20 on average that is in satisfactory position because the lowest and highest amount of outstanding is not good condition for the bank.

4.3.3.(iv) Loan outstanding to equity ratio:

This ratio shows the relationship between loan outstanding and shareholders equity. It is computed by the following way.

$$\text{Loan outstanding to equity ratio} = \frac{\text{Loan outstanding}}{\text{Shareholders equity}}$$

But, here in this study, the FORWARD has not issued any shares. Hence, it is not possible to compute this ratio in the absence of share holders equity

4.3.3.(v) Administrative expenses to loan outstanding ratio:

This ratio shows the relationship between administrative expenses and loans outstanding. It is calculated as follows.

$$\text{Administrative expenses and loans outstanding} = \frac{\text{Administrative ex.}}{\text{Loan outstanding}} \times 100\%$$

Table 12

**Administrative expenses to loans outstanding ratio of FORWARD
FY 2064/65 to 2068/69 BS.**

(Rs.000)

FY	Administrative expenses 1	Loans outstanding 2	Ratio = 1/2
2064/65	16602	235851	7.04%
2065/66	23705	302420	7.84%
2066/67	35379	476419	7.42%
2067/68	53715	709700	7.57%
2068/69	72210	800101	9.02%

Source: Annual report of FORWARD

It is expressed as percentage the administrative expenses include staff and office expenses. The ratio reveals how the institution has been operating its activities. The ratio gives a relation between a balance sheet item and income statement item. Higher ratios show the higher level of expenses.

4.3.3.(vi) Investment to total deposit ratio:

This ratio is calculated by dividing total deposit to investment.

$$\text{Investment to total deposit ratio} = \frac{\text{Investment}}{\text{Total deposit}} \times 100\%$$

Table 13
Investment to total deposit ratio of FORWARD
FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Investment 1	Total deposit 2	Ratio = 1/2
2064/65	26125	73314	35.63%
2065/66	26125	117413	22.25%
2066/67	14500	167382	8.66%
2067/68	17875	249921	7.15%
2068/69	31025	373680	8.30%

Source: Annual report of FORWARD

It is expressed as percentage. It shows the relationship between investment and total deposit. A bank may be two types of investment namely, capital (which includes share capital, shareholders equity on net worth) and deposit etc. In FORWARD, share has not issued. So it's investment consist of deposit investment. A sound investment policy of bank such that its funds are distributed on different types of assets with good profitability in one hand provides maximum safely and security to the depositors and the bank. On the other hand the objective of a bank is to earn maximum profit by giving facility loans and qualitative services to rural area's public. The above shows the positive result on aspect of the investment.

4.3.3.(vii) Loan outstanding to total deposit ratio:

The ratio shows what portion of deposit has been carried by the loan outstanding. The bank has to mobilize deposits collected income generating purpose so that it will be able to pay the interest to its deposits and to earn profit. The loan outstanding to total deposit ratio measures the extent, which the banks under consideration are successful on utilizing the outsider's funds for the profit generating purpose. In other words the ratio measures the bank ability to mobilize its deposits i.e. current saving call and short deposits and others deposit in terms of grading loans outstanding which yield higher return. The ratio is computed by using following formula.

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

Table 14

**Loan outstanding to total deposit ratio of FORWARD from
FY 2064/65 to 2068/69 BS**

(Rs.000)

FY	Loan Outstanding 1	Total deposit 2	Ratio = 1/2
2064/65	235851	73314	3.21:1
2065/66	302420	117413	2.57:1
2066/67	476419	167382	2.85:1
2067/68	709700	249921	2.84:1
2068/69	800101	373680	2.14:1

Source: Annual report of FORWARD

The higher ratio is non preferable for financial company. The ratio of the loan outstanding to total deposit are 3.21:1, 2.57:1, 2.85:1, 2.84:1 and 2.14:1 respectively. It activities are in satisfactory condition in view with loans outstanding and deposits.

