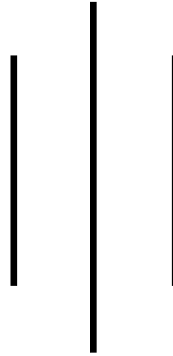
Credit Portfolio of Foreign Joint Venture Commercial Banks of Nepal

A Comparative Study on NABIL Bank Limited and Himalayan Bank Limited



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A Thesis Submitted to

Office of the Dean
Faculty of Management
Tribhuvan University

In partial fulfillment of the requirement for the degree of
Master of Business Studies (M.B.S.)

Kathmandu
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RECOMMENDATION

This is to certify that the thesis

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Credit Portfolio of Foreign Joint Venture Commercial Banks of Nepal

A Comparative Study on NABIL Bank Limited and Himalayan Bank Limited

has been prepared as approved by this department in the prescribed format of the Faculty of Management. This thesis is forwarded for examination.

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and found the thesis to be the original work of the student and written according to the prescribed format of Faculty of Management, Tribhuvan University. We recommend the thesis to be accepted as partial fulfillment of the requirement for the degree of **Master of Business Studies (M.B.S.)**

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DECLARATION

I hereby declare that the work reported in this thesis entitled **"Credit Portfolio of Foreign Joint Venture Commercial Banks of Nepal"** submitted to Office of the Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the Master's Degree in Business Study (M.B.S.) under the supervision of Lecturer **Dr. Arhan Stapit** of People's Campus.

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At last but not least, the thesis writer hopes that this report will be useful to the numerous readers and students who want to know about Credit portfolio.

Thank You!

Anu Maghaiya

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ABBREVIATIONS

AGM	Annual General Meeting
BAFIA	Bank and Financial Institution Act
BFI's	Bank and Financial Institutions
CV	Coefficeint Of Variation
EMLV	Estimated Market Level Value
EPS	Earning Per Share
F.Y	Fiscal Year
HBL	Himalayan Bank Limited
L/C	Letter Of Credit
Ltd.	Limited
NABIL	Nepal Arab Bank Limited
NPA	Non Performong Assets
NPL	Non Performing Loan
NRB	Nepal Rastra Bank
P.E	Probable Error
RBB	Rastriya Banijya Bank
SD	Standard Deviation
T.U	Tribhuvan University

CHAPTER - I

INTRODUCTION

A credit portfolio is an investment portfolio comprised of debts, like home and car loans. Private investors can build credit portfolios, but more commonly they are held by banks and other financial institutions. Credit portfolio management refers to the process of building a series of investments based upon credit relationships and managing the risks involved with these investments. Such a portfolio gains its value from the interest from issued loans but is susceptible to credit default. For that reason, credit portfolio management includes assessing the risk involved with each potential loan and analyzing the total amount of risk the portfolio incurs as whole.

1.1 Background of the Study

Financial sector is required for proper mobilization of investable resources from one sector to another and plays a pivotal role in bridging a gap between deficit units and surplus units. Efficient financial sector mobilizes saving from a broad variety of sources and allocating them into more productive uses, thus bridging benefits to both investors and investee and to the economy overall. In the process of reinvesting these savings, they successfully deal with one fundamental factor i.e. risk. The growth in liquidity of credit markets and the active management of credit risk are among the most significant developments in commercial banking in the past 20 years. These developments hold the potential to permanently reduce the risk profile and improve the financial performance of commercial banks.

Credit portfolio management grew out of the need to improve the financial performance of the large corporate loan portfolios in commercial banks. It is paradoxical that these portfolios created the biggest problems for originators and investors in the marketplace. After all, large corporate loan portfolios typically are composed of loans, commitments, and other lending exposures to banks' most creditworthy customers. Lending is the backbone of commercial banking, so lending is what banks should do best. Yet these

portfolios proved to be the source of recurring problems and the cause of failure for many commercial banks.

Nepal is a developing country. It faces many problems for its economic development and to make expansion in financial sector. In our economy banking system and the Financial Institutions play very significant role in the economy. First and foremost is in the form of catering to the need of credit for all the sections of society. The modern economies in the world have developed primarily by making best use of the credit availability in their systems. An efficient banking system must cater to the needs of high end investors by making available high amounts of capital for big projects in the industrial, infrastructure and service sectors. Financial institutions (FIs) are very important in any economy. Their role is similar to that of blood arteries in the human body, because FIs pump financial resources for economic growth from the depositories to where they are required (Shanmugan & Bourke, 1990). Commercial banks (CBs) are FIs and are key providers of financial information to the economy. They play even a most critical role to emergent economies where borrowers have no access to capital markets (Greuning & Bratanovic, 2003). “Sustainable development is about capital allocation and thus should be at the core of financial markets activity. Hence, the financial institutions can be the major stakeholder in achieving sustainable development (Delphi International Limited, 1997).

Financial market is very important for the economic growth of the country (Economic Survey, 2013) as they are guided by finance. The pace of development of a country largely depends upon its economic activities. Financial institutions provide capital to develop trade, industry and business. Bank, finance companies, cooperative societies, insurance companies, stock exchanges help in the economic progress of a nation (Economic Survey, 2004) Banks are major institutions in financing.

The financial institutions play a key role in development of a national economy because it functions as a medium of collecting and mobilizing resources to finance a business and development project that are essential for economic development (Eichengreen,1997). A country without good financial system can be a major problem for the economy to

function properly, to mediate sustainable private investment and promote entrepreneurship.

Financial institutions ease market friction and influence the allocation of resources over different sectors of the country (Levine,2004). The author introduces five key functions of financial system that are essential to economic growth.

- Produce information about possible investment and allocation capital
- Monitor investments and provide expert corporate governance
- Facilitate the trading, diversification and management of risk
- Mobilize and pool saving
- Ease the exchange of goods and services.

This way banks help to fortify the national development (Economic Survey, 2004/05). Banking is one of the most heavily regulated businesses in the world. Banks are among the most important financial institutions in the economy. They are the principal source of credit (loan-able funds) for millions of individuals and families and for many units of governments. Moreover, banks often act as a major source of credit to small local business for their stock. Banks are among the most important sources of short-term working capital for business and have become increasingly active in recent years in making long-term business loans for new plant and equipment (Shekher & Shekher, 2005). Banks are those financial institutions that offer the widest range of financial services especially credit, savings, payment services and perform the widest range of financial functions of any business firm in the economy.

Banks are expected to support their local communities with a sufficient supply of credit for all lawful business and consumer needs to price that credit reasonably in line with competitively determined interest rates. Bank loan support the growth of new businesses and jobs within the banks trade territory and promote economic vitality. Banks made a wide variety of loans to a wide variety of customers for many different purposes from purchasing automobiles and buying new furniture, taking dream vacations or pursuing

college educations, to constructing home and office buildings. Loans may be divided as; real estate loans, financial institution loans, agricultural loans, commercial and industrial loans, loans to individuals, miscellaneous loans, lease financing receivables etc.

In addition to the above traditional role, the banks and the financial institutions also perform certain new-age functions which could not be thought of a couple of decades ago. The facility of internet banking enables a consumer to access and operate his bank account without actually visiting the bank premises. The facility of ATMs and the credit/debit cards has revolutionized the choices available with the customers. The banks also serve as alternative gateways for making payments on account of income tax and online payment of various bills like the telephone, electricity and tax. The bank customers can also invest their funds in various stocks or mutual funds straight from their bank accounts. In the modern day economy, where people have no time to make these payments by standing in queue, the service provided by the banks is commendable.

Going through loan granting provision, bank will look through safety of funds, purpose of loans, security for loans, profitability spread of loan portfolio etc. Besides this, the character of person receiving credit, the capacity of borrower to utilize the fund, the percentage of borrower stake in the business are the basic elements which measure the excellence of borrower and finally the quantity of the loan. This way bank plays an important part in the development of trade, commerce and industry. Today no banker can survive for long run without proper standing of economy and cannot go ahead without proper banking system built.

Banks and financial intuitions have played major role in the economic development of the country and most of the credit- related schemes of the government to uplift the poorer and the under-privileged sections have been implemented through the banking sector. The role of the banks has been important, but it is going to be even more important in the future.

1.2 Profile of Sample Enterprises

1.2.1 NABIL BANK

(NABIL), the first foreign joint venture commercial bank of Nepal, started operations in July 1984.Nepal Arab Bank Limited was integrated with the objective of extending international standard modern banking services to various sectors of the society. Pursuing its objectives, the bank provides a full range of commercial banking services through its 19 points of representation across the country and over 170 reputed correspondent banks across the globe.

NABIL, as a pioneer in introducing many inventive products and marketing concepts in the domestic banking sector, represents a milestone in the banking history of Himalayanas it started an era of modern banking with customer satisfaction measured as a focal objective while doing business. Highly qualified and experienced team of NABIL bank manages day-to-day operations and risk management. Bank is fully equipped with modern technologies including ATMs, credit cards, state-of-art, world-renowned software from Infosys Technologies System, Banglore, India, Internet banking system and Tele-banking system.

NABIL Bank Limited is providing full-fledged commercial banking services to its clients. From its inception period in 1984 as the first joint venture bank, to commence operations in the Kingdom of Nepal, the bank have been a leader in terms of bringing the very best international standard banking practices, products and services to the kingdom. Today, mission of the bank is to be the “Bank of 1st Choice” to all of its stakeholders and customers.

1.2.2 Himalayan Bank Limited (HBL)

Himalayan Bank Limited, The first bank of Nepal was established in November 15, 1937 A.D (Kartik, 30, 1994). From the very conception and its creation, Himalayan Bank Ltd, was as joint venture between the government and the private sector. Out of 2500 equity shares of NRs. 100 face value, 40% was subscribed by the government and the balanced i.e. 60% was offered for the sale to private sector. There were only 10 shareholders when

the bank first started. The total deposits for the first year was NRs. 17,02,025 where current deposits was about NRs. 12,98,898 fixed was about NRs. 3,88,964 and saving was NRs. 14,163. Loan disbursed and outstanding at the end of the first year was NRs. 1,985,000.

During the past 7 decades, the bank experienced many ups and downs, but it has remained the leading financial institution in Nepal. In early stage bank has provided its services to customers and government manually. Now, it has been using advanced technology to provide banking facilities. Himalayan Bank Limited has helped vastly in developing the country by accumulating the scattered money in small amount in each and every nook and corners of the country and granting loan and advances in various ways. The bank has been tendering modern banking services to the different sectors of the economy like manufacturing and service industries, hydropower projects, traders, small entrepreneurs and the weaker sections of the society through more than 110 branches which spread through all over the five development regions of the country. Himalayan Bank has introduced its ever waited HBL Debit Card by joining the hands with Smart Choice Technologies (SCT), the first company in Nepal to provide networked ATMs.

1.3 Focus of the Study

The study is focused on evaluating the deposit utilization of the sample banks, in terms of loans and advances, investment and its contribution to the profitability of the bank, commercial banks hold deposits of many individuals, government and business units. They make funds available through their lending and investing activities to borrowing individual business firms and government also to evaluate the inter-action of credit risk within a portfolio exposures (especially default correlation), and how these can be measured and quantified.

Here, the study focuses mainly to highlight and examine the credit portfolio of the selected joint ventures banks ignoring other aspects of bank transaction. To highlight the credit portfolio management of the bank, the research is based on the certain statistical tools i.e. mean, standard deviation, co-efficient of variation, coefficient of correlation,

and probable error with a view to find out the true picture of the bank. The main objective of this research is to analyze how credit portfolio modeling is used within risk management and regulatory and economic capital process.

1.4 Statement of the Problem

Commercial banks in Nepal have been facing various challenges and problems. Some of them arising due to the economic condition of the country, confused policy of government and many due to default borrowers. After liberalization of economy, banking sector has various opportunities.

However, the financial institutions are increasing regularly. Liquidity is in maximum level with the financial institutions. Hence, the banks and financial institutions are competing among themselves to advance credit to limited opportunity sectors. Banks and financial institutions are investing in house loan, hire purchase loan for safety purpose. Due to lack of good lending opportunities, banks are facing problems of liquidity. Currently, banks have increasing number of deposits in fixed and saving accounts but have decreasing trend in lending behaviors. So, this has caused major problems in commercial banks.

Nowadays, due to competition among banks, the interest rate charge for loan is in decreasing trend. Due to unhealthy competition among the banks, the recovery of the bank's credit is going towards negative trends. Non-performing credits of the banks are increasing year by year. To control such type of state, the regulatory body of the banks and financial institutions, NRB (Nepal Rastra Bank) has renewed its directives of the credit loss provision. Therefore, it is necessary to analyze the 'credit management' or credit disbursement recovery provision for loss and write off of the credit. As the sample of commercial banks, Himalayan Bank Limited and Nepal Arab Bank Limited have been selected.

The research problems may be stated in the form of following questions:

1. What is the level of liquidity in case of the sample banks?

2. What is the volume of credit and advances made by the sample banks?
3. What is the deposit collection and utilization trend of the sample banks?
4. What is the relationship of deposits, loan and advances and net profits of the sample banks?

1.5 Objectives of the Study

The main objective of this study is to examine the credit portfolio of NABIL Bank Limited and Himalayan Bank Limited. The specific objectives of the study are as follows:

1. To analyze the risk and return associated with the portfolio investment (i.e. investment on loans, advances and overdraft, company shares and treasury bills) of the selected commercial banks.
2. To evaluate the portfolio performance of the selected foreign joint venture commercial banks.

1.6 Significance of the Study

At present the joint venture banks are gaining a wide popularity through their efficient management and professional services and playing an eminent role in the economy. Lending is one of the main functions of commercial banks where the whole banking business is rested upon. Study on joint venture commercial bank and especially their lending practices; carry a great significance to shareholders of the bank, to the professionals, to the students who wants to know about lending practices of commercial banks. This study adds new ideas and findings about the concerned joint venture banks.

This study will have importance to various groups but in particular is directed to a certain groups of people/organizations, which are important to: i) shareholders, ii) management bodies of the bank for evaluation of bank's performance, iii) "outsiders" who are mainly customers, finance agencies, stock exchanges etc, iv) the government bodies or the policy makers such as central bank, v) interested outside parties such as investors, customers (depositors as well as credit takers), competitors, personnel of the banks, stockbrokers, dealers, market makers etc.

1.7 Limitations of the Study

To complete this research, the researcher follows the different books, journals, articles and dissertations. Thus, reliability of the study is based on those things. This study will not examine the credit portfolio of all commercial banks due to lack of time, the study will see only the credit portfolio of two foreign joint venture commercial banks NABIL Bank Limited and Himalayan Bank Limited.

This study will cover only the past five year's period since 2012/13 to 2016/17. To prepare this report, secondary data are collected from annual general meeting (AGM)'s reports of the listed banks and trading reports of NEPSE. Primary information is collected from respective office and related persons. It may not cover the whole qualitative and quantitative analysis of the commercial banks because of time and resource constraints.

The research study has some limitations. The main limitations of the study are as follows:

a. Though, several commercial banks have been established in Nepal, only two commercial banks are taken for the proposed study.
b. This study concentrates only on credit portfolio of selected commercial banks.
c. The secondary data will be used for presentation and interpretation. Only a five years data will be considered.
d. This study is only a case study; hence the conclusion drawn from the study does not ensure wide applicability in all types of enterprise running in different situations.
e. Major portion of analysis and interpretation have been done on the basis of available secondary data and information. Thus, reliability of the study is based on trueness of collected data and information.
f. In this study, only selected financial and statistical tools as well as techniques are used.

1.8 Organization of the Study

The present study is organized in such way that the stated objectives can easily be fulfilled. The structure of the study will try to analyze the study in a systematic way. The

study report has presented the systematic presentation and finding of the study. The study report is designed in five chapters which are as follows:

Chapter I: Introduction

This chapter describes the basic concept and background of the study. It has served orientation for readers to know about the basic information of the research area, various problems of the study, objectives of the study and need or significance of the study. It is oriented for readers for reporting giving them the perspective they need to understand the detailed information about coming chapter.

Chapter II: Review of Literature

Review of Literature is a way to discover what other research in the area of similar field has uncovered. Hence second chapter assures the reader to find out what research studies have been conducted in chosen field of study, and what remains to be done.

Chapter III: Research Methodology

Research methodology refers to the various sequential steps to be adopted by a researcher in studying a problem with certain objectives in view. It describes about the various source of data related with study and various tools and techniques employed for resenting the data.

Chapter IV: Data Presentation and Analysis

The general purpose of this chapter is to examine the processes by which the meaning and implications of research data can best be extracted. Hence, this chapter first explains methods of organizing data by tabulation and then placing in presentable data by using figures and tables & also major procedural steps involved in the analysis of data will be discussed.

Chapter V: Summary, Conclusions and Recommendations

On the basis of the results from data analysis, the researcher will conclude about the performance of the concerned organization for better improvement.

CHAPTER - II

REVIEW OF LITERATURE

2.4 Conceptual Framework

Basically, a bank is a financial institution which deals with deposit and advances and other related services which receives money from those who want to save in the form of deposits and it lends money to those who need it. Previously, the term Bank is derived from Latin word “Bancus”, French word “Banque” and Italian word “Banco”, referring to a Bench that displays coins of different countries on benches or tables, invests, exchanges and keeps record of funds and cash. These commercial and functional activities are regarded as banking activities. According to S. and S.'s definition of bank, "A banker or bank is a person/company carrying on the business of receiving money collecting drafts, for customers subject to the obligation of honoring cheques drawn upon them from time to time by the customers to the extent to the amount available on their customer" (Shekher and Shekher, 2005).

"A bank is an institution, usually incorporated with power to issue its promissory notes intended to circulate as money (known as bank notes); or to receive the money of others on general deposit, to form a joint fund that shall be used by the institution, for its own benefit, for one or more of the purposes of making temporary loans and discounts; of dealing in notes, foreign and domestic bills of exchange, coin, bullion, credits, and the remission of money; or with both these powers, and with the privileges, in addition to these basic powers, of receiving special deposits and making collections for the holders of negotiable paper, if the institution sees fit to engage in such business(USSC, 1899).

A banker takes deposit accounts, current accounts, issues and pay cheques of crossed and uncrossed for his customers. "The real business of the banker is to obtain deposits of money which he may use for his own profit by lending it out again" (In 1901, Justice Holmes wrote, in an Irish case (*Re Shields Estate*). Justic Atkin stated that Bankers never do make a payment to a customer in respect of a current account except upon demand. Hence, if banking activities are carried out by any person is subsidiary to some other business, he cannot be regarded as a banker, as stated by Paget. A bank refers to Central

bank, Commercial bank, Development bank, Exchange bank, Saving bank, Cooperative bank, Merchant bank, Agricultural bank, Tourism bank, Housing bank, Equipment bank, Infrastructure bank and Mutual fund etc. They provide financial as well as non-financial services. It is a financial mediator between depositors or lenders and withdrawal or loaner. A bank plays an immense role that helps investors to invest in different sectors by giving a loan and providing other consultancy and agency services.

