

CHAPTER-I

INTRODUCTION

1.1 Background of the Study

Liquidity management is of crucial importance in financial management decision. The optimal of liquidity management is could be achieve by company that manage the trade-off between profitability and liquidity management (Bhunia& Khan, 2011). Liquidity risk threatens the solvency position of financial institutions. It also negatively affects the health of the institutions. There are two types of liquidity risks (i.e., first type and second type) arise in the financial institutions although they can raise the funds by running down their cash assets, borrowing additional funds in the money markets and selling off other assets (Shrestha, 2012) In case of commercial banks, first type of liquidity risk arises when depositors of commercial banks seek to withdraw their money. They become insolvent if the assets are not enough to meet the liability withdrawals. Similarly, the second type of liquidity risk arises when money supply cannot meet the demand of unexpected loans due to the lack of the funds (Baral, 2005).

Commercial banks' liquidity exposure can be measured by analyzing the sources and uses of liquidity. In this approach, total net liquidity is worked out by deducting the total of uses of liquidity from the total of sources of liquidity. Different liquidity exposure ratios such as borrowed funds to total assets, core deposit to total assets, loans to deposits, and commitments to lend to total assets are used to measure the liquidity position of a commercial bank (Saunders & Cornett, 2004). Nepal Rastra Bank (NRB) has used three financial ratios to measure the liquidity position of commercial banks; viz., NRB balance to total deposit ratio (NRBTDR), Cash vault to total deposit (VTDR), Total liquid fund to total deposit ratio (LFTDR) (NRB, MidJuly 2011). Profitability is a measure of firm's efficiency (Khan & Jain, 1998). It is also a control measure of the earning power of a firm as well as operating efficiency. Weston and Copland (1998) described profitability as net result of a large number of policies and decisions. Ratios are used to measure profitability and give final answers to how effectively the firm is being managed in terms of its financial performance. Therefore, management, creditors and owners are also interested in the profitability ratio of the firm (Pandey, 1995). Short-term profitability refers to a firm's ability to make an operating profit for which financial ratios on a yearly basis are used

(Bierman&Smidt, 1980). This study also did not emphasize the liquidity management. Shrestha (2012) found an association between liquidity and profitability of commercial banks in Nepal, with data up to 2003/04- 2009/10 of 8 private commercial banks taken into consideration. Earlier, Elumilade et al. (2006) described investment decision as one of the most significant decision-areas that affect the future profitability either because it might increase revenues or because it can cause an increase in efficiency and reduction in costs. But, the study did not cover the effects of liquidity on profitability. Pradhan (2007) evaluated the financial ratios, financial distress and stakeholder losses in corporate restructuring and attempted to explain the behavior of financial ratios in financially distressed firms. Regmi (2005) analyzed the profitability of Nepalese commercial banks by analyzing the relationships between EPS, DPS and MPS of the banks. The study, however, did not deal with the profitability forecasting through liquidity ratios. Previous studies were related to profitability as well as profit planning and control for manufacturing companies but the number of studies in the commercial banking is smaller. Moreover, those studies did not examine the effect of liquidity on profitability of the Nepali banking sector. The current study is an attempt towards fulfilling this lacking to some extent.

Liquidity means a matter of maintaining what the bank has promised to pay the depositors -cash. In order to fulfill the promise, primary reserves are the first drawn on to satisfy depositors. In the banking system primary reserves are known as legal reserve and working reserves. The term is economic rather than accounting concept. Legal reserves are the requirement of monetary authority. Bank management, student of banking studies and monetary authority are referring the other names for primary reserve to designate certain ideas and concept regarding banks' assets. Primary reserves include non-earning assets such as cash in vault, the deposits carried out by banks with correspondent banks and central bank, and cash items. The cash items represent cheques held or in process of collection by the banks. The objective of primary reserves in banking system is maintaining liquidity and solvency(Sinke, 1983).

The amount of liquidity that a commercial bank or the commercial banking system should maintain is one of the basic problems of the bank management. If too much liquidity is maintained, it means that the bank and the banking system are foregoing income. Too, little, however, may be fatal not only to an individual bank but to the commercial banking system as a

whole, the financial structure of the country, and the economy of the nation. Too little liquidity and the demands of the depositors in the form of 'runs' on the banks are like oil and water, they do not mix well (Reed; 2002).

1.1.1 Introduction to Selected Bank

Everest Bank limited

Everest Bank limited is a name you can depend for professionalized and efficient for banking services. It has 9 laces customer. Founded in 1994 the bank has been one of the leading bank of the country and has been catering its service to various segments of the society. With the clients from all walks of life agriculturally and industrially.

Punjab National Bank its joint venture partner (holding 20% equity) is the largest nationalized bank in India having presence virtually in all import centers. Everest Bank Limited provide customer friendly service through its wide network connected ABBS system, which enable customer for the operational transaction any branches. The bank has 80 branches, 113 ATM counters, 7 extension counter and 28 revenue collection counters across the country making anytime anywhere.