4.3.4 Profitability Ratios:

Profitability ratio is measure of overall efficiency and the search for it provides an incentive to achieve efficiency. It's ratio measures the management overall performances and effectiveness. Profitability is the net result of a large number of policies and decisions. This ratio gives final answer to how effectively the firm is being managed. Management along is not interested in the profitability of the bank but also the government and owner's or investors are equally interested. Creditors want to return of principal at the due data. Owners want to get a reasonable return on their investment. Employees want may facilities, which is possible only when the bank earns sufficient profit. Profitability position of FORWARD is evaluated on the basis of following ratio analysis.

- (i) Net profit to total assets ratio
- (ii) Net profit to total deposit ratio
- (iii) Operating ratio
- (iv) Interest earned to total assets ratio
- (v) Return on equity ratio

4.3.4.(i) Net profit to total assets ratio:

The net profit is the essential factor for an institution to survive and expand its function. Form the financial statement of FORWARD we can see the profit is in increasing trained during the study period. "Financial statements are essential interim reports and therefore can't be final because the actual gain or loss of a business can be determined only after it put down its shutter."

This ratio of the net profit to total asset is calculated as follows.

$$\text{Net profit to total assets ratio} = \frac{\text{Net profit}}{\text{Total assets}} \times 100\%$$

Table 15
Net profit to total assets ratio of FORWARD
FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Net profit or loss 1	Total assets 2	Ratio = $\frac{1}{2}$
2064/65	17589	296369	5.93%
2065/66	30270	387748	7.80%
2066/67	23368	539616	4.33%
2067/68	39861	808837	4.93%
2068/69	34452	1227905	2.80%

Source: Annual report of FORWARD

The ratio is 5.93% in FY 2064/65 BS, 7.80% in FY 2065/66 BS, 4.33% in FY 2066/67 BS, 4.93% in FY 2067/68 BS and 2.80% in FY 2068/69 BS. The above ratios point out the weak position on the institution like FORWARD. Net profit to total assets ratio indicates whether the total assets of the business has been properly used or not. The given figure shows that the bank must be attention for utilization assets properly in right track.

4.3.4.(ii) Net profit to total deposit:

It is computed by dividing the total deposit into profit.

$$\text{Net profit to total deposit ratio} = \frac{\text{Net profit}}{\text{Total assets}} \times 100\%$$

Table 16
Net profit to total deposit ratio of FORWARD
FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Net profit 1	Total deposit 2	Ratio = $\frac{1}{2}$
2064/65	17589	73314	23.99%
2065/66	30270	117413	25.78%
2066/67	23368	167382	13.96%
2067/68	39861	249921	15.95%
2068/69	34452	373680	9.22%

Source: Annual report of FORWARD

The above table shows the net profit to total deposit of FORWARD for five years of time period. This ratio also shows in percentage. The ratio is maximum in FY 2065/66 BS i. e. 25.78% and it is lowest in FY 2068/69 BS i.e. 9.22%. Higher the ratio indicates higher the return and lower the ratio indicates lower the return.

4.3.4.(iii) Operating ratio:

Operating ratio is an important ratio that shows the change in the net profit margin ratio. This ratio is computed by total operating revenue to total operating expenses.

$$\text{Operating ratio} = \frac{\text{Operating expenses}}{\text{Operating revenue}} \times 100\%$$

Table 17
Operating ratio of FORWARD FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Operating expenses 1	Operating revenue 2	Ratio = 1/2
2064/65	16602	33910	48.95%
2065/66	23705	51218	46.28%
2066/67	35379	66191	53.45%
2067/68	53715	94827	56.65%
2068/69	72210	116038	62.22%

Source: Annual report of FORWARD

It is expressed as percentage ratio. The lower ratio expresses the higher profitability. The operating ratios of FORWARD in FY 2064/65 to 2068/69 BS are 48.95%, 46.28%, 53.45%, 56.65% and 62.22% respectively. The ratio is more than 100%. It means that the operating expenses are lower than operating income. Thus the profitability position of the FORWARD is sustainable.