2.4.1 Concept of Commercial Bank

An institution which accepts deposits makes business loans and offers related services. Commercial banks also allow for a variety of deposit accounts, such as checking, savings, and time deposit. These institutions are run to make a profit and owned by a group of individuals, yet some may be members of the Federal Reserve System. While commercial banks offer services to individuals, they are primarily concerned with receiving deposits and lending to businesses. Additionally, they provide short-term, medium term and long terms credit as well as issuance of guarantees, bonds, and letters of credit etc as various banking activities.

"A bank is an establishment which makes to individuals such advances of money as may be required and safely made, and to which individuals entrust money when not required by them for use." (Kinley)

Commercial bank being the financial institution performs diverse types of functions. It satisfies the financial needs of the sectors such as agriculture, industry, trade, communication, etc. That means they play very significant role in a process of economic social needs. The functions performed by banks are changing according to change in time and recently they are becoming customer centric and widening their functions.

Commercial banks serve as an intermediary indulgent in accepting deposits and providing credits to the required areas. The primary supply of funds for commercial banks are capital (shareholder equity) reserve (retain earning). Other major sources of commercial banks are current deposit, issues of commercial paper bonds etc. Commercial

banks, on the other hand, invest their funds in corporate securities. They invest their funds in long term as well as short-term needs of any trade and industry. They provide financial solutions in the form of cash credits and overdraft. Commercial banks pool scattered funds and channels it to productive utilization. Commercial banks apart from financing also deliver a variety of services like discounting of bills, collection of bills and cheques, safekeeping of precious physical valuables, financial advising, keeping of guarantee, Securitization of Loans etc to their valued customers.

In recent years, commercial banks, particularly in developing countries, have been called upon to help achieve certain socio-economic objectives laid down by the state. For example, the nationalized banks in India have framed special innovative schemes of credit to help small agriculturists, village and cottage industries, retailers, artisans, the self employed persons through loans and advances at concessional rates of interest. Under the Differential Interest Scheme (D.I.S.) the nationalized banks in India advance loans to persons belonging to scheduled tribes, tailors, rickshaw-walas, shoe-makers at the concessional rate of 4 per cent per annum. This does not cover even the cost of the funds made available to these priority sectors. Banking is, thus, being used to serve the national policy objectives of reducing inequalities of income and wealth, removal of poverty and elimination of unemployment in the country.

It is clear from the above that banks help development of trade and industry in the country. They encourage habits of thrift and saving. They help capital formation in the country. They lend money to traders and manufacturers. In the modern world, banks are to be considered not merely as dealers in money but also the leaders in economic development.

Table 2.1

List of Commercial Bank in Nepal

S.No.	Names	Operation Date (A.D.)	Head Office
1.	Nepal Bank Ltd.	1937/11/15	Kathmandu
2.	Rastriya Banijya Bank Ltd.	1966/01/23	Kathmandu
3.	Agriculture Development Bank Ltd.	1968/01/02	Kathmandu
4.	Nabil Bank Ltd.	1984/07/16	Kathmandu
5.	Nepal Investment Bank Ltd.	1986/02/27	Kathmandu
6.	Standard Chartered Bank Nepal Ltd..	1987/01/30	Kathmandu
7.	Himalayan Bank Ltd.	1993/01/18	Kathmandu
8.	Nepal SBI Bank Ltd.	1993/07/07	Kathmandu
9.	Nepal Bangladesh Bank Ltd.	1994/06/05	Kathmandu
10.	Everest Bank Ltd.	1994/10/18	Kathmandu
11.	Bank of Kathmandu Lumbeni Bank Ltd.	1995/03/12	Kathmandu
12.	Nepal Credit and Commerce Bank Ltd.	1996/10/14	Rupandehi
13.	Machhapuchhre Bank Ltd.	2000/10/03	Pokhara, Kaski
14.	Kumari Bank Ltd.	2001/04/03	Kathmandu
15.	Laxmi Bank Ltd.	2002/04/03	Birgunj, Parsa
16.	Siddhartha Bank Ltd.	2002/12/24	Kathmandu
17.	Global IME Bank Ltd.	2007/01/02	Birgunj, Parsa
18.	Citizens Bank International Ltd.	2007/06/21	Kathmandu
19.	Prime Commercial Bank Ltd	2007/09/24	Kathmandu
20.	Sunrise Bank Ltd.	2007/10/12	Kathmandu
21.	NIC Asia Bank Ltd.	2013/06/30	Kathmandu
22.	NMB Bank Ltd.	2008/06/05	Kathmandu
23	Prabhu Bank Ltd.	2009/05/07	Kathmandu
24	Janata Bank Nepal Ltd.	2010/04/05	Kathmandu
25	Mega Bank Nepal Ltd.	2010/07/23	Kantipath, Kathmandu
26	Civil Bank Ltd.	2014/15/26	Kamaladi, Kathmandu
27	Century Commercial Bank Ltd.	2011/03/10	Kathmandu
28.	Sanima Commercial Bank Ltd.	2012/02/26	Kathmandu

Source: www.nrb.org.np

2.4.2 Concept of Credit

A credit management is the blue print used by a bank or business in making its decision to extend credit to a customer. Thus, the main goal of a credit portfolio is to avoid extending credit to customers who are unable to pay their accounts.

Credit is the amount of money lent by a creditor (Bank) to the borrower (Customers) either on the basis of security or without security. A sum of money lent by a bank is known as credit (Oxford Advanced Learners Dictionary, 1992). Credit and advances is an important item on the asset side of the balance sheet of a commercial bank. Bank earns interest on credits and advances as one of its major sources of income. Bank prepares a credit portfolio to avoid bad debts and factors that affect profitability adversely (Varshney, 2004).

Credit portfolio policy is defined as the rules and guidelines established by top management that governs the company's credit department audits performance in the extension of credit privileges (Jim Franklin, 2010). It is simply a set of guidelines designed to minimize costs associated with credit while maximizing benefits from it. Credit portfolio policies entail the credit procedures, credit standards and credit terms.

Credit is a financial asset resulting from the delivery of cash or other assets by a lender to a borrower in return of an obligation to repay on specified time. A good credit portfolio policy should help management to attract and retain customers, without having negative impact on cash flow. Banks generally grant credit in four ways (Chhabra and Taneja, 2009) as follows:

2.4.3 Types of Credit

Overdraft

It is an extension of credit from a lending institution when an account reaches zero. An overdraft allows the individual to continue withdrawing money even if the account has no funds in it. Basically the bank allows people to borrow a set amount of money (www.investopedia.com)

Cash Credit

The credit is not given directly in cash but deposited account is being opened on the name of borrower and the amount credited to that account. Hence, every credit creates deposit.

Term Credit

It refers to money lent to borrowers in lump sum. It is a fundamental form of standard term debt financing having maturities of 1 to 8 years. Barely and Myers urge that bank credits with maturities exceeding 1 year are called term credits. The firm agrees to pay interest amount based on the bank’s prime rate and to repay principle on regular installments. Special procedure of principle payments over time can be agreed upon to meet the firm's special needs (Richard, 2004).

Working Capital Credit

Working capital denotes the difference between current liabilities. It is granted to the customers to meet their working capital gap for supporting production process. A natural process develops in funds to repay a working capital credit.

Priority or Deprived Sector Credit

The deprived sector credit policy is directed credit policy of Nepal Rastra Bank, which is designed to meet micro credit demand of poorer and weaker section of the country. This policy was introduced for commercial banks in 1990. Under this policy provision, commercial banks are liable to lend up to 3 percent of their total loan outstanding to deprived people. Since the inception various policy reforms are carried out to enhance the effectiveness of the policy and programs. Later, the policy was extended to development banks and finance companies also.

Hire Purchase Financing (Installment Credit)

Hire purchase credits are characterized by periodic repayment of principle and interest over the maturity of the credit. Goods are agreed to take on hire at a stated rental including their repayment of principle as well as interest with an option to purchase. A recent survey of commercial banks indicates those banks are planning to offer installment credits on a variable rate basis. It can be secured and unsecured as well as direct and indirect installment credits on a variable rate basis.

Housing Credit (Real Estate Credit)

Financial institutions also extend credit to their customers. It can be residential building, commercial complex, construction of warehouse etc. It is granted to those who have regular income or can earn revenue from housing project itself.

Project Credit

Project credit is granted to the customers as per project viability. The borrowers have to invest certain proportion to the project from their equity and the rest will be financed as project credit. Construction credit is a short-term credit made to developers for the purpose of completing proposed projects. Maturities on construction credits varies from 12 months to 4 to 5 years, depending on the construction credits range from 12 months to as long as 4 to 5 years, depending on the size of a particular project.

Credit Cards and Revolving Lines of Credit

Banks are increasingly utilizing cards and revolving lines of credit to create unsecured consumer credit. Revolving credit line lowers the cost of making credit since operating and processing costs are reduced. Centralized department processes revolving credits to reduce administration cost due to standardization. Continued borrowing arrangement enhances cost advantages. Once the credit line is established, the customer can borrow and repay according to his needs and the bank can provide the fund to the customer at lower cost.

Off-Balance Sheet Transaction

Bank guarantee and letter of credit refer to off balance sheet transactions of financial institution. It is also known as contingent liability. Contingent liability pinpoints the liability, which may or may not arise during the happening of certain event. Footnotes are kept as references to them instead of recording in the books of accounts. It is non-funded based remunerative facilities but riskier than the funded until adequate securities are not taken.

Bank Guarantee

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

Letter of Credit (L/C)

It is issued on behalf of the customer (buyer/importer) in favor of the exporter (seller) for the import of goods and services stating to pay certain sum of money on the submission of certain documents complying the stipulated terms and conditions as per the agreement of L/C. It is also known as importers letter of credit since the bank of importer do not open separate L/C for the trade of same commodities (Johnson, 2007).

2.4.4 Objectives of the Sound Credit Policy

The credit policy should be carefully established, properly communicated and executed effectively by the lending party. The key target of credit policy is to maintain effective credit portfolio and manage its entire procedure. Moreover, it is specified as follows:

To have Good Assets

Loans are risky assets although a bank invests most of its resources in granting loans and advances. Non-performing loans challenge the existence of a bank. It is merely the quality of assets that leads to liquidation of many banks in South East Asia. The purpose of sound loan policy is to protect depositors' interest and maximize returns to the shareholder by balancing liquidity and profitability.

To contribute to Economic Development

A sound credit policy is required to ensure that the loans are given to the productive sector, which contributes to capital formulation and employment generation?

To give guidance to Lending Officials

A borrower should be assured that there is no discrimination whether he deals with one officer or the other. A sound credit policy is crucial to achieve a uniform standard procedure throughout the organization.

To establish a Standard for Control

Every policy requires periodic follow-up to ensure its proper implementation. A sound credit policy helps to determine the variance between actual performance and practices and to take corrective actions. A sound policy is always flexible and works as a guideline. If the variation between the practice and policy is carefully observed, proper plan, execution and amendment of the policy will become inevitable.

2.4.5 Lending Criteria

While screening a credit application, 5 Cs are to be considered first as follows:

Character

Character is the analysis of the applicant in terms of his abilities to meet the obligations put forth by the lending party. For this analysis, generally the following documents are needed:

a. Memorandum and Article of Association
b. Registration certification
c. Tax registration certificate (Renewed)
d. Resolution to borrow
e. Authorization-person authorizing to deal with the bank
f. Reference of other lenders with whom the applicant has dealt in the past

Capacity

It describes the customer's ability to pay. It is measured by applicants past performance records and followed by physical observation. For this, an interview with applicant's customers/suppliers will further clarify the situation. Documents relating to this area are:

a. Certified balance sheet and profit and loss account for at least past 3 years.

b. References or other lenders with whom the applicant has dealt in the past

Capital

This indicates applicant's capacity to inject his own money. By capacity analysis, it can be concluded that whether borrower is true with lender’s money or injecting his own fund to the project. For capital analysis, financial statements, like certified balance sheet, profit and loss account is the only tools.

Collateral

Collateral is a borrower's pledge of specific property to a lender, to secure repayment of a loan. The collateral serves as protection for a lender against a borrower's default - that is, any borrower failing to pay the principal and interest under the terms of a loan obligation.

Conditions

Once the funding company is satisfied with the character, capacity, capital and collateral then a credit agreement (sanction letter) is issued in favor of the borrower stating conditions of the credit to which borrower’s acceptance is accepted.

2.4.6 Matters of Sound Lending Policy

Credit policies are set of objectives, standards and parameters to guide bank officers who grant loans and manage the loan portfolio. Thus, they are procedures, guidelines and rules designed to minimize costs associated with credit while maximizing the benefit from it (Ahimbishwe, 2002).The main objective of credit policy is to have an optimal investment in debtors that minimizes costs while maximizing benefits hence ensuring profitability and sustainability of microfinance institutions as commercial institutions.

“Decision regarding extension of credit, loan review, ALLL, and charge-offs are all important matters that should be addressed by written policies approved by the board of directors. Policies provide objective criteria for evaluating individual credit decision sand help promote consistency and stability in the lending function. In doing so, lending policies help a bank avoid pitfalls that may lead to loan problem”,(Federal Reserve Bank

of Kansas City). According to Federal Reserve Bank of Kansas City features of Sound lending policy are considered as under:

- Acceptable types of loans and loan collateral.
- Guidelines and methods to determine ALLL adequacy
- Proportion of loans by type (agriculture, commercial, consumer, real estate) in the loan portfolio and the maximum amount the bank will commit to a single borrower, groups of borrower, or industries.
- Geographic area in which the bank will ordinarily lend.
- Documentation requirements, acceptable financial ratios, and other factors considered by the bank in credit decisions.
- Collateral appraisal standards and who can perform appraisals.
- Pricing, structure, and other loan terms, including maximum loan term.
- Limits on renewals extensions, including specific criteria for additional lending to problem borrowers.
- Periodic review, inspection, and administration of loans and charging of loans.
- Procedures for exceptions to the loan policy.
- Requirements and limitation on loans to "insiders” and their related interests.
- Compliance with consumer protection, fair lending and community reinvestment laws.
- Internal loan review program.
- Regards to the board of directors
- Loan policy review by the board of directors.

2.4.7 Principles of Credit Policy

Good credit policy is crucial to carry out credit process more effectively. Some policies are as follows

Principle of Safety Fund

Banks should consider the safety of fund to be lent and scrutinize whether there are any unproductive or speculative ventures or dishonest behaviors of the borrower.

Principle of Liquidity

Liquidity refers to ability to pay cash on hands when needed without having to sell long term assets at loss in unfavorable market. A banker has to ensure that money will come in as on demand or as per agreed terms of repayment.

Principle of Security

It serves as a support to grant advances and credits. Adequate values of collateral and securities ensure the recovery of credit accurately at the right time. Received or approves security should be readily marketable, handy and free from hindrances.

Principle of Purpose of Credit

Generally, credit request should be accepted for productive sector only. Banks should decline credit request for speculation, social functions, pleasures trips, ceremonies and repayment of prior credit as they are fruitless.

Principle of Profitability

Profitability denotes the value created by the use of resources more than the total input resources. Bank should provide credit to projects that can provide optimum amount of return. For such purpose, bank should take minimum risk by providing credit for a venturous project.

2.4.8 Lending / Credit Process

Commercial banks follow various steps to disburse loan to their borrowers. The lending policies might be different from one bank to another. Typically, these steps can be as follows.

Application

Borrowers are required to submit an application to the bank along with required documents. The documents required for credit proposal appraisal and processing by banks are as follows:

- Loan application
- Citizenship certificate of applicant
- Firm/ company registration certificate (if self employed)
- Income tax registration certificate (if self employed)

- Authenticated partnership deed in case of partnership firm, and memorandum and article of association in case of company
- Attested copy of board resolution in case of company resolved to avail loan and banking facilities form bank against the pledge, hypothecation, and mortgage of fixed property owned by company or property of third party named.
- Letter of authority authorizing to sign loan deed and other relevant document paper which are deemed necessary while dealing with bank on behalf of firm/company
- Feasibility report/scheme (for new project)

Lending Appraisal and Possessing

Basically, appraisal of loan proposal is for the review of variability of the scheme proposed. It also helps to benefit the actual financial assistance required to run the scheme. Commercial banks perform loan appraisal on the strength of past performance, future projection and information obtainable from the documents submitted by aspirant borrowers.

Banks aim to ascertain the following during loan processing:

- The cost of estimate examined so that the appropriate estimate can be accepted. Under and over estimates are rejected. Similarly, the specification of machinery should be proper.
- Working capital projection has to be reasonable as compared to past performance and on the basis of target for future expansion.
- The return rates should be adequate like Return on Investment (ROI), Internal Rate of Return (IRR) and Debt Service Coverage Ratio (DSCR).
- The capacity, competency and commitment of promoters, partners, proprietors, directors, and personnel should be integral.
- SWOT (Strength, Weakness, Opportunity and Threat) analysis of the proposed project must give reasonable assurance.

2.4.9 Project Appraisal

Before providing credit to the customer, a bank makes analysis of project from various aspects. It helps the bank to see whether project is really suitable to invest. The purpose

of project appraisal is to achieve the guarantee of reasonable return from the project. Project appraisal answers the following questions:

- Is the project technically sound?
- Is the project in line with overall economic objectives of the country?
- Will the project provide a reasonable return?

Generally, the project appraisal involves investigation from the following aspects (Gautam 2004), as

- Economic aspect
- Management /organizational aspect
- Legal aspect
- Financial aspect

Credit Classification and Provisioning

Classification	Provision
Pass Credit	1%
Sub Standard Credit	25%
Doubtful Credit	50%
Bad Credit	100%

Source: NRB Directives 2017

Those credits that have not crossed the time schedule of repayment and are within three months delay of maturity date fall under the classification topic “pass credit”. It is also known as performing credit.

Sub standard credit are those credit which are already crossed the repayment time schedule and are within 3-6 months delay of maturity date. Likewise, within 6-12 months from the time to be recovered are classified as doubtful credit. Those credits, which are not recovered yet after 1 year from maturity date, are known as bad credit. All the above 3 types of credits are classified as non-performing credit also. The credit loss provision

for performing credit is termed as general credit loss provision whereas the credit loss provision for non-performing credit is termed as specific credit loss provision.

Auditor has to correctly rate the credit and ensure that accurate credit loss provision has been made. The auditor should examine whether the bank has obtained complete documentation so that bank interest is secured. In addition, audit is made to inspect compliance of terms and conditions laid down. Credit audit is required to check whether credit given is within authority, drawing power, etc. Credit audit helps the bank to know quality of its credit, its weakness and strengths. This, in turn, helps the bank to adopt corrective measures where weaknesses have been pointed out and to focus further on strengths. General guidelines whether to reject or renew the credit can be established with the help of credit audit.

Limit of Credit and Advances in a Particular Sector

- Fund based credit and advances can be issued up to 25% (upper limit) of core capital to a single customer, firm, company and a group of related customer.
- Non-fund based (off-balance items) can be issued up to 50% of core capital to a single customer, firm, company and group of related customer.

Note: The core capital includes {paid up capital + share premium + nonredeemable preference share + general fund + accumulated profit (loss) – goodwill (if any included)}.