Standard Chartered Bank Nepal Limited

Standard Chartered Bank Limited, which was formerly known as Nepal Grindlays Bank, was established in 1987 A.D. as a second foreign joint venture bank under the company act. Its ownership is 75% of the shares held by Standard Chartered Grindlays Bank, 25% of shares by local ownership. Standard Chartered Bank completes 30 years of operation in 2017. This was

considered a unique opportunity to refresh the Brand. Standard Chartered plays an active role in supporting those communities in which its customers and staffs live. The focus of the Standard Chartered group is on projects that assist needy children, particularly in the area of education and environment. The bank is in a position to service customers through a large domestic network. In addition to which the global network of Standard Chartered Bank gives the Bank the unique opportunity to provide truly international banking in Nepal. SCBNL Standard Chartered Bank focuses mainly on corporate and consumer banking, catering to a wide range of customers from individuals, to mid-market local corporate to multinationals and large public sector companies as well as embassies, aid agencies, airlines, hotels, and government corporations. The bank has been the pioneer in introducing consumer-focused product and services in the country. With the mission statement “To be the leading international bank in our principal markets”, the bank operates through 13 offices, spread throughout Nepal and focuses mainly on corporate, consumer and commercial banking, providing services for international firms as well. The bank contributed to a large extent in the development of the country by the way of loans to industrial projects, the priority and deprived sectors.

1.2 Focus of the Study

Liquidity management refers to as using money to get long-term benefit. Investment in its broad sense means the sacrifice of certain percent value for (possible uncertain) future value. In pure financial sense, the subsequent use of the term investment will be in the prevalent financial sense, of the placing of money in the hands of other for their use, in return for a proper instrument entitling holder's to fixed income payment or the participation in expected profits. The present economic position of Nepal is encouraging the savers to deposit their money in banks rather than investing in stocks, assets and new business etc., which in turn is hampering the bank's portfolio because deposits are higher and limited safe investment areas are decreasing day by day. In spite of low interest rate, the depositors are feeling secured towards commercial banks but the highest surplus deposits are almost idle in the bank due to continuous fall in Nepalese economy because of conflict situation, changed taxation policy, and adversely affected tourism industry and agricultural industry. It revolves round the concept of managing the surplus financial assets in which way, which leads to the wealth maximization and provides a significant future source of income. It focuses on analyzing the causes of investment problems, their

management and remedies, and developing the new investment areas and sectors, which can again boost the Nepalese economy.

1.3 Statement of the Problem

Banks should have ready access to immediately expendable funds at reasonable cost precisely at the time those funds are needed. Lack of adequate liquidity is often one of the first signs that a bank is in serious financial trouble (Rose, 1999). Banks should have adequate liquidity to minimize both asset side liquidity risk and liability side liquidity risk of a commercial bank. Both the liquidity deficit and more liquidity surplus indicate the problem in the financial health of a commercial bank. More liquidity surplus hurts the profitability of the commercial bank as it reduces the return on assets. Similarly, liquid deficit also costs much to the commercial banks in term of the higher purchasing price of liquidity and affects the reputation of the banks. Therefore, the commercial banks should strike the trade-off between the profitability and liquidity risk. The commercial banks are a major player in Nepalese banking sector and financial services industry. Government-owned banks, Nepal Bank Ltd and RastriyaBanijya Bank, are in operation for several decades, foreign joint venture and private banks also started operating since 1984 after the establishment of Nepal Arab Bank Ltd., currently NABIL Bank (Strait, 2009). However, previous studies regarding their profitability and liquidity positions are the area in which researchers, scholars, policy-makers and managers would be interested. Deposit utilization rate of the commercial banks in Nepal is not stable. The growing competition among financial institutions and recent increase in transaction of security and capital markets as well as the taxation laid on higher deposits in banks is adversely affecting the bank's profitability. The commercial banks in Nepal have not succeeded much in mobilizing their capital in productive sectors. A proper effective, efficient and economic media for collecting resources has not been designed to collect the funds in Nepal. So, the banks are attracting the depositors through mass-media with different plans to attract depositors to the maximum possible extent. Inefficiency and weaknesses relating to the analysis of financial statements affect the banks' financial performance. For instance, these banks' cash and bank balance and NRB balance have a fluctuating and declining trend while various deposits have been increasing; it reflects inefficiency in liquidity management of the banks. The following research questions have been set:

1. What is the profitability position of commercial banks in Nepal?
2. What is the liquidity position of commercial banks in Nepal?
3. Does liquidity affect the profitability of commercial banks in Nepal?

1.4 Objective of the Study

The main objective of the study is to investigate the impact of liquidity on the profitability of commercial banks Nepal with reference to Everest Bank Limited and Standard Chartered Bank Limited. The specific objectives of this study are as follows:

1. To assess the profitability position of commercial banks in Nepal.
2. To evaluate the liquidity position of commercial banks in Nepal.
3. To examine the impact of liquidity on profitability of commercial banks in Nepal.