4.3.4.(iv) Interest earned to total assets:

It is computed by the following formula.

$$\text{Interest earned to total assets ratio} = \frac{\text{Interest earned}}{\text{Total assets}}$$

Table 18
Interest earned to total assets ratio of FORWARD
FY 2064/65 to 2068/69 BS

(Rs.000)

FY	Interest earned 1	Total assets 2	Ratio = 1/2
2064/65	44372	296369	14.97%
2065/66	66767	387748	17.21%
2066/67	90326	539616	16.74%
2067/68	141601	808837	17.50%
2068/69	178008	1227905	14.50%

Source: Annual report of FORWARD

It is expressed also percentage ratio. The higher ratio is preferable and favorable on the financial institution. The interests earned to total assets are 14.97%, 17.21%, 16.74%, 17.50% and 14.50% respectively of the study year. It has not seen increased in 17.50% so reveals bad financial performance of this bank.

4.3.4.(vi) Return on equity ratio:

The relationship between net profit and equity is known as return on equity. It is calculated by following way.

$$\text{Return on equity ratio} = \frac{\text{Net profit}}{\text{Equity}} \times 100\%$$

FORWARD has not issued any share equity. So it is not possible to compute this ratio, in this study.

4.4 Correlation Analysis:

Two variables are said to have correlation when they are related that the change on the value of one variable is accompanied by the change in the value of the other. In this study, the researcher follows the Karl Pearson's correlation. The Coefficient method to find out the correlation among the various aspects, deposits and investment, loan disbursement and collection and borrowing and loan outstanding. They are as under:

4.4.1 Borrowing and loans outstanding:

FORWARD has taken its loan by the national and international bank. The national or domestic source of loan is RMDC, several commercial banks and finance company. International loan is taken from Plan Nepal, Asian Development Bank (ADB), UNICEF, CADP, EAFSP and other various funding NGOs, Ingo's. Borrowings are the main source of the fund. On the other sides the loan outstanding includes General loan, seasonal loan, Centre fund loan, Micro

Enterprise loan, foreign employment loan, sanitary construction loan, House construction loan etc .

The borrowings are found to be Rs 180913, 198401, 270056, 411002 and 674716 thousands and loan outstanding found to be Rs. 235851, 302420, 476419, 709700 and 800101 thousands from FY 2064/65 to 2068/69 BS respectively.

Table 19
Calculation of correlation between borrowing and loan outstanding
in '000000'

FY	Borrowing (X)	Loan outs. (Y)	x= (X- 270.05)	x ²	y= (y- 474.62)	y ²	Xy
064/65	180.91	235.85	-89.14	7945.94	-238.77	57011.12	21283.96
065/66	198.40	302.42	-71.65	5133.72	-172.2	29652.84	12338.13
066/67	270.05	474.62	0	0	0	0	0
067/68	411	709.70	140.95	19866.90	235.08	55262.61	33134.53
068/69	674.72	800.10	404.67	163757.81	325.48	105937.23	131711.99
			x= 384.83	x ² = 196704.37	y= 149.59	y ² = 247863.8	xy= 198468.61

Source: Annual report of FORWARD

$$r X \frac{N\phi_{xy} Z\phi_x\phi_y}{\sqrt{N\phi_x^2 Z(\phi_x)^2} \cdot \sqrt{N\phi_y^2 Z(\phi_y)^2}}$$

$$X \frac{5 | 198468.61 - 384.83 | 149.59}{\sqrt{5 | 196704.37 - 384.83 |} \cdot \sqrt{5 | 247863.8 | 149.59}}$$

$$X \frac{992343.05 - 57566.72}{\sqrt{983521.85 - 148294.12} \cdot \sqrt{1239319 - 22377.17}}$$

$$X \frac{934776.33}{\sqrt{835227.73} \cdot \sqrt{1216941.83}}$$

$$X \frac{934776.33}{913.91 | 1103.15}$$

$$X \frac{934776.33}{1008180.60}$$

$$X 0.927$$

The bank pays interest for borrowings and it receives interest from loans an outstanding. The main source of income is interest receipts. Different types of expenses are maintained by the interest earned on loan outstanding. However, there must be positive relationship between borrowings and loans outstanding. The FORWARD has the higher degree correlation between borrowings and loan outstanding because its correlation coefficient is higher degree positive i.e.0.927. It reveals that activities of the bank are going to right track.