Group of Related Customer

- If a company takes 25% or more share of another company.
- Member of board of directors of company shareholders of private limited company and such members and shareholders with others in a single house, even if husband, wife, son, daughter, daughter in law, unmarried daughter, adopted son, adopted unmarried daughter, father, mother, stepmother, brothers and sisters whom be should look after. And the above members personally or combined take 25% or more share of another company.
- Firm, company and members as a related group

- Members of board of directors, shareholders and other relatives as stated in serial number “b” takes less than 25% of board of directors of the company solely or combined but have control on the other company by the following ways:
    a. Being president of board of directors of the company.
    b. Being executive directors of the company.
    c. Nominating more than 25% of members of board of directors of the company.
    d. If cross guarantee is given by one company to another company.

2.5 Review of Regulatory Directives

Bank and Financial Institution Act, 2017 have reviewed in this segment. After February 4, 2004 the ordinance relating bank and financial institutions has been promulgated. The ordinance is popularly called an umbrella act as it reveals and replaces all existing Acts relating to commercial banks, NIDC, other Development banks and finance companies and brings all such institutions under the purview of a single act. Same ordinance was made act by the parliament in 2063 as BAFIA, 2063. It was supposed to be complied since 2063. The act is divided into 12 chapters and contains altogether 94 sections. Provision regarding Credit disbursement and its recovery procedures are mentioned in chapter 8 that re-establishes the NRB’s authority to regulate lending and minimize the chances of loan going to an unscrupulous or diversion of funds.

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

1. Provision for Minimum Capital Fund

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

Table 2.3

Provision for Minimum Capital Fund

Institution	Minimum Capital Fund to Total Risk Weighted Assests	
	Core Capital	Capital Fund
For "A"	6.00%	10.00%
For "B" & "C"	5.5%	11.00%
For "D"	4.00%	8.00%

Source: NRB Directives 2017

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

2. Provision for Credit in the Deprived Sector

Banks should lend 3 percent of total loan and advances to deprive sector as per directives. This provision was imposed to commercial banks only in past but extended it to development banks, "B" class financial institutions, also since fiscal year 2064/065 according to monetary policy 2064-065 published by regulatory body, Nepal Rastra Bank.

3. Provision for Credit to the Priority Sector

NRB requires commercial banks, development banks and finance companies to extend certain percent of total loan and advances to the priority sector/deprived sector. Commercial banks credit to the deprived sector is also a part of priority sector credit. As per the NRB Directive, 2017 percentage of loans and advances required to be flowed in the deprived sector are as follows:-

Class	**Percentage**
Commercial Bank ("A" Class)	3.5%
Development Bank ("B" Class)	3.0%
Finance Companies	2.5%

As per the NRB Directive, 2017 following sectors fall under the deprived sectors:-

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

4. Provision for the Investment in Productive Sector

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

5. Provision for the Single Borrower Credit Limit

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

Licensed institution may extend to a single borrower or group or related borrowers the amount of fund based loans and advances upto 25 percent of the core capital fund and non-fund based (off balance sheet facilities like letter of credit, guarantees, acceptances, commitments) up to 50% of its core capital fund. Fixation of limit on credit and facilities to single borrower shall be made on the basis of core capital fund as per the latest quarterly balance sheet certified by the internal auditor of concerned institution. The fund based loan and non-fund based facilities are separate and accordingly the single borrower limit shall not be calculated by aggregating the both. According to monetary policy 2068-69, the amount and percentage limit can be addition for hydropower projects.

ii. For "D" Class Licensed Institution

Credit to the deprived and low income people may be extended a maximum of up to Rs.60, 000 per group member/individual for operation of micro business and not more than Rs.150,000 per each micro enterprise to be provided on a gradual basis to the group

member for operation of micro enterprise against acceptable collateral. (Monetary Policy, 2068-69 NRB). However, the institution shall extend such- enterprise credit up to 25 percent of the total loans and advances.

6. Cash Reserve Requirement

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

7. Loan Classification and Loan Loss Provision

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

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

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

Table 2.4

Classification of Loan and Required Provisioning

Classification of Loans	Defined as	Criteria	Loans Loss Provision
Pass or Good	Performing Loan	Due upto 3 months	1%
Sub-Standard	Non-Performing Loan	Due upto 3-6 months	25%
Doubtful	Non-Performing Loan	Due upto 6-12 months	50%
Bad	Non-Performing Loan	Due upto 12 months	100%

Source : NRB Directives

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

2.6 Review of Related Studies

2.3.1 Review of Books

The book entitled ***"**Banking Management**"*** says that in banking sector or transaction an unavailability of loan management and its methodology is regarded very important. Under this management many subject matters are considered and thought for example there are subject matters like the policy of loan flow, the documents of loan flow, loan administration, audit of loan, renewal of loan, the condition of loan flow, the provision of security, the provision of the payment of capital and it's interest and other such procedures. This management plays a great role in healthy competitive activities. (Bhandari, 2003) yet another dubbed as: loan and advances dominate the asset side of the 'Balance Sheet' at any bank. Similarly earnings from such loan and advance occupy a major space in income statement of the bank. Lending can be said to be the visor of bank. However, it is very important to be denuded that most of the bank failures in the world are due to shrinkage in the value of loan and advances. Hence, risk of non-payment of loan is known as credit risk or default risk (Dahal, 2002)

Crosse (2003) has mentioned in his book *"Management Policies for Commercial Banks",* that lending is essence of commercial banking, consequently the formulation and implementation of sound lending policies are among the most important responsibilities of bank directors and management. Well conceived lending policies and careful lending practices are essentials if a bank is to perform its credit creating function effectively and minimize the risk inherent in any extension of credit. Before formulation a lending policy, many factors have to be taken into consideration because banks are not the real owners of deposits but rather the custodians of money.

Reed, Cotter, Gill and Smith (2006) in their book entitled *"Commercial Banking"* focus on the importance of loan in banking sector. As per their view, loan are the most important asset held by banks and bank lending provides the bulk of band income. Lending is not only important to the bank only, it is equally important to the community the bank serves. That's why loan policies must be worked out carefully after considering many factors.

Klisse (2007) gives his view in his book ***"****Money and Banking****"*** that in an economy that depends more and more on credit, banks find themselves lending for a variety of purposes, sometimes directly, sometimes through other agencies. This wider use of loan is not due merely to a change in attitude of the banks. It reflets also more fundamental changes such as shifts in the public's consumption patterns and in financial investment policies.

Gitman and Joehk (2008) in their book *"Fundamentals of Investing"* compare the bank investment with a vehicle. He says that it is such vehicle into which funds can be placed with the expectation that will preserve or inverse in a value and generates positive results. A banker seeks optimum combination of earning, liquidity and safety while formulating policy.

Singh and Singh (2009) put forth their view in their book entitled *"Financial Analysis for Credit Management in Banks"* that the investment (credit) policies of bank are conditioned to great extent by the national policy framework, every banker has to apply his own judgement for arriving at a credit decision, keeping his bank's credit policy also in mind.

As inference from all these above stated authors it can be said that loan management refers to systematic identification of needy one or required party (loan taker), verifying their documents, pre and post site visit, disbursement of loan keeping collateral as

cushion for giver and post disbursement inspection cum sound recovery of granted loan as far as practicable.

2.3.2 Review of Journal, Reports and Article

Duchassi, Shawk and Seagle (2012) have showed Commercial Loan Analysis Support System(CLASS) in their article *"A knowledge-Engineered System for Commercial Loan Decisions"*. This article describe an expert system, commercial loan analysis support system(CLASS) is an expert system designed to evaluate a company's financial posture, recommend commercial loan decision and pertinent components, and document loan analysis. Like a loan officer, CLASS constituently synthetics a large number of detailed facts into a loan recommendation. CLASS has been designed to seek our any potential weakness in the prospective borrower and conduct an extensive detailed analysis of each weakness. Weakness may be over analysed but none will be overlooked. This approach is consistent with the general notion in commercial lending that one is primarily concerned with weaknesses instead of strong points which are taken for granted. In addition to the limited validation conducted by the experts a more comprehensive validation can be implemented in two ways. First, the system can be empirically tasted with a large sample of historical loan decisions. Second, field tested can be conducted in which loan officer use CLASS while making actual loan decisions. Their judgements can be compared to those of CLASS at each step in the analysis. By building CLASS, it was demonstrated that financial knowledge can be represented and applied to a complex financial problem. It is hoped that the approached described will pave the way for building expert systems that address other important financial problems.

Gautam, (2013), in the article ***"Credit Sector Reform and NRB"*** has tried to highlight the effects of change or amendment in NRB directives regarding loan classification and loan loss provisioning. "Although the circumstances lending to financial problem or crisis in many Nepali banks differ in many respects, what is common among most of the banks is the increased size of non-performing assers (NPAs), to resolve the problem of the losses of likely losses of this nature facing the industry. NRB, as the central bank, has amended several old directives and issued many new circulars in the recent years.

The Nepalese banking system is riddled with a significant amount of non-performing assets (NPA). Despite a slowdown in real estate and Capital market, the non-performing loan (NPL) of BFI's has increased marginally due to improved policies on credit expansion and its recovery. The NPL of commercial banks, which was 3.2 percent in mid-April 2011, reached 3.5 percent in mid-April 2012. The NPL of Himalayan Bank Limited and Rastriya Banjiya Bank Limited which were under Financial Sector Reform Program stated at 5.9 percent and 10.6 percent respectively in mid-April 2012. The NPL of these two banks were 5.3 and 10.9 percent respectively in mid-July 2011.

Crosby, French and Oughton (2014), in the article ***"****Banking lending valuations on commercial property**"*** had concluded that the banking community are trying to identify the value on which they can apply a loan value ratio and thus protect their loan in the future should the borrower default. A simplistic understanding the value therefore suggest that figure provided should be the figure which has a life for the length of the loan. However, the very concept is economically impossible in any market with volatility. Values can only be snapshots in time. They do not have self life.

For this reason EMLV is conceptually and practically redundant in real estate markets. It appears on the surface to be a solution to the bank's requirement for the reduced risk property lending. In reality, it may indeed transfer that risk by demanding a level of protection to the bank that the valuation cannot give. But if values agree to it, it could open the way to successful negligence claims in the aftermath of poor lending decisions. This is because the concept appears the determinants of the virtually certain level of value below which the value will not fall for an indeterminate time into the future. Values are vulnerable to claims that their valuation was too high, should values fall below that level at any time during the loan. Sustainable value is predictated on having a shelf life but the application believes this fundamental requirement. Values must have a time point. The concept is redundant, the target unidentifiable and the definition ambigious. It is little wonder that the application appears mechanistic. Market value is an obtainable and useful piece of information to the lender. Worth in the market sets this in context and gives the

lender a view of whether market prices are at current sustainable levels. In obtaining worth, the value is obliged to carry out both quantitative and qualitative investigation into the future and this generates other analyses at different time points during the course of the loan.

EMLV appears to be another blind alley which will divert the appraisal profession from its more important task of improving pricing estimates, and thereby influencing market prices, and providing all clients, whatever the valuation purpose, with the information in reports which puts the limitations of valuation figure into perspective.

Mundul, (2015), in the article *"Understanding of credit derivative, Business Age September*" emphasis Credit derivative enable financial institution and companies to transfer credit risk to a third party and thymus reduce their exposure to the risk of an obligor's default. Credit enhancement technique, which helps reduce the credit risk of an obligation, plays a key role in encouraging loans and investment in debts. In legal term credit derivative are privately negotiated bilateral contract to transfer credit risk from one party to another. Some credit enhancement methodologies have existed for the debts. Some credit enhancement methodologies have existed for a longtime with the support of guarantee, letter of credit or insurance product. However, such mechanism works best during economic upturns. As an alternative to commercial risk mechanism, various financial mechanisms have been developed over the past few decades. Such credit risks instruments are normally refers to as credit derivatives. Credit derivative helps to transfer credit risk away from the lender to some other party. Now, credit derivative grew popular both as tool for hedging credit risk exposure as well as method of investing in certain types of credit risk.

Credit derivative not only helps corporation and financial institution to manage to their credit risk but also enabled a new set of individual retail client to invest in bonds and stocks previously unaffordable. Through credit derivative individual investor isolated credit, and transfer it to other investor who are better suited to managing it or who finds

the investment opportunity more intresting. There are many credit instruments in the market. They are:

- Total Return Swap (TRS)
- Credit Default Swaps(CDS)
- Credit Linked Notes (CLN)
- Credit Spread Option (CSO)

According to the behaviour of the asset or deal above credit instrument can be used and minimizing the risk. In this way credit derivative provide protection against credit risk.

Nario, Pfister, Poppensieker, and Stegemann (2016) in the article, "*The evolving role of credit portfolio management*" relates with the Credit Portfolio Management evolvement. Credit Portfolio Management is a key function for banks (and other financial institutions, including insurers and institutional investors) with large, multifaceted portfolios of credit, often including illiquid loans. Historically, its role has been to understand the institution's aggregate credit risk, improve returns on those risks, sometimes by trading loans in the secondary market, and hedging and identifying and managing concentrations of risk. In contrast to traditional origination and credit risk-management functions that look only at individual deals or borrowers, CPM looks across the entire credit book.

The article mainly identified three main reasons for the change of CPM's role.

a. Capital and liquidity constraints

b. Increasing cost and margin pressure

c. Changing market conditions

Jeon, J.J 2017, in the article" *Portfolio credit risk model with extremal dependence of defaults and random recovery"* deals with portfolio credit risk modelling, taking into account the extremal dependence of defaults and random recoveries. The article propose to model a credit portfolio using a factor copula model with random recovery rates and

develop an efficient importance sampling conditional Monte Carlo in order to compute the loss probability.

2.3.3 Review of Previous Thesis

Sejuwal (2009), had conducted a comparative study on "*Credit management of commercial Banks, with reference to Nabi Bank Ltd and SCB Nepal Ltd". *The main objective of the research study was:

- To assess the credit practice and credit efficiency of the selected commercial banks.
- To explore the relationship between loan and advances, non-performing loan and net profit of the selected commercial banks.

Out of the total commercial banks in Nepal only 2 commercial banks were selected i.e. Nabil Bank Ltd and SCB Nepal Ltd was selected as sample. Ratio analysis, Standard deviation, Correlation analysis and Probable error were used as a financial and statistical tool to analyze the study.

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

Basnet (2010) conducted the study on *"Credit management of Rastriya Banijya Bank Limited"*. The main objectives of this study are stated as:

- To analyse the position of loan and advances and recovery status of the Rastriya Banijya Bank.
- To identify the strength and weakness of the credit administration of the bank.
- To offer suitable suggestions based on findings of this study.

Different tool and techniques were used by the researcher to analyse the data namely: financial tools (ratio analyses) and statistical tools (mean, standard deviation, correlation and coefficient of determination.

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

Limbu, A. (2011), in a study *"Credit Management of NABIL Bank Limited"* concluded that increasing total deposit will have positive impact towards loan and advances. The study highlighted the aggregate performance and condition of NABIL Bank Limited. The main objectives of the research study are :

- To evaluate various financial ratio of the Nabil Bank.
- To analyze the portfolio of lending of selected sectors of banks.
- To determine the impact of deposit in liquidity and its effect on lending practices.
- To offer suitable suggestions based on finding of this study.

In the statistical tools analysis, average mean, correlation analysis and trend analysis have been calculated. In the aspect of liquidity position, cash and bank balance reserve ratio shows the more liquidity position. Cash and Bank balance to total deposit has fluctuating trend in 5 years study period. Cash and Bank balance to current deposit is also fluctuating. The average mean of Cash and Bank balance to interest sensitive ratio is able to maintain good financial condition. Correlation coefficient between total credit and total assets shows high degree of positive correlation. Correlation coefficient between total deposit and loan and advance has high degree of positive correlation.

Misra, J. (2012), in a study "*Credit management of Everest Bank Limited"* illustrate that liquidity position, cash reserve ratio shows the more liquidity position. Cash and bank balance to interest sensitive ratio shows the bank is able to maintain good financial condition. Cash and bank balance to current assets ratio shows that the bank's sound ability to meet the daily cash requirement of their customers deposit. That is why liquidity position of the bank is better.

In the aspect of profitability position, interest income to interest expenses ratio shows the more profitable salivation. In addition, total income to total expenses ratio shows the

overall predominance of the bank is satisfactory operating income. Return on loan advances are showing position that is more profitable on of the EBL bank. Analysis of the assets management ratio, loan advances to total assets ratio shows the better performance but loan and advanes to total deposit position in minimum than the averages. Whereas investment in loan and advances is safely and not taking more risk. That's why assets management position of the bank shows better performance in the latest year.

Rajkar, S. (2013), had conducted the study on "*The Loan management of Himalayan Bank Limited*". The main purpose of the study was:

- To analyse the efficiency of the selected banks in terms of loan management.
- To analyse the non-performing loan in terms of growth rate of loan outstanding, loan recovery, loan investment and provisions made.
- To offer suitable suggestions based on the findings of this study.

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

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

Thapa (2014) , analysed the "*Credit management and practices of Rastriya Banijya Bank Ltd*". The main objectives of the research study were:

- To assess the credit practices.
- To assess the efficiency and current position of Rastriya Banijya Bank Ltd.

- To analyze the ratio of credit invested in different sectors and securities.

Out of the total commercial banks of Nepal, Rastriya Banijya Bank Ltd was selected for the study purpose. Various financial tools and statistical tools (mean, Standard deviation and correlation) were used to analyze the findings of the study.

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

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

Satyal (2015), had conducted the study on "*The Credit Practices of Nabil Bank Ltd, SCB Nepal Ltd and Himalayan Bank Ltd".* The major objectives of the study was:

- To measure the credit performances in quality, efficiency and its contribution in total income.
- To determine the liquidity position
- To determine the impact of deposit in liquidity and its effect on credit practices.

Nabil Bank Ltd, SCB Nepal Ltd and Himalayan Bank Ltd were selected as sample for the study among the total commercial banks of Nepal. Portfolio analysis, Ratio analysis, comparative analysi were used as the tools to analyze the study.

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

Shrestha. S, (2016), conducted a study on "*Credit risk management of Nabil Bank Limited and Nepal Investment Bank Limited in Nepal"*. The main objective of the study is to evaluate the credit risk management. In order to achieve this, specific objectives have been formulated.

- The main objective of the research study is to evaluate the status of the loan portfolio of the banks.
- To evaluate problems and weakness in credit risk management.
- To review the prevailing laws rules and regulation enforced by Nepal Rastra Bank and assess its impact on profitability and liquidity of bank.
- To offer suitable suggestions based on findings of this study.

The profitability position of Nabil and NIB are: Return on loan and advances ratio of Nabil is higher than that of NIB i.e 4.64% > 2.46%. Return on total asssets ratio of Nabil is slightly higher than NIB i.e. 2.61% > 1.79%. However, Nabil seems successful in managing and utilizing the available assets in order to generate revenue.

The credit risk ratio shows the proportion of non-performing loan in total loan and advances. Average credit risk ratio of NIB is higher than Nabil. These ratios indicate the more efficient operating of credit management of both banks according to NRB directives because according to NRB directives NPL ratio must be less than 5%. The liquidity risk of the bank defines its liquidity need for deposit. The average mean ratio of NIB is greater than that of Nabil. The analysis shows that both banks have the assets risk ratio on fluctuating trend.