1.5 Significance of the Study

Nepalese commercial banks are operating in the competitive environment. In this situation, banks have to adopt suitable strategies for their existence. They should balance and co-ordinate the different functional areas of business concern. The success or failure of any organization depends on its strategy, which is affected by working capital management. Working capital management is the problem to prepare proper strategy on its favor. The study helps to know how well the banks are utilizing their deposits. It is important to policy makers and academic professionals to formulate policies and plans based on the performance of these banks. The study also guides to investors, customers (depositors, loan takers as well as other types of clients), competitors, personnel of the banks, stockbrokers, dealers, market makers, etc. to take various decisions regarding deposits and borrowings

1.6 Limitations of the Study

The study has following Limitations:

- The study is based only on secondary data so it may contain reporting errors.
- There are total, 28 commercial banks in the financial market but this researcher takes only two from them. The sampled banks are Everest Bank and Standard Chartered Bank.

- The study covers the past and present state of the commercial banks in Nepal and will not make any projection in future.
- The study is made within limited timeframe, limited data, and with lack of research experiments.
- This research used only the selective tools for analysis and interpretation of data.
- Only limited statistical and financial tools, including simple average, profitability ratio (i.e., ROE) and other five liquidity ratios as well as simple regression models were used for data analysis. Not using more scientific and sophisticated tools may limit the validity of the study-findings.

1.7 Organization of the Study

The first chapter includes general background of the study, historical perspective of banking industry, overview of sample banks, statements of the problem, objectives of the study, significance of the study and limitation of the study. The second chapter, review of literature contains the review of related books, journals, and past research works. Similarly the third chapter expresses the way and the technique of the studying applied in the research process. It includes research design, population and sample, data collection procedure and processing, tools and methods of analysis. The fourth chapter is the important chapter in which collected and processed data are presented, analyzed and interpreted with using financial tools as well as statistical tools. Finally, the fifth and the last chapter provide the summary of the study, conclusion and recommendation.

CHAPTER – II

REVIEW OF LITERATURE

2.1 Conceptual Review

Liquidity refers to how quickly and cheaply an asset can be converted into cash. Money (in the form of cash) is the most liquid asset. Assets that generally can only be sold after a long exhaustive search for a buyer are known as illiquid. Managing liquidity involves estimating liquidity needs and providing for them in the most cost-effective way possible. Banks can obtain

liquidity from both sides of the balance sheet as well as from off-balance-sheet activities. A manager who attempts to control liquidity solely by adjustments on the asset side is sometimes ignoring less costly sources of liquidity. Conversely, focusing solely on the liability side or depending too heavily on purchased wholesale funds can leave the bank vulnerable to market conditions and influences beyond its control. Effective liquidity managers consider the array of available sources when establishing and implementing their liquidity plan (Khubchandani, 2002).

Liquidity means a matter of maintaining what the bank has promised to pay the depositors -cash. In order to fulfill the promise, primary reserves are the first drawn on to satisfy depositors. In the banking system primary reserves are known as legal reserve and working reserves. The term is economic rather than accounting concept. Legal reserves are the requirement of monetary authority. Bank management, student of banking studies and monetary authority are referring the other names for primary reserve to designate certain ideas and concept regarding banks' assets. Primary reserves include non-earning assets such as cash in vault, the deposits carried out by banks with correspondent banks and central bank, and cash items. The cash items represent cheques held or in process of collection by the banks. The objective of primary reserves in banking system is maintaining liquidity and solvency (Sinkey, 1983).

The amount of liquidity that a commercial bank or the commercial banking system should maintain is one of the basic problems of the bank management. If too much liquidity is maintained, it means that the bank and the banking system are foregoing income. Too, little, however, may be fatal not only to an individual bank but to the commercial banking system as a whole, the financial structure of the country, and the economy of the nation. Too little liquidity and the demands of the depositors in the form of 'runs' on the banks are like oil and water, they do not mix well (*Reed ;2002:115*).

2.1.1 Practice of Liquidity Management in Nepalese Commercial Banks

Nepal Rastra Bank (NRB) is the regulatory body of the banking industry. NRB issues the rules and regulations to facilitate the banking operation in Nepal like other regulations. There is a regulation for maintaining liquidity by commercial banks. Revision in monetary policy and operational procedure is continuation from time to time. The regulation is called Cash Reserve

Ratio (CRR). It is directly related to the liquid assets of commercial banks. The regulation specifies the cash reserve ratio of commercial to central bank and its own vault to operate day-to-day operation (transaction). It is a policy instrument of central bank for money supply. Money supply is a variable of monetary policy through which the bank plans to maintain adequate liquidity in the economy. It changes as per the requirement of the economy. According to the central bank's regulation, commercial banks need to consider the following rule to calculate Total deposit means liquid, saving and fixed deposit account as well as call money deposit and certificate of deposit. For this purposes, deposits held in convertible foreign currency, employee guarantee amount and margin account would not be included.

- a. Fixed deposit means a deposit in local currency accepted with a condition to repay on
- b. Completion of stipulated time period.
- c. Liquid and saving deposit means all deposit accounts other than fixed deposit.
- d. Cash in vault shall include only the local liquid and foreign currency (except clearing cheque)

A complete procedure for compliance test is in place. Failure in any respect under the regulations liable to pay penalty at a very high rate of interest. Procedures for compliance test are as follows:

- a) The cash reserve requirement is examined on a weekly basis.
- b) The cash reserve requirement shall be examined against the average weekly balance of deposit liabilities of immediately preceding 4th week. In case of full holiday in the preceding 4th week, the average deposit of immediately preceding 5th week shall be considered.
- c) Only the balance held in ordinary account with Nepal Rastra Bank (NRB) shall be eligible for inclusion in cash reserve. Balance held with NRB in special accounts opened for specific purpose and foreign currency accounts shall not be included for this purpose.
- d) For the purpose, all branches offices of the bank shall constitute as one unit.
- e) The central bank monitors that the regulation is followed or not.