4.4.2 Correlation between disbursement and collections:

FORWARD has disbursed loans for general loans, seasonal loans, loans, centre fund loan, Micro Enterprise loan, foreign employment loan, sanitary construction loan, House construction loan etc. The objective of FORWARD is to flow the loans in rural poor people in the facility rate of interest to decrease the poverty growth of the nation. it conducts its activities upon who have no land and property to deposit in the bank for the security. in the other

word it seems that the gives loan to rural people without any security. so it has more chance to increase its overdue loan.

Table 20

Calculation of correlation between loan disbursements and collections.

In “000000”

FY	Loan disbursement (X)	Loan collection (Y)	x = (X-2266)	x ²	y = (y-1790)	y ²	xy
2064/65	831	595	-1435	2059225	-1195	1428025	1714825
2065/66	1407	1104	-859	737881	-686	470596	589274
2066/67	2266	1790	0	0	0	0	0
2067/68	3615	2905	1349	1819801	1115	1243225	1504135
2068/69	5281	4481	3015	9090225	2691	7241481	8113365
			x= 2070	x ² = 13707132	y= 1925	y ² = 10383327	xy= 1192159 9

Source: Annual report of FORWARD

$$r = \frac{N\sum xy - \sum x \sum y}{\sqrt{N\sum x^2 - (\sum x)^2} \cdot \sqrt{N\sum y^2 - (\sum y)^2}}$$

$$= \frac{5 | 11921599 - 2070 | 1925}{\sqrt{5 | 13707132 - (2070)^2} \cdot \sqrt{5 | 10383327 - (925)^2}}$$

$$= \frac{59607995 - 3984750}{8015.66 | 6943.41}$$

$$= \frac{55623245}{55656013.8006}$$

$$= 0.99$$

There is higher position correlation rate i.e. 0.99 between loans disbursement and loan collection (repayment). it indicates that loans disbursement and loan collection has closer relationship as 99%. It helps to create good financial performance of the bank.

CHAPTER-FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

1.1 Summary:

Nepal is predominantly rural country where rural sector provides large contribution to the nation's economy. Among various problems in rural financing is one of the major problems. FORWARD is a micro-finance institution which is entrusted with the responsibilities of imitating effective approaches for the development of rural and committed to raise the economic condition of rural woman by availing credit and capital inputs in easy and smooth manner. Further, the FORWARD finance rural woman on group liability and expend it's scope of financing to promote cottage industries.

To meet the basic objectives of the FORWARD financial strength ness is key variable. For this a regular financial appraised is most necessary. This study therefore tries to display the financial performance of FORWARD over past five years from FY 2064/65 BS to 2068/69 BS. As per the data presentation and analysis, following result was obtained from this study in brief. Income statement shows the following result over past five fiscal years.

Table 21
Summary of total income, expenses and net profit

All amount in NRS. Thousand

Year	2064/65	2065/66	2066/67	2067/68	2068/69
Total income	48055	69416	94581	151180	194302
Total expenses	16602	23705	35379	53715	72210
Net profit	17589	30270	23368	39861	34452

Source: Annual audit reports of FORWARD – Appendix B

The total income consist interest income & other operational income and total expenses consist personnel expenses and other operational expense.

The total assets and liabilities of the FORWARD of the past five year base Rs.296369, 387748, 539616, 808837 and 1227905 thousand respectively from the FY 2064/65, 2065/66, 2066/67, 2067/68, 2068/69 BS. The major financial sources of funds as over past five years are as follows:

Table 22
Summary of major financial sources of fund

All amount in NRS. Thousand

Year	2064/65	2065/66	2066/67	2067/68	2068/69
Reserve & fund	37077	64596	89882	131167	154982
Internal & external borrowing	180913	198401	270056	411002	674716
Deposit	73314	117413	167382	249921	373680

Source: Annual audit reports of FORWARD – Appendix A

The reserve & fund consists General reserve, Growth fund, ID fund, Insurance fund, Welfare fund Fixed asset fund & net profit and deposit consist group saving, personal saving, centre fund saving, child saving, special saving, Double scheme saving, Upkar fund etc.