2.7 Research Gap

The review of above relevant literature has contributed to enhance the fundamental understanding and knowledge, which is required to make this study meaningful and purposeful. There are various researchers conduct on lending practice, credit policy, financial performance and credit portfolio of various commercial banks. Some of the researchers have done the financial performance, credit policy between two or three different commercial bank. In order to perform those analysis researchers have used

various ratio analysis. Actually, credit portfolio is determined by various factors. In this research various ratio are systematically analyzed and generalized. Past Researchers are not properly analyzed about lending and its impact on the profitability.

Here in this research all ratios are categorized according to their area and nature. In this study of credit portfolio of Himalayan Bank Limited is measuring by various ratios, trend analysis and various statistical tools as well and financial tools are used for analyzing survey data. Since the researcher have used data only five fiscal year but all the data are current and fact. Clearly these are the issue in Nepalese commercial bank the previous scholar could not present facts. Thesis of Misra, (2009) “Credit portfolio management of Everest Bank Limited” has not use correlation, probable error and trend analysis. Limbu (2009) “Credit portfolio management of NABIL Bank Limited” has done using all financial as well as statistical tools.

This study tries to define credit portfolio management by applying and analyzing various financial tools like liquidity ratio, leverage ratio, profitability ratio and lending efficiency ratio as well as different statistical tools like coefficient of correlation and trend analysis. Probably this will be the appropriate research in the area of credit portfolio management of Bank and financial institutions.

CHAPTER - III
RESEARCH METHODOLOGY

Research methodology is a way to systematically solve the research problem. It may be understood as a science of studying how research is done scientifically. In research methodology the researchers study the various steps that are generally adopted by a researcher in studying his/her research problem along with the logic behind them.

3.6 Research Design

The word "Research" is derived from French word "Researcher" which means to seek again. Therefore to seek and compare the concerned banks for the case study, the research is designed as per objectives of the study.

"Research designs are plans and the procedures for research that span the decisions from broad assumptions to detailed methods of data collection and analysis. This plan involves several decisions, and they need not be taken in the order in which they make sense to me and order of their presentation here. The overall decision involves which design should be used to study a topic. Informing this decision should be the worldview assumptions the researcher brings to the study; procedures of inquiry (called strategies): and specific methods of data collection, analysis and interpretation. The selection of a research design is also based on the nature of the research problem or issue bring addressed, the researchers' personal experiences, and the audiences for the study" (Creswell, 2009).

The present study follows the descriptive as well as investigative design to meet the stated objectives of the study. The research design then focuses on the data-collection methods, the research mechanisms, and the sampling plan to be followed.

3.7 Nature and Sources of Data

Secondary sources data have been collected in order to achieve the real and actual results.

i. Secondary Sources of Data

Secondary data are indispensable for much of organizational research. Secondary data are compiled data that are taken from several primary sources and synthesized or summarized. The several sources of such data are:

- Published sources: Reports published by NRB; annual reports, prospectus & brochures etc of concerned banks; laws, guidelines and directives regarding the subject matter; articles published in newspapers, journals, magazines and other publications; bulletins and publications; text books regarding the subject matter etc.
- Unpublished sources: Records maintained by banks for their internal purpose; other related websites and internet sources; unpublished thesis and dissertations

The study is based highly on secondary data and besides secondary data, primary data such as questionnaire and interview method also can be used.

3.8 Population and Sample

Population or universe refers to the entire group of people, events or things of interest that the researcher wishes to investigate. A small segment chosen from the whole population for reviewing its features is called sample. The sample represents the total population. The method of selecting a small portion of the population to study and draw conclusions about the population is known as sampling. Sampling may be defined as the selection on part of the population on the basis of which a judgment or inference about the universe is made (Sharma and Chaudhary, 2058).

Here, the total 31commercial banks shall constitute the population of the data and single bank under the study constitute the sample under the study. So among the various commercial banks in the banking industry, Here NABIL and HBL have been selected as samples for the present study.

3.9 Data Collection Procedure

Chiefly, the annual reports from website of sample banks are taken as main source of data collection. Sources for data and substance availability are NRB publications such as economic reports and bulletins, banking and financial statistics, annual reports of NRB, website of NRB and Nepal share market.

3.10 Methods of Data Analysis

Collected data need to be presented, edited, tabulated and analyzed. The data should be presented not only in the systematic form but also be calculated in systematic way to get the desired output relating to the subject matter to achieve the basic objectives. On the basis of analyzed data, specific conclusions of the study are made. Two basic data analysis tools are used. The researcher uses two types of tool for analysis as,

- Financial Analysis.
- Statistical Analysis.

1.8.1 Financial Tools

Stakeholders of a business firm perform numerous analyses and reviews about financial statements of a particular bank. All of these analyses rely on comparison and quality of information that improve the utility or practical value of accounting data.

1.8.1.1 Ratio Analysis

Ratio-analysis means the process of computing, determining and presenting the relationship of related items and groups of items of the financial statements. They provide in a summarized and concise form of fairly good idea about the financial position of a unit. They are important tools for financial analysis.

Ratio Analysis as a tool possesses several important features. The data, which are provided by financial statements, are readily available. The computation of ratios facilitates the comparison of firms which differ in size. Ratios can be used to compare a firm's financial performance with industry averages. In addition, ratios can be used in a form of trend analysis to identify areas where performance has improved or deteriorated over time. Thus ratio analysis is useful to evaluate, judgment and taking proper decisions.

A. Liquidity Ratio

Liquidity refers to the ability of a firm to meet its short-term or current obligations. So liquidity ratios are used to measure the ability of a firm to meet its short-term obligations and from them the present cash solvency as well as ability to remain solvent in the event of adversities of the same can be examined (Van Horne, 1999).

Insufficient liquidity can lead to unexpected cash short falls that must be covered at inordinate costs, thus reducing profitability. It can lead to the liquidity insolvency of the institution. On the other hand, extreme liquidity can lead to low asset yields and contribute to poor earnings performance. To find out the ability of bank to meet their short-term obligations, which are likely to mature in the short period, these ratios are calculated. The following ratios are developed under the liquidity ratios to identify the liquidity position.

i. Current Ratio

Current ratio is an indication of a company's ability to meet short-term debt obligations; the higher the ratio, the more liquid the company is. Current ratio is equal to current assets divided by current liabilities. If the current assets of a company are more than twice the current liabilities, then that company is generally considered to have good short-term financial strength. If current liabilities exceed current assets, then the company may have problems meeting its short-term obligations.

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

Current assets can be converted into cash within a year and so it includes cash and bank balance, investment in treasury bills, bills purchased and discounted, customer acceptances liabilities, prepaid expenses, bills for collection, likewise current liabilities denotes current account deposits, saving account deposits, margin deposits, bills payable, call deposits, bank overdraft, interbank reconciliation account, provisions, customer's acceptance liabilities etc.

ii. Cash and Bank Balance to Total Deposit Ratio

Cash and bank balance are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make instant payment to the depositors. Both higher and lower ratios are not desirable. The reason is that if bank maintains higher ratio of cash, it has to pay interest on deposits and some earnings may be lost. In contrast, if a bank maintains low ratio of cash, it may fail to make payment for the demands of depositors. So, sufficient and appropriate cash reserve should be maintained properly. This ratio shows the ability of banks' immediate funds to cover their deposit. Higher the ratio, higher the liquidity position and ability to cover the deposits, and vice versa. This ratio can be calculated using the following formula:

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

iii. Cash and Bank Balance to Current Deposit Ratio

Cash and bank balance are the most liquid current assets. This ratio measures the percentage of most liquid fund with the current deposit. Higher ratio indicates a bank's sound ability to meet the daily cash requirement of their customer's deposit. If bank maintain low ratio, the bank may not able to make the payment of against cheques. So the bank has to maintain cash and bank balance to current ratio properly. This ratio is computed to disclose the soundness of company to pay total calls made of current deposits. This ratio can be calculated using the following formula:

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

iv. Cash and Bank Balance to Interest Sensitive Deposit Ratio

Saving deposit is deposited by public in a bank with an objective of increasing their wealth where interest rate plays significant role in the flow of interest sensitive deposit. Fixed and current deposits are not interest sensitive. Fixed deposits have a fixed term to maturity and current deposits are not sensitive toward interest rate. The ratio of cash and bank balance to interest sensitive deposits measure the bank ability to meet its sudden outflow of interest sensitive deposits due to the change in interest rate. This ratio can be calculated using the following formula:

Cash and Bank Balance to Interest Sensitive Deposit Ratio= $\frac{\text{Cash and Bank Balance}}{\text{Saving Deposit}}$

B. Activity/Efficiency Ratio

It is also known as turnover or efficiency ratio or assets management ratio; measures how efficiently a firm employs its assets and resources. Turnover refers to the number of times the assets flow through a firm's operations and into sales (Kulkarni, 2006). Greater rate of turnover or conversion indicates more efficiency of a firm in managing and utilizing its assets, being other things equal. Various ratios are examined under this heading.

i. Loan and Advances to Total Deposit Ratio

A lending institution that accepts deposits must have a certain measure of liquidity to maintain its normal daily operations. Loans given to its customers are mostly not considered liquid meaning that they are investments over a longer period of time. Although a bank will keep a certain level of mandatory reserves, they may also choose to keep a percentage of their non-lending investing in short term securities to ensure that any monies needed can be accessed in the short term. This ratio can be calculated using the following formula:

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

ii. Loan and Advances to Total Assets Ratio

The loans to assets ratio measure the total loans outstanding as a percentage of total assets. The higher this ratio indicates a bank is loaned up and its liquidity is low. The higher the ratio, the more risky a bank may be to higher defaults. The ratio can be calculated using the following formula:

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

iii. Total Investment to Total Deposit Ratio

Commercial banks may mobilize their deposits by investing its fund in different securities issued by government and other financial and non-financial companies. Efforts

have been made to measure the extent to which the banks are successful in mobilizing the total deposit on investment. A high ratio is the indicator of high success to mobilize the banking fund as investment and vice-versa. The ratio can be calculated using the following formula:

$$\text{Total Investment to Total Deposit Ratio} = \frac{\text{Total Investment}}{\text{Total Deposit}}$$

C. Profitability Ratios

Profit is the difference between revenues and expenses over a period of time. A firm should earn profit to survive and to grow over a long period of time. So profits are essential, but profit earning is not the ultimate aim of a firm and it should never be earned at the cost of employees, customer and society. Profitability Ratio is a type of measurement that help to determine the ability of a company to generate earnings in comparison to its costs and expenses over a certain time period. The company with a higher profitability ratio than their competitors is considered to be doing well.

Profitability ratios are the indicators of degree of managerial success in achieving firm's overall goals (Pradhan, 1996). It shows the overall efficiency of the business concern. The following ratios are calculated under the profitability ratios:

i. Interest Income to Interest Expenses Ratio

Interest income to interest expenses ratio measures the gap between interest rates offered and interest rate charged. NRB has restricted the gap between the interest taken in loan, advances and interest offered in deposits. The credit creation power of commercial banks has high impact on this ratio.

This ratio can be calculated using the following formula:

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

ii. Return on Loan and Advances Ratio

This ratio measures the earning capacity of the commercial banks through its fund mobilization as loan and advances. Higher ratio indicates greater success to mobilize

fund and vice versa. Mostly, loan and advances include cash, credit, overdraft, bills purchased and discounted.

This ratio can be calculated using the following formula:

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

iii. Net Profit/Loss to Total Assets Ratio

The ratio is useful to measure how well management uses all the assets in the business to generate an operating surplus. Higher ratio indicates the higher efficiency in utilization of total assets and vice-versa. In other words, it is low utilization of bank assets and excess use of higher interest bearing amount of debt and vice-versa. In this study, net profit/loss to total assets ratio is examined to measure the profitability of all the financial resources in bank-assets.

This ratio can be calculated using the following formula:

Net Profit/Loss to Total Assets Ratio = $\frac{\text{Net Profit}}{\text{Total Assets}}$

iv. Interest Income to Total Loan and Advances Ratio

It shows the income as interest from total loan and advances. It is useful to know the fact that whether the loan has offered good return or not. We can increase interest income by taking proper issuing and recovery credit policy. High return shows the reliability of credit policy. This ratio can be calculated using the following formula:

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

v. Earnings Per Share (EPS)

EPS is one of the most widely quoted data when there is a discussion of a firm's performance or share value. The profit amount after tax is divided by the number of common shares to calculate the value of earnings per share. EPS demonstrates what profit the common shareholders for every share held, have earned. A company can decide whether to increase or reduce the number of shares on issue. This decision will

automatically affect the earnings per share. The profits available to the ordinary shareholders are represented by net profit after taxes and preference dividend. This ratio can be calculated using the following formula:

$$\text{Earnings Per Share} = \frac{\text{Net Profit After Tax}}{\text{No.of Common Stock Outstanding}}$$

D. Lending Efficiency Ratio

The efficacy of a firm depends to a large extent on the efficiency with which its assets are managed and utilized. This ratio is concerned with measuring the competence of a concerned bank. This ratio also shows the utility of funds available. The following are the various types of lending efficiency ratios:

i. Non – Performing Loan to Total Loan and Advances Ratio

NRB has directed all commercial banks to create loan loss provision against doubtful and bad debts. But both of our concerned sample banks have not provided data on non-performing loan in balance sheet and profit and loss account. This ratio can be calculated using the following formula:

Non – Performing Loan to Total Loan and Advances Ratio

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

ii. Loan Loss Provision to Total Loan and Advances Ratio

Loan loss provision to total loan and advances depicts the quality assets that a bank holds. The provision for loan loss reflects the increasing probability of nonperforming loan. The provision of loan means the net profit of the bank shall lessen by such amount. Increase in loan loss provision decreases profit resulting to, decrease in dividends but it is an affirmative impact to support financial conditions of a bank by calculating the credit risk and diminishing the risks related to deposits. Hence, sound financial conditions and safety of loans ensures a bank's prosperity resulting in increasing profits for long term. The low ratio indicates the good quality of assets in total volume of loan and advances.

High ratio indicates more risky assets in total volume of loan and advances. This ratio can be calculated using the following formula:

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

Constraints of Ratio Analysis

Ratio analysis has limitations that are directly innate from financial statements. Some of the most common weaknesses of ratio analysis are:

a. Financial statements are an index of past transactions. They do not depict current position of a bank. Evidently, ratio analysis is also primarily concerned with analyzing the past, which may or may not be relevant today. It is thus a sort of 'POSTMORTEM' analysis rather than a guide for decision-making.
b. In the context of constant price level changes, intra firm trend analysis loses much of its operational significance.
c. The differences in the characterization of items in balance sheet and income statement make the analysis of ratios intricate.
d. Occasionally, ratio analysis may suffer from what is known as fallacy of misplaced concreteness (Singh, 2007).

Despite of various confinements of ratio analysis and uncertainties about the valid measure of the financial performance, they are extensively used to measure the financial performance of a firm.

1.8.2 Statistical Tools

For supporting the study, statistical tools for instance, mean, standard deviation, coefficient of variation, correlation, trend analysis and diagrammatic as well as illustrative representation tools have been practiced.

i. Arithmetic Mean ($\bar{X}$):

Average is statistical constants, which enables us to comprehend in a single effort of the whole (Gupta, 2000). It represents the entire data by a single value. It provides the general and simplified vision of the immense accumulation of numerical data.

This can be calculated by using the following formula:

$X = \frac{1}{n} \sum_{i}^{N} = 1 X^{i}$

Where,

$\overline{X}$ = Arithmetic mean

N = Number of observations

Σ x = Sum of observations

ii. Standard Deviation (S.D.)

Standard deviation is the positive square root of the mean of the square of the deviations taken from the arithmetic mean. It is denoted by σ (Bajracharya, 2063). It is the absolute measure of dispersion in which the drawbacks present in other measures of dispersion are removed. It is calculated as:

$$\sigma = \sqrt{\frac{\Sigma(X - \overline{X})^2}{N}}$$

Where,

σ = Standard deviation

$\overline{X}$ = Arithmetic mean

N = Number of observations

iii. Coefficient of Variation (C.V.)

The co-efficient of dispersion based on standard deviation multiplied by 100 is known as coefficient of variation (C.V.). It is independent of units. Hence, two distributions can better be compared with the help of C.V. for their variability. Less the C.V., more will be the uniformity, consistency or more stable and vice versa.

It is calculated as:

$C.V = \frac{\sigma}{\overline{X}} \times 100\%$

Where,

σ = Standard Deviation

$\overline{X}$ = Mean

iv. Correlation Coefficient (r)

The correlation coefficient, denoted by r, is a measure of the strength of the straight-line or linear relationship between two variables. It is used to describe the extent to which one variable is linearly related to the other. It refers the proximity of the relationship and a study of covariance between two or more variables. "The correlation coefficient requires that the underlying relationship between the two variables under consideration is linear. If the relationship is known to be linear, or the observed pattern between the two variables appears to be linear, then the correlation coefficient provides a reliable measure of the strength of the linear relationship. If the relationship is known to be nonlinear, or the observed pattern appears to be nonlinear, then the correlation coefficient is not useful or at least questionable". The correlation coefficient takes on values ranging between +1 and -1.Where 0 indicates no linear relationship. +1 indicates a perfect positive linear relationship: as one variable increases in its values, the other variable also increases in its values via an exact linear rule and -1 indicates a perfect negative linear relationship: as one variable increases in its values, the other variable decreases in its values via an exact linear rule.

This can be calculated by using the following formula:

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

Where,

r_{xy} = Correlation between X and Y

$N\sum X.Y$ = No. of Product observation and sum of product X and Y

$(\sum X)(\sum Y)$ = Sum of Product X and sum of Product Y

v. Probable Error (P. E.)

The probable error of the coefficient of correlation helps in interpreting its value. With the help of probable error, it is possible to determine the reliability of the value of the coefficient as it depends on the conditions of random sampling. However, the probable error of correlation coefficient may lead to fallacious conclusions particularly when n, the number of pairs observation, is small. Also, the probable error of correlation coefficient may be used to determine the limits within which the population correlation coefficient may be expected to lie. This can be calculated by using the following formula:

$$P.E. = 0.6745 \times \frac{1-r^2}{\sqrt{N}}$$

Where,

r = Correlation coefficient

N = Number of pairs of observations

If the value of 'r' is less than the probable error, there is no evidence of correlation, i.e., the value of 'r' is not at all significant. On the other hand, if the value of 'r' is more than six times of the probable error, the coefficient of correlation is practically certain, i.e., the value of 'r' is significant.

1.9 Limitations of the Research Methodology

To carry out the research work, various financial and statistical tools are used. Similarly, descriptive as well as analytical analysis of credit management has been practiced. However, these tools and techniques have some limitations.

- Time Limitation

  The study has covered only five fiscal year, i.e, from the fiscal year 2012/13 to 2016/17. This period may not be enough to draw conclusions as major economic fluctuations may influence the economic performance of the commercial banks and therefore wrong conclusions may have arrived at during this study.