2.1.2 Liquidity Monitoring Framework of Nepal Rastra Bank

Liquidity means a matter of maintaining what the bank has promised to pay the depositors -cash. In order to fulfill the promise, primary reserves are the first drawn on to satisfy depositors. In the banking system primary reserves are known as legal reserve and working reserves. The term is economic rather than accounting concept. Legal reserves are the requirement of monetary authority

1) Ratio Approach: Liquid Assets to Short Term Liabilities

Liquid Assets to Short term Liabilities = Unencumbered Liquid Assets / 100

Short term Liabilities coming due in 30 days

For the liquidity monitoring purpose, Liquid assets are defined as;

Liquid Assets is the sum of;

- Cash
- Bank Balance
- Money at calls at short notice
- Investment in Government Securities and Reverse Repo
- Placement up to 30 days

Liquid assets should include unencumbered liquid assets only. Unencumbered assets are those assets which are free from any debt obligation and can be easily sold or mortgaged.

Short Term Liabilities/Cash Outflows

Similarly short-term liabilities are the immediate obligations of the banks. Banks and financial institutions should have sufficient liquid assets to meet expected outflows over the next 30 days. Total short term liabilities (cash outflows) are total expected outflows over the next 30-day period. Each item will have an assumed 30-days outflow based on the defined contractual obligation. Short term liabilities in the above ratio include;

On Balance Sheet Item:

- 20% of Current Deposit
- 15% of Saving Deposit

- 50% of Call Deposit
- 100 % of Margin Deposits to be paid within next 30 days
- 100% of Fixed Deposit maturing in next 30 days
- 100 % of borrowing from the NRB which should be paid in next 30 days
- 100% of borrowings from other Banks and financial Institutions maturing in next 30 days
- All other contractual obligations coming due within 30 days). Fundamentals of Investments.

Off-balance sheet items:

- 100% of LC amount to be settled within next 30 days.
- 100% of Irrevocable loan commitments
- 100% of Acceptance liabilities maturing within next 30 days.

A bank having sufficient pool of liquid assets to cover its liability is considered a bank having satisfactory liquidity position. Quantifying same principle, when liquid assets to short term liabilities is more than 100%, the bank has sufficient liquid assets to meet its obligation reflecting a comfortable scenario in terms of liquidity. The ratio shall be monitored on a weekly basis. Other Liquid assets and liabilities, which are not defined, should be included on the remaining term to maturity.

Reporting Requirement: The report should cover the assets and liability portion as stated From Sunday to Friday of every week.

- Interval: weekly (as on Friday of every week).
- Submission Every Tuesday for immediate Past week.

2. Deposit and Credit Concentration

- A. Top 10 Depositors: Corporate
- B. Top 10 Depositors: Individual
- C. Top 10 Borrowers: Funded Only

Reporting Requirement:

- Interval: Monthly (as on month end data).
- Submission: Every month; within 7th of following month of Nepali calendar

3. Inter-bank Transaction

- Number of times the bank borrowed during the period (one week):
- Number of rollover of the borrowing from same institution (regardless of partial payments):
- Outstanding borrowing at the end of the reporting period
- Maximum amount of borrowing in one transaction: (Rs in lakhs)
- Average borrowing per transaction: (Rs in lakhs)

(Sum of all the borrowing during the period divided by number of transactions)

Reporting Requirement:

- Interval: weekly (as on Friday of every week).
- Submission: Every Tuesday for immediate past week.

4. Borrowing from NRB

New reporting formats are developed for the banks and financial institutions. They are;

A. Repo Monitoring

- Number of times the bank used Repo facilities during the last month:
 - Outstanding repo at the end of the period:
 - Maximum amount Per Transaction: (Rs in Lac)
 - Average Amount Per Transaction: (Rs in Lac)
- (Sum of all the Repo transaction during the period divided by number of transaction)

Reporting Requirement:

- Interval: weekly (as on Friday of every week).
- Submission: Every Tuesday for immediate Past/Previous week.

B. SLF Monitoring

- Number of times the bank used SLF facilities during the week:
- Outstanding SLF at the end of the period:
- Maximum Amount Per Transaction: (Rs in Lakhs)
- Average Amount Per Transaction: (Rs in Lakhs)
(Sum of SLF amount during the period divided by number of transaction)

Reporting Requirement

- Interval: weekly (as on Friday of every week).
- Submission: Every Tuesday for immediate Past week.

C. Refinance from NRB

Outstanding amount of Refinance facilities from NRB:

Number of times the bank utilized the facility during the last one month period:

Reporting requirement:

- Interval: Monthly.
- Submission: Every month; within 15th of following month of Nepali Calendar.