The loan investment assets over the past five years are as follows:

Table 23

Summary of loan investment assets

All amount in NRS. Thousand

Year	2064/65	2065/66	2066/67	2067/68	2068/69
Loan investment	26125	26125	14500	17875	31025
Provision for doubtful debt	5179	7302	15371	19558	29307

Source: Annual audit reports of FORWARD – Appendix A

Similarly loan distributed and collects till over the past five years are as follows:

Table 24

Summary of loan distributed and collected till now

All amount in NRS. Thousand

Year	2064/65	2065/66	2066/67	2067/68	2068/69
Loan distributed till now	830521	1406693	2266430	3615106	5280606
Loan repaid till now	594670	1104273	1790011	2905406	4480505

Source: Annual audit reports of FORWARD – Appendix A

The summaries of the various ratios calculated in this study are as follows:

Table 25
Summary of various ratio

All amount in NRS. Thousand

Ratio	2064/65	2065/66	2066/67	2067/68	2068/69
1. Liquidity ratio:					
i. Current ratio	0.43:1	0.47:1	0.27:1	0.29:1	0.89:1
ii. Cash & bank bal. total deposit	40.10%	45.56%	21.47%	22.78%	87.69%
iii. Cash & bank bal. to current assets	86.89%	90.60%	72.03%	72.67%	91.91%
2. Leverage ratio:					
i. Debt equity ratio	-	-	-	-	-
ii. Debt assets ratio	87.48%	83.34%	83.34%	83.78%	87.37%
iii. Net fixed assets to equity	-	-	-	-	-
iv. Interest coverage	3.505:1	3.408:1	2.932:1	2.888:1	2.440:1
v. Current assets to equity	-	-	-	-	-
3. Activity ratio:					
i. Loan outstanding to collection	0.396:1	0.273:1	0.266:1	0.244:1	0.179:1
ii. Loan collection to disbursement	0.72:1	0.78:1	0.79:1	0.80:1	0.84:1
iii. Loan outstanding to disbursement	28.39%	21.49%	21.02%	19.63%	15.15%
iv. Loan outstanding to equity	-	-	-	-	-
v. Administrative ex. to loan outs.	7.04%	7.84%	7.42%	7.57%	9.02%
vi. Investment to total deposit ratio	35.63%	22.25%	8.66%	7.15%	8.30%
vii. Loan outstanding to total deposit	3.21:1	2.57:1	2.85:1	2.84:1	2.14:1
4. Profitability ratio:					
i. Net profit to total assets	5.93%	7.80%	4.33%	4.93%	2.80%
ii. Net profit to total deposit	23.99%	25.78%	13.96%	15.95%	9.22%
iii. Operating ratio	48.95%	46.28%	53.45%	56.65%	62.22%
iv. Interest earned to total assets	14.97%	17.21%	16.74%	17.50%	14.50%

Source: Annual audit reports of FORWARD – Appendix A

1.2 Conclusion:

After the presentation and analysis of data the following points are drawn as follows:

1. Share capital and borrowing is the main sources of fund although the main source of fund is used in loan disbursement.
2. Financial ratio indicates poor financial position.
3. Trend of operating expenses is increasing day by day.
4. Reserve & fund has been increased during the study periods it is also permanent source of fund.
5. Loan disburse by the bank are quite small in amount, it is not practicable to legal action against the defaulters.
6. The FOORWARD is not going to break even level. Its activities are also expanding day by day.
7. Loan has timely recovered so interest receivable has not been increased in the study period.
8. The bank has shown overdue loans.
9. The bank has charged interest of its branches against borrowing amount therefore show the actual viability position of the branches.

1.3 Recommendations:

Financial viability and sustainability is the key variable for the development of the FOORWARD. Only financially strong institution can meet the required objectives. FOORWARD has been facing many kinds of problem to sustain/live in the competitive environment. Some of the essential recommendations have been given to the bank for its better future financial performance.

1. FOORWARD is not at all non-profit oriented organization, keeping in this mind; it must try to overcome the breakeven point for the survival by minimizing the unproductive expenses and cost and investing profitable area.