- Data limitation

The study is mostly based on the published financial statements of the concerned banks and thus excludes analysis of primary data. The validity of the secondary data depends upon the reliability of the published financial statements of the bank and conclusions are confined to the same period.

- Sample Limitation

  Among thirty commercial banks two commercial banks have been chosen as samples in this study. The sample size is somehow small and may hinder the generalization of the result to all the commercial banks in Nepal.

- Limitation of Statistical Tools.

  Simple statistical tools have been used in this study. The study is concerned with credit portfolio management of the concerned commercial banks and hence does not touch the other financial aspects

CHAPTER - IV

PRESENTATION AND ANALYSIS OF DATA

Introductions, review of literature and research methodology that are presented in the previous chapters provide the basic inputs to analyze & interpret the data from which concrete result can be obtained. In this section, collected filtered data are analyzed & interpreted as the stated methodology in the previous chapters. The included data are collected from various sources. These available data are tabulated, analyzed and interpreted to measure the various scopes of difficulties of the study and major conclusions of the study are presented systematically. The main objective of analyzing the financial performance and interpretation is to highlight the strength and weakness of the business. The collected data are analyzed & interpreted by using the financial & statistical tools.

In order to make our study effective, precise and easily understandable, this chapter is categorized in three parts; presentation, analysis and interpretation. The analysis is fully based on secondary data. In presentation section data are presented in terms of table. The presented data are then analyzed using different statistical tools mentioned in chapter three. At last the results of analysis are interpreted.

4.1 Liquidity Ratio

"Liquidity position shall mean the expected needs of a bank for liquid assets, expressed as the ratio between actual and potential liabilities and the actual and potential consumption of liquid assets in the same period. A commercial bank shall periodically calculate its liquidity position. A bank shall calculate the liquidity position with a liquidity ratio" (Marco Kranjec).

Following tools can be used to calculate the liquidity position of the bank.

4.1.1. Current Ratio

Current ratio is an indication of a bank's ability to meet short-term debt obligations; the higher the ratio, the more liquid the company is. Current ratio is equal to current assets divided by current liabilities

Table 4.1

Current Ratio of NABIL and HBL

(Rs. in millions)

NABIL				HBL		
Year	**Current Assets**	**Current Liabilities**	**Ratios**	**Current Assets**	**Current Liabilities**	**Ratios**
2012/13	25988.555	33950.842	0.71	17178.295	33482.241	0.51
2013/14	31515.334	39854.024	0.79	27186.689	47178.980	0.58
2014/15	36787.150	47275.782	0.78	33702.235	45075.167	0.75
2015/16	42945.158	52167.906	0.82	37085.147	48683.083	0.76
2016/17	46726.164	56207.806	0.83	41734.533	58280.934	0.72
Average			**0.786**			**0.664**
S.D			**0.042**			**0.101**
C.V			**5.34%**			**15.21%**

Note: Annual Reports of Concern Banks

The above able 4.1 shows the current ratio of NABIL and HBL from the fiscal year 2012/13to 2016/17 of five years study period. The mean ratio of five years study period of NABIL and HBL is 0.786 and 0.664 times respectively. Similarly, standard deviation is 0.042 and 0.101 times, and coefficient of variation is 5.34% and 15.21% respectively. The above table can also be illustrated by following figure.

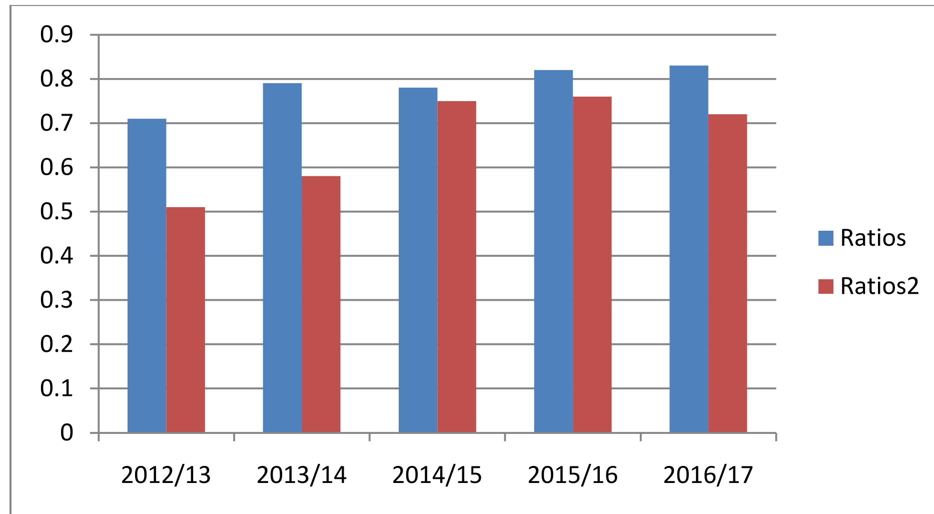

Figure 4.1

Current Ratio of NABIL and HBL

Comparative Analysis of Current Ratio

Table 4.1 exhibits the current ratio of NABIL and HBL during the five years of study period. Where ratios of NABIL are not constant and the ratio is highest in the year 2016/17. And the ratios of HBL are in increasing trend except the year 2016/17. Comparing the study period, NABIL kept highest mean ratio of current assets to current liabilities ratio than HBL. And the ratios of NABIL have more variation and less consistency than HBL because of high standard deviation and coefficient of variation. Though the most favorable standard of current ratio should be 2:1; however the conventional measure of liabilities may not applicable to banking sector.

As per recent Reserve Bank of India's guidelines a minimum current ratio of 1.33:1 is to be ensured for large borrowers. But even the both banks are not able to maintain the ratio of 1:1. Hence the study shows that both of the banks are not managing the current ratio as per the standard of Nepal Rastra Bank.

4.1.2 Cash and Bank Balance to Total Deposit Ratio

Cash and Bank Balance to Total Deposit ratio indicates the bank ability to meet their daily requirement of depositors. Higher ratio shows the greater ability to meet customer demands on their deposits.

Table 4.2

Cash and Bank Balance to Total Deposit Ratio of NABIL and HBL

(Rs. in millions)

	NABIL			HBL		
Year	**Cash & Bank Balance**	**Total Deposit**	**Ratios**	**Cash & Bank Balance**	**Total Deposit**	**Ratios**
2012/13	2671.141	31915.047	0.084	7117.29	39014.200	0.182
2013/14	3372.512	37348.255	0.090	9171.790	45194.232	0.203
2014/15	1400.097	46340.700	0.030	10141.280	42882.039	0.236
2015/16	2458.549	49608.376	0.050	12013.865	46808.435	0.257
2016/17	4294.046	54905.676	0.078	14063.693	56052.373	0.251
Average			**0.066**			**0.225**
S.D			**0.023**			**0.028**
C.V			**34.84%**			**12.44%**

Note: Annual Reports of Concern Banks

Above table illustrates the cash and bank balance to total deposit ratio of NABIL and HBL over the five years period. Here, mean ratio of NABIL and HBL is 0.066 and 0.225 respectively. Similarly, standard deviation is 2.3% and 2.8 %, and coefficient of variation is 34.84% and 12.44%. Again, Cash and bank balance and total deposits of both banks are be presented graphically as follows.

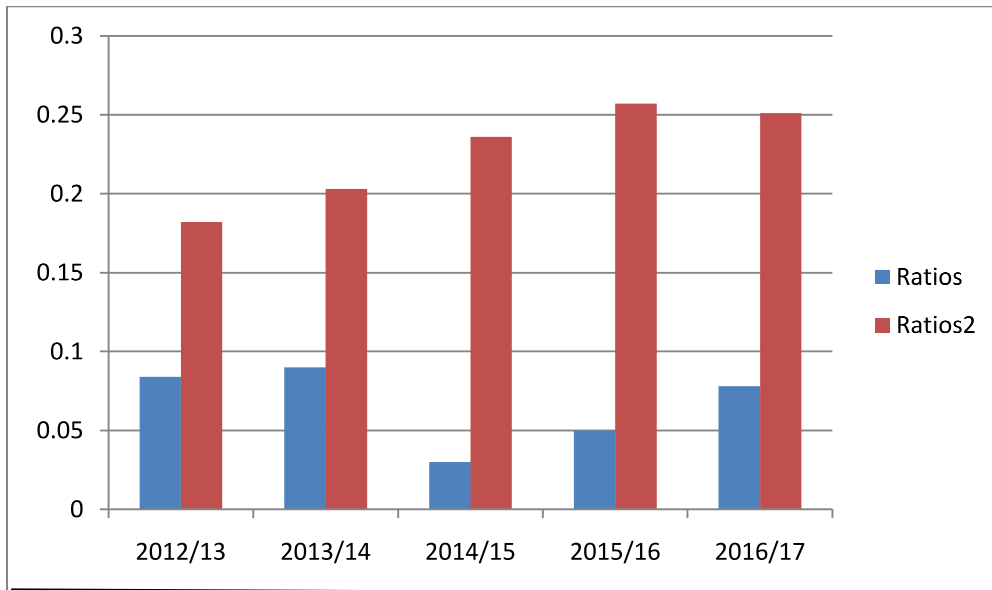

Figure 4.2

Cash and Bank Balance to Total Deposit Ratio of NABIL and HBL

A Comparative Analysis of Cash and Bank Balance to Total Deposit Ratio

The cash and bank balance to total deposit ratio of NABIL is in increasing trend, but it is remarkable that the ratio declines by 3.0 percent and reached to 5.0 percent in the year 2015/16. The ratio of HBL is also in increasing trend except the year 2016/17 of the study period. Comparatively, HBL has maintained the higher ratio than NABIL in each year.

However the ratio of both banks is not consistent. Commercial banks have to maintain their cash and bank balance in terms of total deposit as directed by NRB time to time to meet the withdraw demand of the depositors. Otherwise they are imposed penalty. On the other side by decreasing the cash and bank balance the banks can maximize the profit if they invest the amount in to short-term marketable securities, treasury bills etc.

4.1.3 Cash and Bank Balance to Current Deposit Ratio

This ratio is the proportion of most liquid fund over current deposit of the bank. Higher ratio indicates the bank's sound ability to meet the daily cash requirement of its customers' deposits. If the bank maintains low ratio, the bank may not be able to make the payment against cheques issued.

Table 4.3

Cash and Bank Balance to Current Deposit Ratio of NABIL and HBL

(Rs. in millions)

	NABIL			HBL		
Year	**Cash & Bank Balance**	**Current Deposit**	**Ratios**	**Cash & Bank Balance**	**Current Deposit**	**Ratios**
2012/13	2671.141	5284.368	0.505	7117.29	8178.393	0.870
2013/14	3372.512	5480.533	0.615	9171.790	9923.275	0.924
2014/15	1400.097	7904.619	0.177	10141.280	10942.415	0.927
2015/16	2458.549	5456.894	0.451	12013.865	10905.854	1.102
2016/17	4294.046	6572.215	0.653	14063.693	12326.788	1.141
Average			**0.480**			**0.993**
S.D			**0.168**			**0.108**
C.V			**35%**			**10.87%**

Note: Annual Reports of Concern Banks

Table 4.3 depicts the cash and bank balance to current deposit ratio of NABIL and HBL over the five years period. Average ratio of NABIL and HBL is 0.480 and 0.993 respectively. Similarly, standard deviation is 16.8% and 10.8%, and coefficient of variation is 35% and 10.87%. Graphically, cash and bank balance and current deposit of the sample banks can be illustrated as follows.

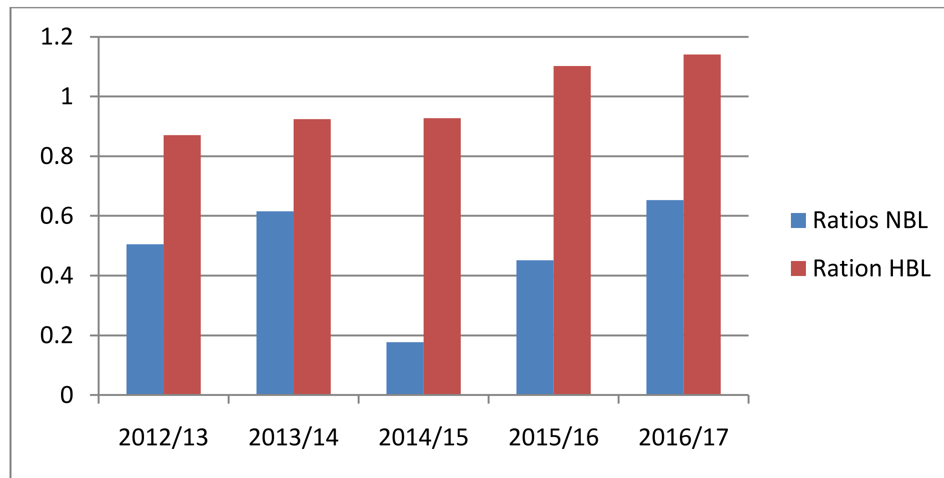

Figure 4.3

Cash and Bank Balance to Current Deposit Ratio of NABIL and HBL

A Comparative Analysis of Cash and Bank Balance to Current Deposit Ratio

Cash and Bank balance to Current Ratio of NABIL is in increasing trend for the first 2 years and it decreases again whereas the ratio is in increasing trend.. The mean ratio of HBL is higher than NABIL. Again, ratios of NABIL have more variation and less consistency than HBL. HBL has high liquid assets than NABIL. It means that NABIL can closely meet its daily requirement to make the payments on customer deposit withdrawals than HBL. However, NABIL can maximize its profit by mobilizing the fund.

4.1.4 Cash and Bank Balance to Saving Deposits Ratio

The ratio of cash and bank balance to interest sensitive deposits measures the ability to meet its sudden outflow of interest sensitive deposits due to the change in interest rate.

Table 4.4

Cash and Bank Balance to Saving Deposits Ratio of NABIL and HBL

(Rs. in millions)

	NABIL			HBL		
Year	**Cash & Bank Balance**	**Saving Deposit**	**Ratios**	**Cash & Bank Balance**	**Saving Deposit**	**Ratios**
2012/13	2671.141	12159.966	0.220	7117.29	21284.329	0.334
2013/14	3372.512	14620.407	0.231	9171.790	31284.260	0.293
2014/15	1400.097	13783.585	0.102	10141.280	27313.755	0.371
2015/16	2458.549	14288.520	0.172	12013.865	22501.339	0.534
2016/17	4294.046	17994.746	0.238	14063.693	24909.160	0.565
Average			**0.193**			**0.419**
S.D			**0.051**			**0.109**
C.V			**26.42%**			**26.01%**

Note: Annual Reports of Concern Banks

The above table illustrates the cash and bank balance to saving deposit ratio of NABIL and HBL over the five years period. Here, mean ratio of NABIL is 0.193 and of HBL remains at 0.419. Similarly, standard deviation is 0.051 and 0.109 respectively, and coefficient of variation is 26.42% and 26.01%. Cash and bank balance and saving deposit of NABIL and HBL can be graphically illustrated as follows.

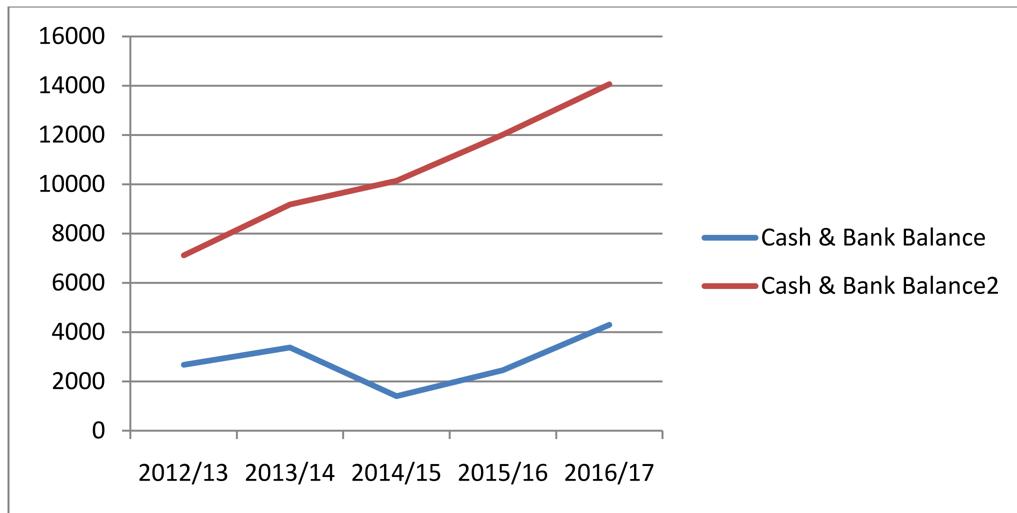

Figure 4.4

Cash and Bank Balance to Interest Sensitive Deposit Ratio of NABIL and HBL

A Comparative Analysis of Cash and Bank Balance to Saving Deposit Ratio

Cash and bank balance to saving deposit ratio of NABIL is in increasing trend till the year of 2013/14 and again it is decreasing, whereas the ratio of HBL is also following the same trend and it reaches to the highest point in the year of 2015/16. The mean ratio of HBL is higher than NABIL. Hence, it can be concluded that HBL has high degree of liquid assets than NABIL. However, high degree of liquid assets is not better because of interest expenses and inverse impact on profitability.

4.2 Activity/Efficiency Ratios

This ratio is also known as turnover or efficiency ratio or assets management ratio. It measures how efficiently the firm employs the assets. Turnover means, how many numbers of times the assets flow through a firm's operations and into sales (Kulkarni, 2006:26). Greater rate of turnover or conversion indicates more efficiency of a firm in managing and utilizing its assets, being other things equal. Various ratios are examined under this heading.

4.2.1 Loans and Advances to Total Deposit Ratio

This ratio measures either a bank is successful to manage its total deposit on loan and advances for the rationale of income generation or not. A high ratio indicates better mobilization of collected deposit and vice-versa.

Table 4.5

Loans and Advances to Total Deposit Ratio of NABIL and HBL

(Rs. in millions)

NABIL				HBL		
Year	**Loan & Advances**	**Total Deposit**	**Ratios**	**Loan & Advances**	**Total Deposit**	**Ratios**
2012/13	21365.053	31915.047	0.669	10584.781	39014.200	0.271
2013/14	27589.933	37348.255	0.739	17614.898	45194.232	0.390
2014/15	32268.873	46340.700	0.696	23560.955	42882.039	0.549
2015/16	38034.097	49608.376	0.767	24671.281	46808.435	0.527
2016/17	41605.683	55023.695	0.756	27670.840	56052.373	0.494
		Average	**0.725**			**0.446**
		S.D	**0.037**			**0.103**
		C.V	**5.10%**			**23.09%**

Note: Annual Reports of Concern Banks

Table 4.5 shows the loan and advance to total deposit ratio of NABIL and HBL over the five years study period. Similarly, the mean ratio of NABIL and HBL remains at 0.725 and 0.446 respectively. Likewise, standard deviation is 0.037 and 0.103, and coefficient of variation is 5.10 % and 23.09%. Graphically, loans and advance to total deposit of sample banks are illustrated as follows.