D. Outright Sales

Reporting Requirement:

- Interval: Monthly.
- Submission: Every month; within 15th of following month of Nepali Calendar.

5. Matching Assets and Liabilities: Liquidity Profile/ Structural Liquidity Table

In addition to above information, banks are required to submit the assumption made for categorization of the assets and liabilities (which has no fixed maturity) under different time buckets. For example;

Assumptions on:

- Categorization of Current Deposit
- Categorization of Saving Deposit
- Assets and liability categorization which have no fixed maturity.

Negative net assets during the one week, one month, 31-90 days and 91-180 days buckets exceed the limit of 5 %, 10%, 15 % and 20% of the total liabilities in the respective time buckets, the bank need to show by way of a foot note as to how does it propose to finance the gap to bring the mismatch within the prescribed limits.

Reporting requirement:

- Interval: Monthly (as on month end data).
 - Submission: Every month; within 7th of following month of Nepali Calendar
- Note: Bank refers to A, B and C class institutions licensed by Nepal Rastra Bank.

2.2 Liquidity provision as per NRB Directives

Provisions Relating to Compulsory Reserve/Statutory Liquidity

The following directives have been issued with regard to compulsory reserve and liquid assets to be maintained by a licensed institution based on its deposit and borrowing liabilities having exercised the powers conferred by Section 79 of the Nepal Rastra Bank Act, 2002.

(A) Provisions Relating to Compulsory Reserve:

1. For "A", "B" & "C" Class Banking Institutions Collecting

Deposits of General Public

1. It shall be mandatory for class "A" institutions licensed by this bank and for the "B" and "C" classes institutions licensed by this bank and accepting the current/calls accounts to maintain a deposit of 5.5 percent of the total deposit liabilities at this bank. Provided that, "B" and "C" class licensed institutions accepting deposits other than the "Current Deposit and "D" class micro-banking institutions collecting deposits of general public shall have to maintain mandatory balance at 2 percent of their total deposit liabilities.
2. The "B" and "C" class licensed institution and class "D" micro-banking institutions accepting deposits from general public situated in the location where there is no office of this bank may maintain a separate current account for this purpose with the nearby "A" class institution. However, the amount deposited in a class "A" licensed institution with the condition of earning interest shall not be counted as compulsory reserve. The information of

such account shall be given to this bank's bank and Financial Institution's Regulation Department and Concerned Supervision Department.(Liquidity Management in Banking Crisis)

3. In case the balance to be maintained as above Sub-Clause (1) falls short, the following fine is imposed
 - (a) For the first time of shortfall in maintaining the compulsory reserve, at the rate of the percentage of the existing bank rate on such shortfall amount;
 - (b) For the second time of shortfall in maintaining the compulsory reserve, at the rate of double of the percentage of the existing bank rate on such shortfall amount;
 - (c) For the third time and successive times of shortfalls thereafter in maintaining the compulsory reserve, at the rate of triple of the percentage of the existing bank rate on such shortfall amount.
- 4 For the purpose of calculation of "times" under sub-clauses (a), (b), and (c) above, separate times is calculated on every fiscal year basis. Moreover, in case any licensed institution fails to maintain compulsory reserve for a consecutive period of three weeks, it is fined at the rate of first time for the first week, of the second time for the second week and of the third time for the third week.
- 5 The fine at the existing bank rate on shortfall amount is on weekly basis. Such shortfall amount shall be multiplied by the percentage of bank rate and be divided by 52.
- 6 For the purpose of calculation of compulsory reserve to be maintained, the following procedures is followed: -
 - a) The compulsory reserve shall be examined on weekly basis (from every Sunday to Saturday).
 - b) The compulsory reserve shall be examined against the average weekly Balance of deposit liabilities of immediately preceding two weeks. In the case of full holidays in any week, the average deposit of immediately preceding week is considered.
 - c) For the purpose of calculation compulsory reserve, the weekly average of total deposit liabilities and balance held with this bank is determined by aggregating the total amount of daily balances from Sunday to Saturday and dividing the same by the figure seven. In doing so, if any holiday falls in the week, the balance of the preceding day is considered as the balance for the day.

d) For this purpose, the particulars relating to each Sunday to Saturday (in the case of holiday, the previous day's balance has to be mentioned) is compulsorily submitted to the concerned Supervision Department of this bank in the prescribed format referred to in Directives Form No. 13.1 within seven days from the date of the end of the week.

7 For this purpose, all offices of a licensed institution is constituted as one unit.

8 Any amount of local currency lying in transit for fund transfer and meant to be credited in the account with this bank shall be included in the balance held with this bank. Explanation:

- a. For the purpose of this Section, "total deposit" means the amount of current, savings, and fixed deposit including the money collected by the licensed institutions through various financial instruments as prescribed by this Bank.
- b. Only the balance held in ordinary account of this Bank shall be considered for compulsory reserve. For the purpose, balances held in special accounts and foreign currency accounts shall not be included.
- c. For the purpose of calculating compulsory reserve, balance of foreign currency accounts and staff guarantee account and margin account shall not be included for this purpose.
- d. "Current Account" means the deposit accounts maintained with the bank and financial institutions having the facility for withdrawal on demand.
- e. "Savings Deposit" means the deposit accounts maintained with the bank and financial institutions with an objective of saving.
- f. "Fixed Deposit" means the deposit accounts maintained with the bank and financial institutions for a stipulated time period.
- g. For the purpose of calculating compulsory reserve, the cash in transit to be balanced at the note fund of RastriyaBanijya Bank and Nepal Bank Limited in the places where there is no office of this bank may also be included. If amount is balanced at or withdrawn from the note fund, the concerned bank has had to send details thereof to the Currency Management Department and the concerned supervision department.