2. FORWARD must be serious in timely recovering of loans because if the loan disbursed by the co-operative is not timely recovered, its liquidity position will be hampered.
3. Equity is the permanent source of funds, its help manage the source of funds. The FORWARD must be increase its reserve & fund and decrease in its borrowings. Therefore, the co-operative can operate its financial activities on low risk.
4. To increase in deposit amount is to increase its financial activities, such a increase in deposit is helpful for the further investment. Increase in deposit is the sign of the faithful of public towards the bank. On the other side, an interest expenses is lower in deposit by comparing the interest expenses on borrowings of loans. Its helps to minimize the cost of the bank. So deposit amounts must be increase by convincing and attracting people.
5. FORWARD has not investment in government bonds, company share as well as fixed deposit of commercial bank. It helps to reach in the access of the capital market.
6. The FORWARD has over liquidity position. So it should be decrease in cash and bank balance for good liquidity position.
7. The bank must segregate the fixed costs and variable costs for its total administrative expenses and try to minimize the former. It should also try its level best to reduce the proportionality constant for such variable costs by improving the cost effectiveness.
8. Employees should be sufficiently motivated with proper incentives.
9. The accounts receivable and interest receivable should be collected with due care.
10. Employees should be given training how to behave with clients. Its helps to increase client's beliefs on the bank that makes huge amount of deposits.
11. The bank should emphasis on the clear and true recording of financial transaction and other financial statement.

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Forum For Rural Women Ardency Development (FORWARD)

Duhabi-3, Sunsari, Nepal

Balance-Sheet

From the fiscal Year 2064/65 BS to 2068/69 BS.

(Appendix-1)

Rs. 000

	2064/65	2065/66	2066/67	2067/68	2068/69	Assets	2064/65	2065/66	2066/67	2067/68
Liabilities & Capital										
Share Capital	-	-	-	-	-	1. Current asset:	13	65	513	198
Reserve & Surplus	37077	64596	89882	131167	154982	Cash				
Borrowings	180913	198401	270056	411002	674716	Bank/financial ins. Bal.	2470	3855	7483	8676
Current Liabilities:						(current)				
Deposit	73314	117413	167382	2249921	373680	Money at call & short notice	26919	49576	27954	48048
Other Liabilities	5065	7338	12296	16747	24527	(Selling & call)	26125	26125	14500	17875
						Investment (FD, Share debenture)	235851	302420	476419	709700
						Loan & advance (Loan loss reserve)	(5179)	(7302)	(15371)	(19558)
						2. Fixed asset	5740	7463	14159	22500
						3. Other asset	4430	5546	13959	21398
Total	2,96,369	3,87,748	5,39,616	8,08,837	12,27,905	Total	2,96,369	3,87,748	5,39,616	8,08,837

Forum For Rural Women Ardency Development (FORWARD)

Duhabi-3, Sunsari, Nepal

Profit and loss A/C

From the fiscal Year 2064/65 BS to 2068/69 BS.

(Appendix-2)

Rs. 000

Particulars	2064/65	2065/66	2066/67	2067/68	2068/69
(1) Income:					
(i) Interest Income	44372	66767	90326	141601	178008
(ii) other operational income	3684	2649	4256	9579	16294
A) Total Income (i + ii)	48056	69416	94582	151180	194302
(2) Expenses:					
(i) personnel expenses	10750	16516	23054	37216	40615
(ii) Other operational exp.	5950	7189	12325	16500	31595
B) Total Expenses (i + ii)	16600	23705	35379	53716	72210
3) Operational surplus before loan loss provision (A- B)	31456	45711	59203	97464	122092
Less: loan loss provision	2180	2184	8069	5616	9377
4) Operational profit before interest and tax (EBIT)	29276	43527	51134	91848	112715
Less: interest expenses	116857	18075	26462	48641	78263
5) Operational profit before tax (EBT)	17589	25452	24672	43207	34452
Add: Non-operational surplus	-	4818	-	-	-
Less: Provision for employees Bonus	-	-	1304	3346	-
6) Profit after interest and provision for bonus	17589	30270	23368	39861	34452
Less: Provision for tax	-	-	-	-	-
7) Net profit/ loss	17589	30270	23368	39861	34452