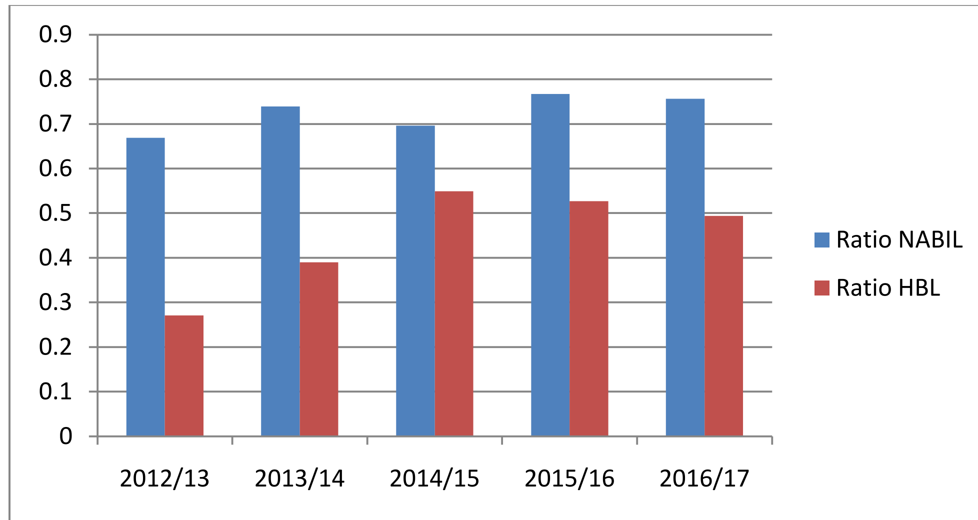

Figure 4.5

Loans and Advances to Total Deposit Ratio of NABIL and HBL

A Comparative Analysis of Loans and Advances to Total Deposit Ratio

Loan and advances to total deposit ratio of NABIL is in increasing trend, whereas the ratio of HBL is also is in increasing trend except in 2014/15. Mean ratio of NABIL is higher than HBL, whereas standard deviation and coefficient of variation of HBL are higher than of the NABIL. Hence, the liquid assets of HBL have higher variation. Additionally, lending ratios are very low than collection ratios over the study period. From this perspective, loans and advances to total deposit ratios of the banks is satisfactory.

4.2.2 Loans and Advances to Total Assets Ratio

Loan and advances of any commercial bank symbolizes the key portion in the volume of total working fund. This ratio measures the volume of loan and advances in the structure of total assets. High degree of loan and advances to total assets ratio indicates good performance of the bank in mobilizing its funds through lending function. However, reversely, high ratio is repressed enactive of low liquidity ratio. Granting of loans and advances always carries a certain scale of risk. Thus, this asset of banking business is regarded as risky assets. This ratio measures the management attitude toward risky assets. The low ratio is indicative of low productivity and high degree of safety in liquidity and vice-versa. The relations between risk and return determine this ratio. This ratio also shows the credit risk taken by the bank towards mobilizing its funds into different types of assets. This ratio reveals the extent to which the banks are successful in mobilizing their total assets on loan and advances for the purpose of income generation.

Table 4.6

Loans and Advances to Total Assets Ratio of NABIL and HBL

(Rs. in millions)

NABIL				HBL		
Year	**Loan & Advances**	**Total Assets**	**Ratios**	**Loan & Advances**	**Total Assets**	**Ratios**
2012/13	21365.053	37132.759	0.575	10584.781	39258.000	0.270
2013/14	27589.933	43867.397	0.629	17614.898	47559.110	0.370
2014/15	32268.873	52079.725	0.620	23560.955	44736.652	0.527
2015/16	38034.097	58099.619	0.655	24671.281	51158.657	0.482
2016/17	41605.683	63200.298	0.658	27670.840	58615.521	0.472
		Average	**0.627**			**0.424**
		S.D	**0.030**			**0.093**
		C.V	**4.78%**			**21.93%**

Note: Annual Reports of Concern Banks

The above table depicts the loan and advances to total assets ratio of NABIL and HBL during the five years period. Where average ratio of NABIL and HBL remain at 0.627 and 0.424 respectively. Similarly, standard deviation is 0.030 and 0.093, and coefficient of variation is 5.918% and 30.778%. Loans and advances to total assets ratio of NABIL and HBL are graphically presented as follows.

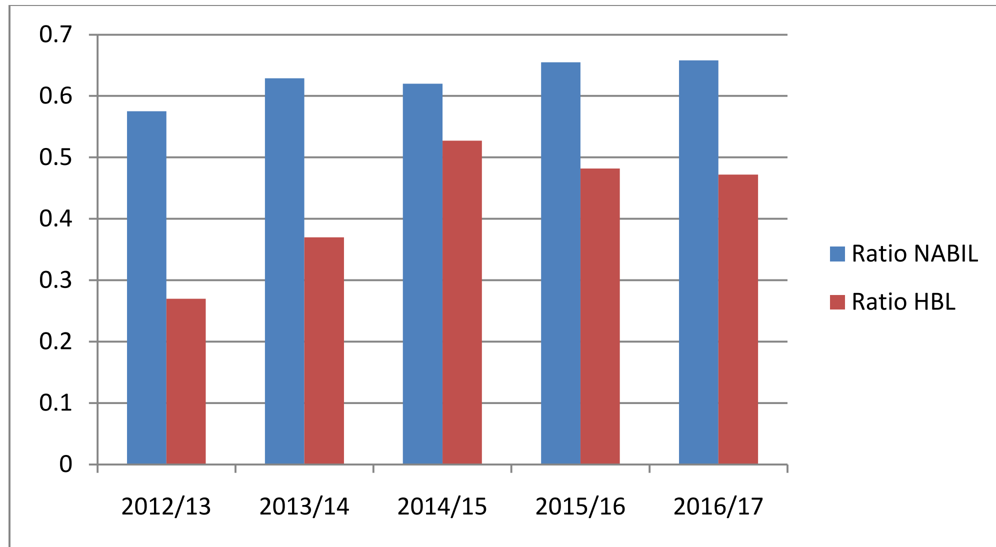

Figure 4.6

Loans and Advances to Total Assets Ratio of NABIL and HBL

A Comparative Analysis of Loans and Advances to Total Assets Ratio

Loan and advances to total assets ratio of NABIL and HBL is in increasing trend over the study period. Similarly, HBL has highest mean ratio than that of NABIL. Therefore, it can be concluded that NABIL is a risk taker than HBL. Also, HBL has sound lending policy so that it is able to mobilize its resources as loans and advances than NABIL.

4.2.3 Total Investment to Total Deposit Ratio

A commercial bank organizes its deposit by investing in different securities issued by government and other financial and non-financial organizations. The ratio measures the extent to which banks are able to mobilize their deposits on investment in various securities. In the process of management of bank assets, various factors such as excess availability of fund, liquidity requirement, central banks norms etc. are to be considered in general. This ratio indicates the proportion of deposits utilized for the purpose of income generation as well as for maintaining liquidity in an appropriate level. A high ratio is the indicator of high success of mobilizes deposits in securities and vice-versa.

Table 4.7

Total Investment to Total Deposit Ratio of NABIL and HBL

(Rs. in millions)

	NABIL			HBL		
Year	**Total Investment**	**Total Deposit**	**Ratios**	**Total Investment**	**Total Deposit**	**Ratios**
2012/13	9939.771	31915.047	0.311	26657.000	39014.200	0.683
2013/14	10826.379	37348.255	0.289	13397.559	45194.232	0.296
2014/15	13600.916	46340.700	0.293	5784.372	42882.039	0.135
2015/16	13003.205	49608.376	0.262	7585.544	46808.435	0.162
2016/17	14076.850	54905.676	0.256	8391.726	56052.373	0.150
		Average	**0.282**			**0.285**
		S.D	**0.020**			**0.207**
		C.V	**7.09%**			**72.63**

Note: Annual Reports of Concern Banks

Table 4.7 illustrates the total investment to total deposit ratio of NABIL and HBL over the study period. Mean ratio of NABIL and HBL is 0.282 and 0.285 respectively during study period. Likewise, standard deviation is 0.020 and 0.207 and coefficient of variation is 7.09% and 72.63% respectively. Total investment and total deposit of the sample banks can be graphically shown as follows.

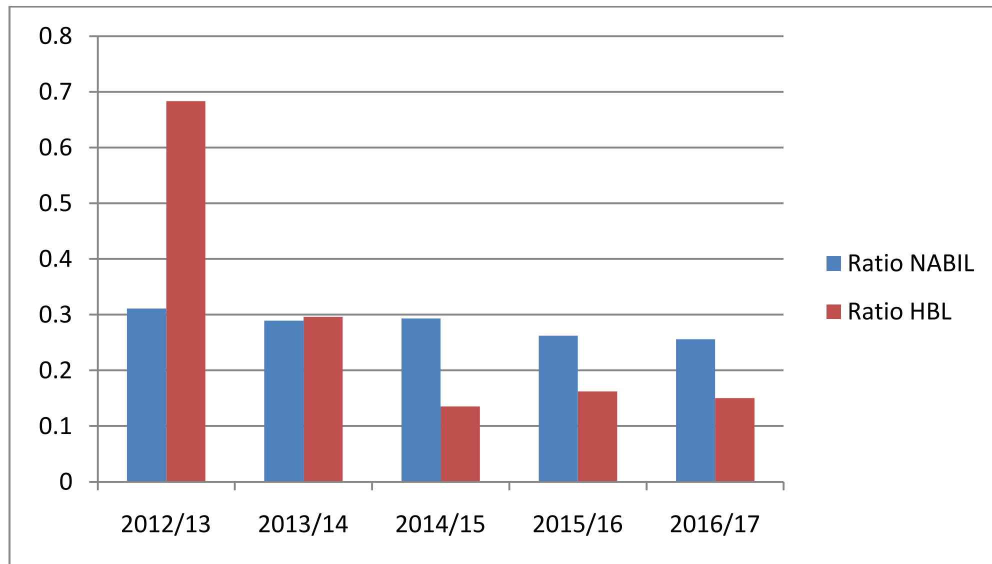

Figure 4.7

Total Investment to Total Deposit Ratio of NABIL and HBL

A Comparative Analysis of Total Investment to Total Deposit Ratio

Total investment to total deposit ratio of both bank is in decreasing trend over the five years of study period. And HBL has highest mean ratio than that of NABIL. Likewise, the ratios of HBL have more variation and less consistency. It is seen that the total deposit of both bank is increasing each year but the investment is decreasing. This may be happening due to unfavorable economic condition and environment for investment.

4.3. Profitability Ratios

Profitability ratios are very effective and advantageous to measure the overall operation efficiency of a financial institution. A bank cannot survive without profit. The banks acquire profit by providing different services to its customers or by providing loan and advances and making various kinds of investment opportunities. Profitability ratios measure the efficiency of bank. A higher profit ratio shows higher efficiency of a bank. The following ratios are included under profitability ratio.

4.3.1 Interest Income to Interest Expenses Ratio

Interest income to interest expenses ratio is the difference between interest rates offered for deposits and interest rate charged for loans and advances offered by a bank, which is restricted and controlled by NRB in the context of Nepal. The credit creation power of a commercial bank has high impact on this ratio.

Table 4.8

Interest Income to Interest Expenses Ratio of NABIL and HBL

(Rs. in millions)

NABIL				HBL		
Year	**Interest Income**	**Interest Expenses**	**Ratios**	**Interest Income**	**Interest Expenses**	**Ratios**
2012/13	1978.696	758.436	2.609	1849.354	773.294	2.392
2013/14	2798.486	1,153.280	2.427	2690.058	791.710	3.398
2014/15	4047.725	1,960.107	2.065	3067.553	909.990	3.371
2015/16	5258.269	2,946.691	1.784	3740.719	1482.204	2.524
2016/17	6145.751	3152.940	1.949	4051.152	2197.137	1.844
Average			**2.167**			**2.706**
S.D			**0.306**			**0.599**
C.V			**14.12%**			**22.14%**

Note: Annual Reports of Concern Banks

Table 4.8 depicted the interest income to interest expenses ratio of sample banks over the five years period. The mean ratio of NABIL and HBL remains at 2.167 and 2.706 respectively. Similarly, standard deviation is 0.306 and 0.599, and coefficient of variation is 14.12% and 22.14%. The ratio can be graphically illustrated as follows.

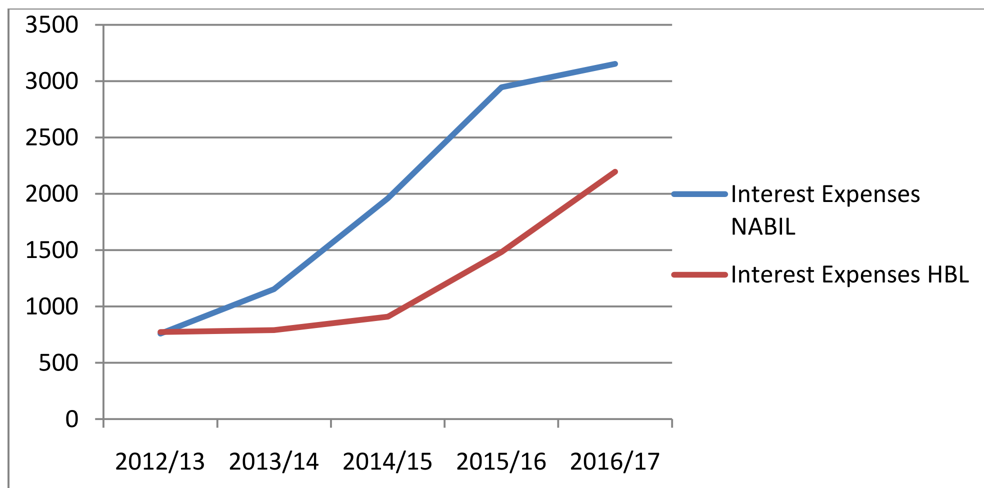

Figure 4.8

Interest Income to Interest Expenses Ratio of NABIL and HBL

A Comparative Analysis of Interest Income to Interest Expenses Ratio

The ratio of NABIL is in decreasing trend whereas the ratio of HBL is firstly increasing, then decresing. It means the gap between lending and borrowing of NABIL is decreasing. The ratio of HBL is more inconsistence than that of NABIL.

4.3.2 Return on Loan and Advances Ratio

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

Table 4.9

Return on Loan and Advances Ratio of NABIL and HBL

(Rs. in millions)

NABIL				HBL		
Year	**Net Profit**	**`Loan and Advances**	**Ratios**	**Net Profit**	**`Loan and Advances**	**Ratios**
2012/13	746.468	21365.053	0.035	250.131	10584.781	0.024
2013/14	1031.053	27589.933	0.037	894.254	17614.898	0.051
2014/15	1139.011	32268.873	0.035	249.382	23560.955	0.011
2015/16	1337.745	38034.097	0.035	128.346	24671.281	0.005
2016/17	1696.276	41605.683	0.041	176.361	27670.840	0.006
		Average	**0.037**			**0.019**
		S.D	**0.002**			**0.017**
		C.V	**5.41%**			**89.47%**

Source: Annual Reports of Concern Banks

Above table 4.9 shows the return on loan and advances ratio of NABIL and HBL over the five years period. The mean ratio of NABIL and HBL remains at 0.037 and 0.019 respectively. Likewise, standard deviation is 0.002 and 0.017; and coefficient of variation is 5.41% and 89.47%. The ratio can be graphically illustrated as follows.

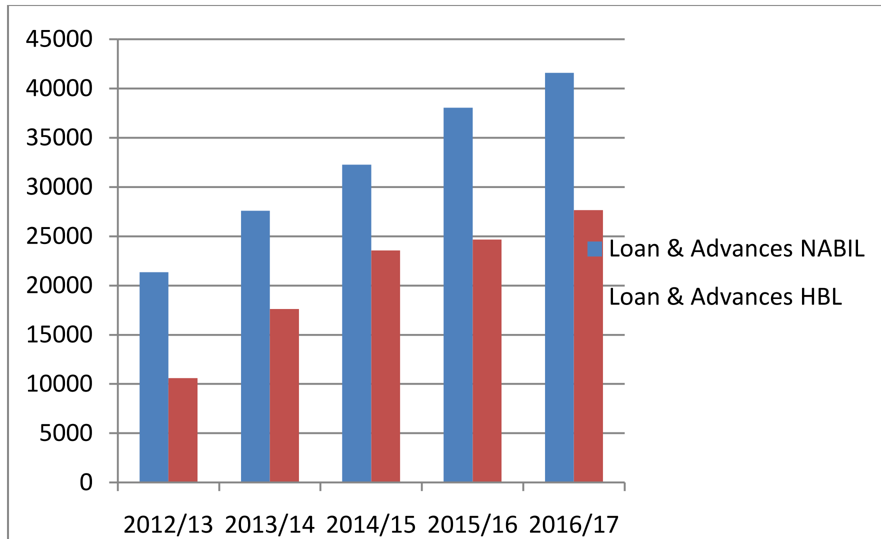

Figure 4.9

Return on Loan and Advances Ratio of NABIL and HBL

A Comparative Analysis of Return on Loan and Advances Ratio

Return on loan and advances ratio of both sample bank is in decreasing trend, though loan amount of both bank is increasing every year. It means the lending policy of both bank is very poor. However, the data shows a bit better performance of NABIL than HBL.

4.3.3 Net Profit/Loss to Total Assets Ratio

The ratio is beneficial to measure how well management uses all the assets in business to generate an operating surplus. Higher ratio indicates higher efficiency in the utilization of total assets and vice-versa.

Table 4.10

Net Profit/Loss to Total Assets Ratio of NABIL and HBL

(Rs. in millions)

NABIL				HBL		
Year	**Net Profit**	**Total Assets**	**Ratios**	**Net Profit**	**Total Assets**	**Ratios**
2012/13	746.468	37132.759	0.020	250.131	29258.334	0.006
2013/14	1031.053	43867.397	0.024	894.254	47559.110	0.019
2014/15	1139.011	52079.725	0.022	249.382	44736.652	0.006
2015/16	1337.745	58099.619	0.023	128.346	51158.657	0.003
2016/17	1696.276	63200.298	0.027	176.361	58615.521	0.003
		Average	**0.023**			**0.007**
		S.D	**0.002**			**0.006**
		C.V	**8.69%**			**85.71%**

Source: Annual Reports of Concern Banks

Above table 4.10 shows the return on total assets ratio of NABIL and HBL over the five years period .The mean ratio of NABIL and HBL remains at 0.023 and 0.007 respectively. Likewise, standard deviation is 0.002 and 0.006; and coefficient of variation is 8.69%.and 85.71%. The ratio can be graphically illustrated as follows.