(B) Provisions Relating to Statutory Liquidity Ratio:

The licensed banks and financial institution of classes 'A', 'B' and 'C' shall have to maintain the statutory liquidity ratio at the rate prescribed from time to time. While maintaining the statutory

liquidity ratio according to this provision, the government securities, the amount in the call deposit in the class "A" commercial bank for the same purpose and the remaining amount in excess of the amount required for the compulsory reserve ration may also be calculated as the eligible instruments. The following provisions have been made with regard to calculation of the statutory

Liquidity ratio:

- a. The domestic deposit liability maintained at the end of the just preceding month is taken as the basis for calculating the statutory liquidity ratio.
- b. Such ratio shall be calculated and the statement the statutory liquidity ratio amount of each whole month is submitted as stated in Directive Form No.
- c. In case the said deposit falls short, fine shall be imposed as follows subject to the provision made in sub-Section (1) of Section 99 of the Nepal Rastra Bank Act, 2002:
 - i. In cases where the statutory liquidity ratio falls short for the first time, at the percentage of prevailing bank rate for the amount fallen short;
 - ii. In cases where the statutory liquidity ratio falls short for the second time, at double of the percentage of prevailing bank rate for the amount fallen short;
 - iii. In cases where the statutory liquidity ratio falls short for the third time and whatsoever time thereafter, at triple of the percentage of prevailing bank rate for the amount fallen short.
- d. While determining the time for clauses (a), (b) and (c), separate time is determined for each of the fiscal year.
- e. In the amount falling short of the statutory liquidity ratio, fine is imposed fallen short is multiplied with the percentage of the bank rate and divided by twelve.
- f. For the purpose of fine in the event of falling short of the statutory liquidity ratio, the bank rate published as prescribed by this bank shall be taken as the base.

2.3 Review of Related Studies

Chalermdumrichai (2011). There is various aspects of liquidity, but to confine the definition in related context, longer term liquidity management will be in focus. As it became evident in the crisis, liquidity rather than insolvency caused banks' failure. In this regards, Liquidity has divided good banks from ailing ones. Sound but poor liquidity banks may not be able to

withstand bankruptcy risk. Thus, it is not exaggerate to say "Liquidity is real king", especially, when market is squeezed or under crisis.

From liquidity management's perspective, with notice, banks have been encouraged to extend or lengthen sources of funding. Non-technically speaking, primary purpose is to narrowing the gap between funding and lending. The greater the gap is, the more risky the bank is exposed to. As a result, term funding including interbank borrowing rather than overnight or call can be considered as a more secure funding source, in a sense that it creates certainty of due maturities in orderly manner. In retail market, banks started offering long-dated financial products i.e., B/E and ultra-long fixed deposits as they learn to be less reliable on short-term funding to mitigate the gapping.

Khadak (2010).Measuring and managing the liquidity needs are vital for effective operation of commercial banks. By assuring a bank's ability to meet its liabilities as they become due, liquidity management can reduce the probability of an adverse situation developing. The importance of liquidity transcends individual institutions, as liquidity shortfall in one institution can have repercussions on the entire system. Bank managements should measure, not only the liquidity positions of banks on an ongoing basis, but also examine how liquidity requirements are likely to evolve under different conditions.

Banks are in the business of maturity transformation. They lend for longer time periods, as borrowers normally prefer a longer time frame. But their liabilities are typically short term in nature, as lenders normally prefer a shorter time frame (liquidity preference). This results in long-term interest rates typically exceeding short-term rates. Hence, the incentive for banks for performing the function of financial intermediation is the difference between interest receipt and interest cost which is called the interest spread. It is implicit, therefore, that banks will have a mismatched balance sheet, with liabilities greater than assets in short term, and with assets greater than liabilities in the medium and long term. These mismatches, which represent liquidity risk, are with respect to various time horizons. Hence, the overwhelming concern of a bank is to maintain adequate liquidity.

Liquidity has been defined as the ability of an institution to replace liability run off and fund asset growth promptly and at a reasonable price. Maintenance of superfluous liquidity will, however, impact profitability adversely. It can also be defined as the comprehensive ability of a bank to meet liabilities exactly when they fall due or when depositors want their money back. This is a heart of the banking operations and distinguishes a bank from other entities.

Objectives and Methodology of the Study though Basel Capital Accord and subsequent NRB guidelines have given a structure for Liquidity Management and Asset Liability Management in banks, the Indian banking system has not enforced the guidelines in total. The banks have formed Asset-Liability Committee (ALCO) as per the guidelines; but these committees rarely meet to take decisions. Taking this as a base, this research article attempts to find out the status of Liquidity Management in State Bank of India with the help of "Cash Flow Approach" methodology for controlling liquidity risk. To achieve the main purpose, the following objectives are set forth:

- To identify the liquidity risks faced by the banks.
- Classification of assets and liabilities into different time buckets as per RBB guidelines issued for liquidity management in banks.
- Analysis of liquidity risk through Cash Flow Approach Method.