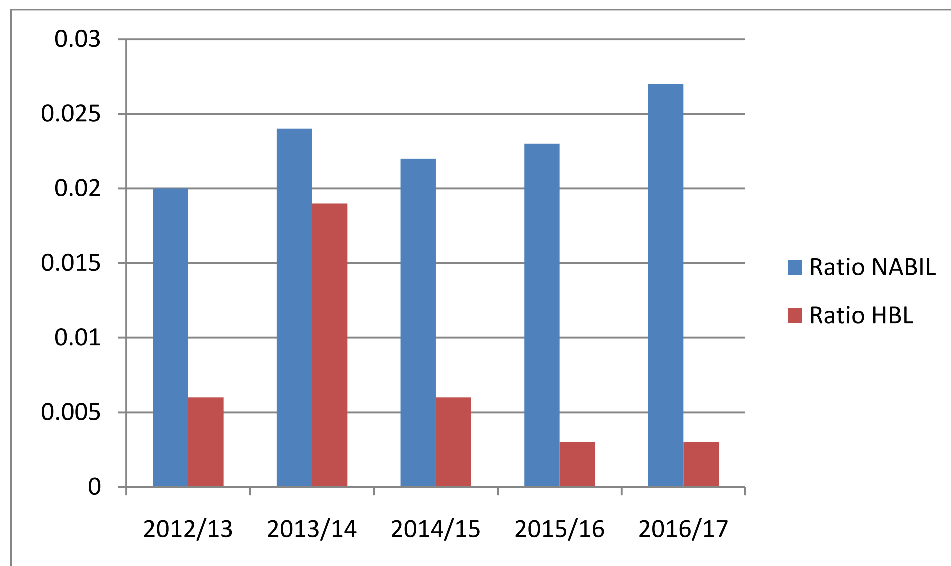

Figure 4.10

Net Profit and Total Assets of NABIL and HBL

A Comparative Analysis of Return on Total Assets Ratio

The return on total assets ratio of NABIL and HBL is increased in second year of study period and it goes down in next year. Likewise, the ratios of HBL have more variation and less consistent than NABIL. Comparatively, ratio of NABIL shows that it has good performance than that of HBL.

4.3.4 Earning Per Share (EPS)

EPS is one of the most commonly quoted statistics to know a company's performance or share value. It is the profit after tax quantity that is divided by the number of common shares to calculate the value of earnings per share. This figure shows the profit common shareholders for every share held have earned. A company can decide whether to increase or reduce the number of shares on issue. This decision will automatically affect the earnings per share. The profits available to the ordinary shareholders are represented by net profit after taxes and preference dividend. Symbolic expression of EPS is given below.

Table 4.11

Earning Per Share of NABIL and HBL

(Rs. In hundred)

Year	2012/13	2013/14	2014/15	2015/16	2016/17	Average
NABIL	1.15	1.13	0.838	0.707	0.836	0.932
HBL	0.628	2.350	0.655	0.337	0.464	0.887

Source: Annual Reports of Concern Banks

Table 4.11 represents the earning per share of NABIL and HBL over the five years period. The mean EPS of NABIL and HBL remains at 0.932 and 0.887 respectively. EPS demonstrates what profit the common shareholders for every share held, have earned. A company can decide whether to increase or reduce the number of shares on issue. The ratios can be graphically presented as follows.

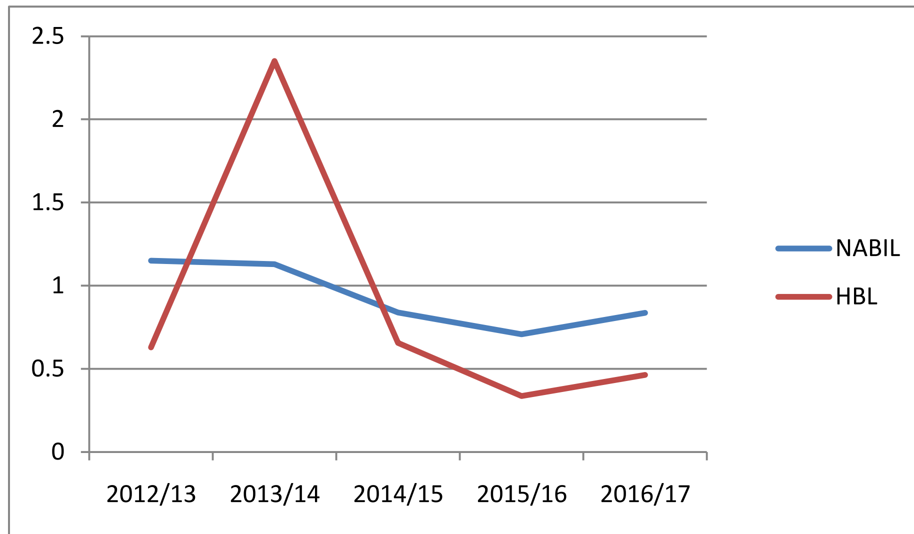

Figure 4.11

Earning Per Share of NABIL and HBL

A Comparative Analysis of Earning Per Share

In the above figure, the Earning per Share of HBL is in increasing trend till 2013/14 and the Earning per share of NABIL is in decreasing trend till 2015/16. After this, EPS of HBL is decreasing rapidly and EPS of NABIL has increased. Similarly, NABIL has the highest mean of EPS than that of HBL. We can conclude that NABIL is able to earn and provide good return to its shareholders than HBL over the study period.

4.4 Lending Efficiency Ratios

Under this, lending efficiency, quality of lending and its effects are measured. The efficiency of a firm depends to a large extent on the efficiency with which its assets are managed and utilized. This ratio also shows the utility to available fund. The following are the various type of lending efficiency ratios.

4.5 Coefficient of Correlation Analysis

The statistical tool, coefficient of correlation has been studied to find out whether the two available variables are inter-correlated or not. If the result falls with the correlated point, the two variables are inter-correlated, otherwise not. Now to find out the correlation coefficient between total deposit and loan and advances as well as net profit and loan and

advances, the widely used method Karl Pearson's Coefficient of Correlation method has been adopted.

4.5.1 Coefficient of Correlation between Total Deposits and Total Loan and Advances

The coefficient of correlation between total deposit and total loan and advances measures the degree of relationship between these two variables. For analysis, total deposit is independent variable and total loan and advances are dependent variable. The main objective of calculating 'r' between these two variables is to justify whether total deposits are significantly used as total loan and advances in a proper way or not.

Table 4.12

Correlation between Total Deposits and Total Loan and Advances of NABIL

Correlation (rxy)	P.E.	6 P.E.
0.988	0.0072	0.0432

Note: Appendix I

Table 4.12 shows that there is high degree of positive correlation between Total Deposits and Total Loan and Advances of NABIL. That means, if the total deposit is increased absolutely the total loan and advances is also increased and vice versa. The coefficient of correlation between total deposits and total loan and advances is +0.998 and probable error is 0.0072. Comparing the value of 'r' and 6 times P.E., 'r' is greater than 6 times of P.E., i.e. 0.988>0.0432. From the above analysis, we can conclude that NABIL has positive relationship and significant at all time between total deposits and total loan and advances. The relationship is significant, i.e. loan and advances is increase as the portion increase in deposits in relation to 0.988 and vice-versa.

Table 4.13

Correlation between Total Deposits and Total Loan and Advances of HBL

Correlation (rxy)	P.E.	6 P.E.
0.799	0.109	0.654

Note: Appendix II

Table 4.13 shows that there is positive relationship between total deposits and total loan and advances of HBL. The coefficient of correlation between total deposits and total loan and advances is 0.799 and probable error is 0.109. While, comparing the value of 'r' and 6 times of P.E., we can say that there is significantly positive relationship between total deposits and total loan and advances of HBL because 'r' is higher than 6 times P.E., i.e. 0.799 > 0.654. That means HBL has positive relationship with significant between total deposits and total loan and advances. The relationship is significant, i.e. loan and advances is increase as the portion increase in deposits in relation to 0.799 and vice-versa**.**

4.5.2 Coefficient of Correlation between Total Loan and Advances and Net Profits

Total loan and advances is independent variable and net profit is dependent variable. The main objectives of computing 'r' between these two variables are to justify whether total loan and advances are significantly used to earn profit in a proper way or not.

Table 4.14

Correlation between Total Loan and Advances and Net Profits of NABIL

Correlation (rxy)	P.E.	6 P.E.
0.983	**0.010**	**0.06**

Note: Appendix III

Table 4.14 shows that the coefficient of correlation between total loan and advances and net profit is 0.983 and probable error is 0.010. It means there is highly positive correlation between total loan and advances and net profit of NABIL. Hence, if the total loan and advances is increased absolutely the net profit is also increased and vice versa. Comparing the value of 'r' and 6 times P.E., there is significantly positive relationship between total loan and advances and net profit of NABIL because 'r' is higher than 6 times P.E., i.e. 0.983 > 0.06. From the above analysis, we can conclude that NABIL has positive relationship with significant between total loan and advances and net profit. The relationship is significant, i.e. profit increases as the portion increases in loan and advances in relation to 0.983and vice-versa.

Table 4.15

Correlation between Total Loan and Advances and Net Profits of HBL

Correlation (rxy)	P.E.	6 P.E.
-0.356	**0.263**	**1.578**

Note: Appendix IV

Table 4.15 shows that the coefficient of correlation between total loan and advances and net profit is -0.356 and probable error is 0.263. There is negative correlation between total loan and advances and net profits of HBL. That means, if the total loan and advances is increased absolutely the net profit is decreased and vice versa.. Comparing the value of 'r' and 6 times P.E., we can say that there is negative relationship but not significant at all time between total loan and advances and net profit of HBL because 'r' is less than 6 times P.E., i.e. -0.356<0.263. From the above analysis, we can conclude that HBL has negative correlation and significant at all time between total loan and advances and net profit. The relationship is significant, i.e. profit is increase as the portion decrease in loan and advances in relation to 0.356 and vice-versa and significant at all.

4.6 Major Finding of the Study

From the analysis, the study has revealed the following issues.

1. NABIL kept the highest mean ratio of current assets to current liabilities ratio than HBL. And the ratios of HBL have more variation and less consistency than NABIL. But even the both banks are not able to maintain the ratio of at least 1:1. Hence the study shows that both of the banks are not managing the current ratio as per the standard of Nepal Rastra Bank.
2. NABIL has maintained lower degree of cash and bank balance to total deposit ratio than NABIL. It helps NABIL to maximize the profit by mobilizing the fund. But, HBL can easily meet the withdraw requirement of depositors.
3. Assets management is one of the important factors of commercial banks. Investing in the higher quality assets reduces the credit risk and generates higher profits. HBL has lower average ratio of loan and advances to total deposit ratio of 44.60% and with NABIL is 72.50%. But the trend of both banks is increasing. NABIL has

higher ratio of lending to total deposit which means they are earning they are earning higher return from their deposits from lending. But higher the loan and advances to total deposit ratio increases the liquidity risk which the HBL has managed well.

4. Total investment to total deposit ratio of HBL is higher than NABIL
5. Interest income to interest expenses ratio of HBL is higher than NABIL. It can be concluded that HBL has high degree of gap between interest offered and interest charged than NABIL. This shows that NABIL has charged high interest rate to borrowers and offering low interest rate to depositors.
6. Return on loan and advances ratio of HBL is lower than that of NABIL. That means lending policy of NABIL is sounder than HBL.
7. Earning capacity of NABIL is better than HBL.
8. Interest income ratio of HBL is higher than NABIL. It means that HBL is mobilizing its loan in high interest earning area.
9. Loan loss provision of NABIL is lower than HBL. However, HBL is also decreasing the amount of loan loss provision each year. This indicates that both sample banks has tried to decrease the volume of nonperforming loans.

NABIL has positive with significant relationship at all time between total deposits and total loan and advances. NABIL has positive with significant relationship between total deposits and total loan and advances. HBL has positive with significant relationship between total loan and advances and net profit. HBL has negative with significant relationship at all time between total loan and advances and net profit.

CHAPTER V
SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

This final chapter is an outcome of all the efforts done from first to forth chapter. Though this chapter seems to be the shortest amongst previous ones, it is the most important one because it contains the extract of the whole research. This chapter includes not only all the study, findings and conclusions but recommendations and suggestions are also made on the basis of them.

5.1 Summary

This research is concerned about the credit portfolio management of foreign joint venture commercial banks namely Nabil bank and Himalayan bank limited. This study helps to know about credit portfolio management of the company. For the purpose of obtaining the up-to- date understanding of the subject and its significance on the past, identify the methods used in the previous researches and to find out the comparison of the research findings, a review of related studies have been done. It basically comprise of major findings, conclusions and recommendations of the previous studies relevant to the research.

This research is based on the secondary source of data. The researcher used descriptive and analytical research design for the Nabil Bank limited and Himalayan Bank limited. Descriptive research design defined the situation and analytical research design analyzed that the information are critically evaluated. The researcher also used various financial tools likes Net profit, EPS, current ratio, deposits ratio, Profitability ratios etc, of these banks.

The researcher has analyzed about the credit portfolio for these banks. The study is concentrated on the analysis of chosen foreign joint venture commercial banks and their credit portfolio. The main objective of this study is to analyze the risk and return associated with the portfolio investment (i.e. investment on loans, advances and overdraft, company shares and treasury bills) of the selected commercial banks and also

to evaluate the portfolio performance of the selected foreign joint venture commercial banks. To fulfill the objectives, an appropriate research methodology has been developed, which includes financial tools and valuation. The necessary data derived from annual report for the period of 2012-13 to 2016-17.

In the introduction chapter, it described the subject matters of the study, background of selected development banks, statements of the problem, objectives of the study and importance of the study.

Literature review sections included discussions on the conceptual framework on credit portfolio. It reviews the major studies relating with credit portfolio management of several authors and from the several books and journals.

Research methodology chapter explained impact of credit portfolio management of selected commercial banks. It includes introduction, research design, selection of sample sources of data collection, limitation of the study and method of analysis of financial and statistical tools.

Data presentation and analysis of data is to fulfill the objectives of the study by presenting the data and analyzing them with the help of various statistical tools and graph followed by the methodology.

Last Chapter included summary and conclusions on the basis of which the recommendations sector presents suggest to the studied commercial banks and the central bank.(NRB)

This study is basically the theoretical background of the different concepts that clarifies about the credit management of foreign joint venture commercial banks of Nepal.

5.2 Conclusion

The bank is a financial intermediary that accepts deposits and channels those deposits into lending activities either directly by loaning or indirectly through capital markets. It receives money from those who want to save in the form of deposits and it lends money to those who want to save in the form of deposits and it lends money to those who need it. It works as a channel between borrowers and savers and plays a major role in money multiplication. Credit portfolio plays significant role. For the credit portfolio management liquidity ratio should be analyzed. The fundamental analysis is all about getting an

understanding of a company, the health of its business and its future prospects. It includes reading and analyzing annual reports and financial statements to get an understanding of the company's comparative advantages, competitors, and its portfolio management. Actual position of an organization is reflected in its financial statements. Fundamental analysis of the companies is very important so as to have the glance of true picture of the company.

This study is successful to explore the findings of the results designed for the study. Various financial as well as statistical tools were used as per requirement of nature of data. Primary as well as secondary source of information were used for analysis of data. Based on the data analysis and finding of the result, the following conclusion can be drawn.

Current ratio of NABIL is higher than HBL, Cash and bank balance to total deposit ratio of HBL is more than NABIL. Similarly, Cash and bank balance to current deposit and saving deposit of HBL is higher than NABIL. Loan and advances to total deposit ratio of NABIL is higher than HBL. Similarly, loan and advances to total assets ratio of NABIL is higher than HBL. Hence, NABIL is able to mobilize its resources in lending as loan and advances than HBL. Investment portion of HBL is higher than NABIL. Gap between lending and borrowing of HBL is higher than NABIL. Return on loan and advances as well as interest income to total loan and advances ratio of HBL is higher than NABIL during the study period.

Net profit on total assets and EPS of NABIL is higher than HBL. Loan loss provision to Loan and Advances ratio of HBL is higher than NABIL. This means the investment and loan is grants in risky sector. Ratio of non-performing loan of HBL is higher than NABIL. HBL has kept high loan loss provision than NABIL because of high nonperforming to total lending ratio. NABIL has positive and significant relationship between total deposit collection and total lending. Where HBL has positive with significant relationship between these two variables. NABIL has positive with significant

relationship between total loan and advances and net profits. Where HBL has negative relationship between these two variables.

So, main findings of this study is that even NABIL bank has less liquid assets, it is able to maintain daily cash requirement, high lending ratio, low leverage ratio, low non-performing assets level, low loan loss provision ratio, high profit ratio than that of Nepal Bank (HBL). Therefore, the management of HBL must revise the lending policy and invest in profitable as well as productive sectors rather than only to increase lending ratio. Again, remarkable issue is that HBL has negative relationship between total loan and advances and net profit. SO, HBL has high granted non performing loan.

5.3 Recommendations

On the basis of the findings and study the following recommendations are made:

- NABIL and HBL, Both banks should be careful about customer satisfaction, employee motivation and competitive strength equally plays important role to gain success in the market. Loan and advances to total deposit ratio of HBL is very low, which is less than 35%. So, they still have opportunity to lend with minimum liquidity risk so they should identify the appropriate sector and lend for high return.
- HBL should adopt the sound credit collection policy. It helps to decrease loan loss provision and non-performing loan of the bank. Thus, the credit portfolio management of HBL must follow the policy as rapid identification of delinquent loans, immediate contact with borrower and continual follow-up until a loan is recovered to decrease its non-performing loan and loan loss provision.
- Banks should regularly follow the credit customers to confirm that whether the customers have utilized their credit for the same purpose or not, committed at the time of taking credit from the banks. Credit related financial indicators in Himalayan Bank Limited seem irrelevant in comparison with the specified standard of NRB. Therefore more focus should be given to improve the credit management of HBL, such that credit granting procedure, updating the credit

files, assure the value of collateral and maintaining the loan loss provision adequately

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Appendix -I

Correlation between Total Deposit and Total Loan & Advances of NABIL

(Rs. in billions)

S.no.	Year	X	Y	X^2	Y^2	XY
1	2012/13	31.92	21.37	1018.8864	456.6769	682.1304
2	2013/14	37.35	27.59	1395.0225	761.2081	1030.4865
3	2014/15	46.34	32.27	2147.3956	1041.3529	1495.3918
4	2015/16	49.6	38.03	2460.16	1446.2809	1886.288
5	2016/17	55.02	41.60	3027.2004	1730.560	2288.832
Total	**N= 5**	**220.23**	**160.86**	**10048.6649**	**5436.0788**	**7383.1287**

Where,

X = Total Deposit of NABIL

Y= Total Loan & Advances of NABIL

Here, $\Sigma X = 220.23$, $\Sigma Y = 160.86$, $\Sigma X^2 = 10048.6649$ $\Sigma Y^2 = 5436.0788$, $\Sigma XY = 7383.1287$

Now,

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

= +0.988

$$P.E. = 0.6745 \times \frac{1-r^2}{\sqrt{N}}$$

= 0.0072

Appendix -II

Correlation between Total Deposit and Total Loan & Advances of HBL

(Rs. in billions)

S.no.	Year	X	Y	X^2	Y^2	XY
1	2012/13	39.01	10.58	1521.78	111.936	412.726
2	2013/14	45.19	17.61	2042.136	310.112	795.795
3	2014/15	42.88	23.56	1838.694	555.073	1010.253
4	2015/16	46.81	24.61	2191.176	605.652	1151.994
5	2016/17	56.05	27.67	3142.724	765.629	1550.904
Total	**N= 5**	**229.94**	**104.03**	**10736.51**	**2348.402**	**4921.672**

Where,

X = Total Deposit of NBL

Y= Total Loan & Advances of NBL

Here, $\Sigma X = 229.94$, $\Sigma Y = 104.03$, $\Sigma X^2 = 10736.51$, $\Sigma Y^2 = 2348.402$, $\Sigma XY = 4921.672$

Now,

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

= +0.799

$$P.E. = 0.6745 \times \frac{1-r^2}{\sqrt{N}}$$

= 0.036

Appendix -III

Correlation between Total Loan & Advances and Net Profits of NABIL

(Rs. in billions)

S.no.	**Year**	**X**	**Y**	**X^2**	**Y^2**	**XY**
1	2012/13	21.37	0.74	456.6769	0.548	15.814
2	2013/14	27.59	1.03	761.2081	1.061	28.418
3	2014/15	32.27	1.14	1041.3529	1.299	36.789
4	2015/16	38.03	1.38	1446.2809	1.904	52.481
5	2016/17	41.6	1.69	1730.56	2.856	70.304
Total	**N= 5**	**160.86**	**5.98**	**5436.0788**	**7.668**	**203.806**

Where,

X = Total Loan & Advances of NABIL

Y= Net Profits of NABIL

Here, $\Sigma X = 160.86$ $\Sigma Y = 5.98$, $\Sigma X^2 = 5436.079$, $\Sigma Y^2 = 7.668$, $\Sigma XY = 203.806$

Now,

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

= +0.983

$$P.E. = 0.6745 \times \frac{1-r^2}{\sqrt{N}}$$

= 0.010

Appendix -IV

Correlation between Total Loan & Advances and Net Profits of HBL

(**Rs. in billions)**

S.no.	Year	X	Y	X^2	Y^2	XY
1	2012/13	10.58	0.250	111.936	0.063	2.645
2	2013/14	17.61	0.894	310.112	0.799	15.743
3	2014/15	23.56	0.249	555.073	0.062	5.866
4	2015/16	24.61	0.128	605.652	0.016	3.150
5	2016/17	27.67	0.176	765.629	0.031	4.869
Total	**N= 5**	**104.03**	**1.697**	**2348.402**	**0.971**	**32.273**

Where,

X = Total Loan & Advances of HBL

Y= Net Profits of HBL

Here, $\Sigma X = 104.03$ $\Sigma Y = 1.697$, $\Sigma X^2 = 2348.402$, $\Sigma Y^2 = 0.971$, $\Sigma XY = 32.273$

Now,

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

= -0.356

$$\text{P.E.} = 0.6745 \times \frac{1-r^2}{\sqrt{N}}$$

= 0.263

Credit Portfolio of Foreign Joint Venture Commercial Banks of Nepal

A Comparative Study on NABIL Bank Limited and Himalayan Bank Limited

A Proposal

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Submitted to

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CHAPTER - I

INTRODUCTION

A credit portfolio is an investment portfolio comprised of debts, like home and car loans. Private investors can build credit portfolios, but more commonly they are held by banks and other financial institutions. Credit portfolio management refers to the process of building a series of investments based upon credit relationships and managing the risks involved with these investments. Such a portfolio gains its value from the interest from issued loans but is susceptible to credit default. For that reason, credit portfolio management includes assessing the risk involved with each potential loan and analyzing the total amount of risk the portfolio incurs as whole.

1.1 Background of the Study

Financial sector is required for proper mobilization of investable resources from one sector to another and plays a pivotal role in bridging a gap between deficit units and surplus units. Efficient financial sector mobilizes saving from a broad variety of sources and allocating them into more productive uses, thus bridging benefits to both investors and investee and to the economy overall. In the process of reinvesting these savings, they successfully deal with one fundamental factor i.e. risk. The growth in liquidity of credit markets and the active management of credit risk are among the most significant developments in commercial banking in the past 20 years. These developments hold the potential to permanently reduce the risk profile and improve the financial performance of commercial banks.

Credit portfolio management grew out of the need to improve the financial performance of the large corporate loan portfolios in commercial banks. It is paradoxical that these portfolios created the biggest problems for originators and investors in the marketplace. After all, large corporate loan portfolios typically are composed of loans, commitments, and other lending exposures to banks' most creditworthy customers. Lending is the backbone of commercial banking, so lending

is what banks should do best. Yet these portfolios proved to be the source of recurring problems and the cause of failure for many commercial banks.

Nepal is a developing country. It faces many problems for its economic development and to make expansion in financial sector. In our economy banking system and the Financial Institutions play very significant role in the economy. First and foremost is in the form of catering to the need of credit for all the sections of society. The modern economies in the world have developed primarily by making best use of the credit availability in their systems. An efficient banking system must cater to the needs of high end investors by making available high amounts of capital for big projects in the industrial, infrastructure and service sectors. Financial institutions (FIs) are very important in any economy. Their role is similar to that of blood arteries in the human body, because FIs pump financial resources for economic growth from the depositories to where they are required (Shanmugan & Bourke, 1990). Commercial banks (CBs) are FIs and are key providers of financial information to the economy. They play even a most critical role to emergent economies where borrowers have no access to capital markets (Greuning & Bratanovic, 2003). "Sustainable development is about capital allocation and thus should be at the core of financial markets activity. Hence, the financial institutions can be the major stakeholder in achieving sustainable development (Delphi International Limited, 1997).

Financial market is very important for the economic growth of the country (Economic Survey, 2013) as they are guided by finance. The pace of development of a country largely depends upon its economic activities. Financial institutions provide capital to develop trade, industry and business. Bank, finance companies, cooperative societies, insurance companies, stock exchanges help in the economic progress of a nation (Economic Survey, 2004) Banks are major institutions in financing.

The financial institutions play a key role in development of a national economy because it functions as a medium of collecting and mobilizing resources to finance a business and development project that are essential for economic development (Eichengreen, 1997). A

country without good financial system can be a major problem for the economy to function properly, to mediate sustainable private investment and promote entrepreneurship.

Financial institutions ease market friction and influence the allocation of resources over different sectors of the country (Levine, 2004). The author introduces five key functions of financial system that are essential to economic growth.

- Produce information about possible investment and allocation capital
- Monitor investments and provide expert corporate governance
- Facilitate the trading, diversification and management of risk
- Mobilize and pool saving
- Ease the exchange of goods and services.

This way banks help to fortify the national development (Economic Survey, 2004/05). Banking is one of the most heavily regulated businesses in the world. Banks are among the most important financial institutions in the economy. They are the principal source of credit (loan-able funds) for millions of individuals and families and for many units of governments. Moreover, banks often act as a major source of credit to small local business for their stock. Banks are among the most important sources of short-term working capital for business and have become increasingly active in recent years in making long-term business loans for new plant and equipment (Shekher & Shekher, 2005). Banks are those financial institutions that offer the widest range of financial services especially credit, savings, payment services and perform the widest range of financial functions of any business firm in the economy.

Banks are expected to support their local communities with a sufficient supply of credit for all lawful business and consumer needs to price that credit reasonably in line with competitively determined interest rates. Bank loan support the growth of new businesses and jobs within the banks trade territory and promote economic vitality. Banks made a wide variety of loans to a wide variety of customers for many different purposes from purchasing automobiles and buying new furniture, taking dream vacations or pursuing college educations, to constructing home and office buildings. Loans may be divided as; real estate loans, financial institution loans,

agricultural loans, commercial and industrial loans, loans to individuals, miscellaneous loans, lease financing receivables etc.

In addition to the above traditional role, the banks and the financial institutions also perform certain new-age functions which could not be thought of a couple of decades ago. The facility of internet banking enables a consumer to access and operate his bank account without actually visiting the bank premises. The facility of ATMs and the credit/debit cards has revolutionized the choices available with the customers. The banks also serve as alternative gateways for making payments on account of income tax and online payment of various bills like the telephone, electricity and tax. The bank customers can also invest their funds in various stocks or mutual funds straight from their bank accounts. In the modern day economy, where people have no time to make these payments by standing in queue, the service provided by the banks is commendable.

Going through loan granting provision, bank will look through safety of funds, purpose of loans, security for loans, profitability spread of loan portfolio etc. Besides this, the character of person receiving credit, the capacity of borrower to utilize the fund, the percentage of borrower stake in the business are the basic elements which measure the excellence of borrower and finally the quantity of the loan. This way bank plays an important part in the development of trade, commerce and industry. Today no banker can survive for long run without proper standing of economy and cannot go ahead without proper banking system built.

Banks and financial intuitions have played major role in the economic development of the country and most of the credit- related schemes of the government to uplift the poorer and the under-privileged sections have been implemented through the banking sector. The role of the banks has been important, but it is going to be even more important in the future.

1.2 Profile of Sample Enterprises

1.2.1 NABIL BANK

(NABIL), the first foreign joint venture commercial bank of Nepal, started operations in July 1984.Nepal Arab Bank Limited was integrated with the objective of extending international standard modern banking services to various sectors of the society. Pursuing its objectives, the bank provides a full range of commercial banking services through its 19 points of representation across the country and over 170 reputed correspondent banks across the globe.

NABIL, as a pioneer in introducing many inventive products and marketing concepts in the domestic banking sector, represents a milestone in the banking history of Himalayanas it started an era of modern banking with customer satisfaction measured as a focal objective while doing business. Highly qualified and experienced team of NABIL bank manages day-to-day operations and risk management. Bank is fully equipped with modern technologies including ATMs, credit cards, state-of-art, world-renowned software from Infosys Technologies System, Banglore, India, Internet banking system and Tele-banking system.

NABIL Bank Limited is providing full-fledged commercial banking services to its clients. From its inception period in 1984 as the first joint venture bank, to commence operations in the Kingdom of Nepal, the bank have been a leader in terms of bringing the very best international standard banking practices, products and services to the kingdom. Today, mission of the bank is to be the "Bank of 1st Choice" to all of its stakeholders and customers.

1.2.2 Himalayan Bank Limited (HBL)

Himalayan Bank Limited, The first bank of Nepal was established in November 15, 1937 A.D (Kartik, 30, 1994). From the very conception and its creation, Himalayan Bank Ltd, was as joint venture between the government and the private sector. Out of 2500 equity shares of NRs. 100 face value, 40% was subscribed by the government and the balanced i.e. 60% was offered for the sale to private sector. There were only 10 shareholders when the bank first started. The total

deposits for the first year was NRs. 17,02,025 where current deposits was about NRs. 12,98,898 fixed was about NRs. 3,88,964 and saving was NRs. 14,163. Loan disbursed and outstanding at the end of the first year was NRs. 1,985,000.

During the past 7 decades, the bank experienced many ups and downs, but it has remained the leading financial institution in Nepal. In early stage bank has provided its services to customers and government manually. Now, it has been using advanced technology to provide banking facilities. Himalayan Bank Limited has helped vastly in developing the country by accumulating the scattered money in small amount in each and every nook and corners of the country and granting loan and advances in various ways. The bank has been tendering modern banking services to the different sectors of the economy like manufacturing and service industries, hydropower projects, traders, small entrepreneurs and the weaker sections of the society through more than 110 branches which spread through all over the five development regions of the country. Himalayan Bank has introduced its ever waited NBL Debit Card by joining the hands with Smart Choice Technologies (SCT), the first company in Nepal to provide networked ATMs.

1.3 Focus of the Study

The study is focused on evaluating the deposit utilization of the sample banks, in terms of loans and advances, investment and its contribution to the profitability of the bank, commercial banks hold deposits of many individuals, government and business units. They make funds available through their lending and investing activities to borrowing individual business firms and government also to evaluate the inter-action of credit risk within a portfolio exposures (especially default correlation), and how these can be measured and quantified.

Here, the study focuses mainly to highlight and examine the credit portfolio of the selected joint ventures banks ignoring other aspects of bank transaction. To highlight the credit portfolio management of the bank, the research is based on the certain statistical tools i.e. mean, standard deviation, co-efficient of variation, coefficient of correlation, and probable error with a view to find out the true picture of the bank. The main objective of this research is to analyze how credit portfolio modeling is used within risk management and regulatory and economic capital process

1.4 Statement of the Problem

Commercial banks in Nepal have been facing various challenges and problems. Some of them arising due to the economic condition of the country, confused policy of government and many due to default borrowers. After liberalization of economy, banking sector has various opportunities.

However, the financial institutions are increasing regularly. Liquidity is in maximum level with the financial institutions. Hence, the banks and financial institutions are competing among themselves to advance credit to limited opportunity sectors. Banks and financial institutions are investing in house loan, hire purchase loan for safety purpose. Due to lack of good lending opportunities, banks are facing problems of liquidity. Currently, banks have increasing number of deposits in fixed and saving accounts but have decreasing trend in lending behaviors. So, this has caused major problems in commercial banks.

Nowadays, due to competition among banks, the interest rate charge for loan is in decreasing trend. Due to unhealthy competition among the banks, the recovery of the bank’s credit is going towards negative trends. Non-performing credits of the banks are increasing year by year. To control such type of state, the regulatory body of the banks and financial institutions, NRB (Nepal Rastra Bank) has renewed its directives of the credit loss provision. Therefore, it is necessary to analyze the 'credit management' or credit disbursement recovery provision for loss and write off of the credit. As the sample of commercial banks, Himalayan Bank Limited and Nepal Arab Bank Limited have been selected.

The research problems may be stated in the form of following questions:

1. What is the level of liquidity in case of the sample banks?
2. What is the volume of credit and advances made by the sample banks?
3. What is the deposit collection and utilization trend of the sample banks?
4. What is the relationship of deposits, loan and advances and net profits of the sample banks?

1.5 Objectives of the Study

The main objective of this study is to examine the credit portfolio of NABIL Bank Limited and Himalayan Bank Limited. The specific objectives of the study are as follows:

1. To analyze the risk and return associated with the portfolio investment (i.e. investment on loans, advances and overdraft, company shares and treasury bills) of the selected commercial banks.
2. To evaluate the portfolio performance of the selected foreign joint venture commercial banks.

1.6 Significance of the Study

At present the joint venture banks are gaining a wide popularity through their efficient management and professional services and playing an eminent role in the economy. Lending is one of the main functions of commercial banks where the whole banking business is rested upon. Study on joint venture commercial bank and especially their lending practices; carry a great significance to shareholders of the bank, to the professionals, to the students who wants to know about lending practices of commercial banks. This study adds new ideas and findings about the concerned joint venture banks.

This study will have importance to various groups but in particular is directed to a certain groups of people/organizations, which are important to: i) shareholders, ii) management bodies of the bank for evaluation of bank's performance, iii) "outsiders" who are mainly customers, finance agencies, stock exchanges etc, iv) the government bodies or the policy makers such as central bank, v) interested outside parties such as investors, customers (depositors as well as credit takers), competitors, personnel of the banks, stockbrokers, dealers, market makers etc.

1.7 Methodology of the Study

A research is in depth study for the advancement of the knowledge about the subject matter. Similarly, research methodology is the process of arriving at the solution of the problem through planned and systematic dealing with the collection, analysis and interpretation of facts and

figures. Methodology of the study is the process of arriving at a solution of the problem through planned and systematic dealing with the collection, analysis and interpretation of facts and figures.

1.7.1 Study, Plan and Design

Study design is the framework of the activities taken during formulating, implementing & controlling the study so as to obtain answers to research questions & to control variance. It encompasses the methodology and procedures employed to conduct scientific research that includes the tools and techniques for the data collection and analysis sampling plan.

1.7.2 Sample Criteria and Population

Among the total population of the commercial banks, two joint ventures commercial banks are taken as sample for the study. In the study, NABIL Bank Limited and Himalayan Bank Limited are taken for the study of credit portfolio management. Thus certain criteria of two commercial banks are taken into consideration as sample for the study. Selection of these two banks can be justified with the fact that they were established before 1995. Besides that they are the foreign joint venture banks of Nepal.

1.7.3 Sources of Data

The report will mainly based on secondary data and data collection from primary sources. The data required for the analysis will be directly obtain from balance sheet and P/L account of the concerned banks annual reports. Supplementary data and information will be collect from number of institutions and regulating authorities like NRB, SEBSON, NEPSE, budget speech etc. All the secondary data will be complied, process and tabulate in time series as per the need and objectives of the study.

1.7.4 Instruments

The motive of the study will identify the credit portfolio management of two foreign joint venture banks of Nepal. Various statistical tools like Mean, Standard deviation, Covariance, Trend analysis, coefficient of correlation, Regression analysis etc.

1.8 Limitations of the Study

To complete this research, the researcher follows the different books, journals, articles and dissertations. Thus, reliability of the study is based on those things. This study will not examine the credit portfolio of all commercial banks due to lack of time, the study will see only the credit portfolio of two foreign joint venture commercial banks NABIL Bank Limited and Himalayan Bank Limited.

This study will cover only the past five year's period since 2012/13 to 2016/17. To prepare this report, secondary data are collected from annual general meeting (AGM)'s reports of the listed banks and trading reports of NEPSE. Primary information is collected from respective office and related persons. It may not cover the whole qualitative and quantitative analysis of the commercial banks because of time and resource constraints.

The research study has some limitations. The main limitations of the study are as follows:

a. Though, several commercial banks have been established in Nepal, only two commercial banks are taken for the proposed study.
b. This study concentrates only on credit portfolio of selected commercial banks.
c. The secondary data will be used for presentation and interpretation. Only a five years data will be considered.
d. This study is only a case study; hence the conclusion drawn from the study does not ensure wide applicability in all types of enterprise running in different situations.
e. Major portion of analysis and interpretation have been done on the basis of available secondary data and information. Thus, reliability of the study is based on trueness of collected data and information.
f. In this study, only selected financial and statistical tools as well as techniques are used.

1.9 Organization of the Study

The present study is organized in such way that the stated objectives can easily be fulfilled. The structure of the study will try to analyze the study in a systematic way. The study report has presented the systematic presentation and finding of the study. The study report is designed in five chapters which are as follows:

Chapter I: Introduction

This chapter describes the basic concept and background of the study. It has served orientation for readers to know about the basic information of the research area, various problems of the study, objectives of the study and need or significance of the study. It is oriented for readers for reporting giving them the perspective they need to understand the detailed information about coming chapter.

Chapter II: Review of Literature

Review of Literature is a way to discover what other research in the area of similar field has uncovered. Hence second chapter assures the reader to find out what research studies have been conducted in chosen field of study, and what remains to be done.

Chapter III: Research Methodology

Research methodology refers to the various sequential steps to be adopted by a researcher in studying a problem with certain objectives in view. It describes about the various source of data related with study and various tools and techniques employed for resenting the data.

Chapter IV: Data Presentation and Analysis

The general purpose of this chapter is to examine the processes by which the meaning and implications of research data can best be extracted. Hence, this chapter first explains methods of organizing data by tabulation and then placing in presentable data by using figures and tables & also major procedural steps involved in the analysis of data will be discussed.

Chapter V: Summary, Conclusions and Recommendations

On the basis of the results from data analysis, the researcher will conclude about the performance of the concerned organization for better improvement

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