Walt (2008). In his article, “Sound practices for Managing Liquidity in Banking Organizations” attributed Liquidity, or the ability to fund increases in assets and meet obligations as they come due, is crucial to the ongoing viability of any banking organization. Sound liquidity management can reduce the probability of serious problems. Indeed, the importance of liquidity transcends the individual bank, since a liquidity shortfall at a single institution can have system – wide repercussions. For this reason, the analysis of liquidity requires bank management not only to measure the liquidity position of the bank on an ongoing basis but also to examine how funding requirements are likely to evolve under various scenarios, including adverse conditions.

Shrestha (2007) in his article “The Efficiency of Liquidity Monitoring and Forecasting Framework the Nepal Rastra Bank in the Context of Liquidity Management in the Nepalese

Banking and Financial System” has stated liquidity management as the part of risk management framework of financial services industry. He found taking high liquidity risk as well as high credit risk are two main factors that cause banks to fail. Although high liquidity risk alone is not likely to cause banks failures, a liquidity crisis usually signals a need for change. He concluded proper liquidity management ensures that banks and financial institutions' financial commitments and obligations are met. Maintaining adequate liquidity also helps in avoiding forced sale of assets. The need for bank liquidity stems from seasonal, cyclical trend and short-term irregular movements in deposits and loans. The different sources available to meet these liquidity needs were identified and grouped into asset and liability liquidity sources. The treasury manager must consider the purpose of the liquidity need, the length of time for which funds are needed, the access to liability markets, the cost and the characteristics of various liquidity sources and interest rate forecasts.

Limbu(2010) in his dissertation, “Credit Management of NABIL Bank Limited” highlighted that aggregate performance and condition of Nabil bank. 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.

- The main objectives of the research study are as follow.
- To evaluate various financial ration of the Nabil Bank.
- To analyze the portfolio of lending of selected sector of banks
- To determine the impact of deposit in liquidity and its effect on lending practices.
- To offer suitable suggestions based on findings of this study.

Poudel(2011)made a thesis report entitled "A Study on Liquidity and Investment Position of Joint Venture Commercial Banks in Nepal", the study had based on the special reference to the Everest Bank Ltd and NABIL Bank ltd.

His major objectives were as under:

- To analyze the functions, objectives procedure and activities of the Everest Bank and
- Standard Chartered Bank Ltd

- To analyze the lending practices and resources utilizations of sample banks.
- To determine the impact of growth in deposit on liquidity and lending practices.
- To examine the lending efficiency and its contribution to profit.
- To make suitable suggestions based on the findings of this study. The financial and statistical tools are used.

The major findings from the study were:

There is no standard and uniform rate or ratio for maintaining liquid assets by the commercial banks. The manager may decide to maintain an appropriate level of liquid assets based on his own judgment. Liquidity management decision should be made based on the relation to the source of funds and statutory obligation. Nature of a source of fund may vary with the other. Like there are demand deposit and time deposit bearing different natures. Demand deposit has nature of high turnover. Therefore it requires high level of liquid assets to support withdrawals. Since the 80-90 Percent of funds of commercial banks is deposit, the proportion of demand deposit to total deposit liability largely determined the level of liquid fund. The banks do not have constant and consistent liquidity and investment policy. Both the banks are adopting discretionary fund management approach. The banks are adhering to theory of shift ability while investing on marketable securities, especially on government securities. Anticipated income approach is also adopted in case of long-term loans. There are various active external factors affecting liquidity position of the banks, the deposit liability in the latest two year has increased substantially. Therefore, it is suggested to conduct a study to find the reason behind over increasing trend of deposit of the banks.

2.4 Concluding Remarks

There are various researchers conduct on lending practice, credit policy, financial performance, credit management and liquidity mobilization of various commercial banks. In order to perform those analysis researchers have used various ratio analysis. In the past research topic on liquidity mobilization the researcher has focused on the limit ratios which are incapable of solving the

problems. Actually liquidity mobilization is determined by various factors. In this research various ratio are systematically analyzed and generalized. Past researchers are not properly analyzed about investment aspect' mobilization of fund and its impact on the profitability. The ratios are not categorized according to nature. Here in this research all ratios are categorized according to their area and nature.

CHAPTER-III

RESEARCH METHODOLOGY

3.1 Introduction

Research methodology is a collective term for the structured process of conducting research. There are many different methodologies used in various types of research and the term is usually

considered to include research design, data gathering and data analysis. Research methodologies can be quantitative (for example, measuring the number of times someone does something under certain conditions) or qualitative (for example, asking people how they feel about a certain situation). Ideally, comprehensive research should try to incorporate both qualitative and quantitative methodologies but this is not always possible, usually due to time and financial constraints. Research methodologies are generally used in academic research to test hypotheses or theories. A good design should ensure the research is valid, i.e. It clearly tests the hypothesis and not extraneous variables, and that the research is reliable, i.e. It yields consistent results every time.

Part of the research methodology is concerned with the how the research is conducted. This is called the study design and typically involves research conducted using questionnaires, interviews, observation and/or experiments. The term research methodology, also referred to as research methods, usually encompasses the procedures followed to analyze and interpret the data gathered. These often use a range of sophisticated statistical analyses of the data to identify correlations or statistical significance in the results. Objective, representative research can be difficult to conduct because tests can normally only be conducted on a small sample (e.g. you cannot test a drug on every person in the world so a sample needs to be used in research). This means that researchers need to have a very detailed understanding of the types and limitations of research methodologies which they are using.

The study has used a descriptive and analytical research design. It is based on secondary data taken from financial statements, annual reports, unpublished official records of concerned banks and web-sites of Nepal Rastra Bank as well as Nepal Stock Exchange.

3.2 Research Design

Research designs are concerned with turning the research question into a testing project. The best design depends on research questions. Every design has its positive and negative sides. The research design has been considered as a "blueprint" for research, dealing with problems: what questions to study, what data are relevant, what data to collect, and how to analyze the results. To achieve the objective of this study, analytical and descriptive research designs have been used.

3.3 Population and Sample

In the present context, there are 28 commercial banks operating in Nepal. The study of all these banks within this research was almost impossible. Hence, considering this number of banks as total population. Due to limited time and resource information among 30 commercial banks the study has been confined to only two commercial banks, namely Standard Chartered Bank Nepal Limited (SCBNL) and Everest Bank Limited via simple random sampling method which tried to achieve the objectives set out by analyzing the data.

3.4 Nature and Sources of Data

The data used in this study are secondary in nature. Published annual reports of the concerned banks are taken as basic source of data. The data relating to financial performance are directly obtained from the concerned banks. Similarly, related books, magazine, journals, articles, reports, bulletins, data from Nepal Stock Exchange and Nepal Rastra Bank, Central Bureau of statistics, related website from internal sources etc. as well as other supplementary data and various economic surveys are also used. Previous related studies to the subject are also counted as source of information. Since the data have been obtained from secondary sources, after collection of financial statement, master sheet of financial data have been extracted and tabulated as per the need of this study. In order to process the data, financial statement and other available information were reviewed. These data were grouped in different tables and charts according to their nature. Most of the data have been compiled in one form and processed and interpreted as required.

3.5 Method of Data Analysis

Financial as well as the statistical tools are used to make the analysis more convenient, reliable and authentic. For data analysis, different items from the balance sheet and other statements are tabulated. Their ratios, percentages, mean, standard deviations, and coefficients of variations are then calculated and presented in the tables. Likewise, trend analysis is also used to know the trend of various ratios. Following are the brief introductions of the financial and statistical tools used in this study.

3.5.1 Financial Tools.

i.) Profitability Ratios

Profitability ratios are used to indicate and measure the overall efficiency of a firm in terms of profit and financial performance. For better performance, profitability ratios of firm should be higher. Under this, the following profitability ratio will be computed.

a.) Return on Equity (ROE)

Net worth refers to the owner's claim of a bank. The excess amount of total assets over total liabilities is known as net worth. This ratio measures how efficiently the bank has used funds of the shareholders. This ratio can be computed by dividing net profit by total equity capital (net worth). This can be calculated as;

$$\text{Return on Equity} = \frac{\text{Net Profit}}{\text{Total Equity Capital}}$$

b.) Earnings per Share (EPS)

Earnings per share are the portion of company's profit that is allocated to each outstanding share of common stock. EPS is calculated by dividing the common's net income with the total number of shares. The higher the earning per share of a company, the better is its profitability. While calculating EPS, it's advisable to use the weighted ratio as number of share outstanding can change overtime. EPS is computed following formula

$$\frac{\text{Total Assets}}{\text{Total Share Outstanding}}$$

ii.) Liquidity Ratios

The ratio measures the liquidity position of a firm. It measures the firm ability to meet its short-term obligations. As Financial Analytical tools, following liquidity ratio will be used.

a.) Quick Ratio

Quick ratio establishes a relationship between quick assets and current liabilities. An asset is liquid if it can be converted into cash immediately or reasonably soon without a loss of original value. Cash is a most quick asset. Other assets which are considered to be relatively liquid and included in quick assets are book debts and marketable securities. For Quick Ratio, Cash and bank balance and government securities are included in quick assets. This ratio can be found out by dividing the total of quick assets by total liquid liabilities.

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

3.5.2 Descriptive Statistics

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

i) Mean:

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

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

Where

\bar{X} = Mean of the values

ΣX = Summation of the values

N = No. of Observations

ii) Coefficient of variation:

The calculated standard deviation gives an absolute measure of dispersion. Hence where the mean value of the variables is not equal, it is not appropriate to compare two pairs of variables based on standard deviation only. The coefficient of variation (C.V.) is given by the following formula in the percentage basis:

$$\text{Coefficient of variation (C.V.)} = \frac{\sigma}{\bar{X}} * 100$$

3.5.3 Correlation Analysis

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

$$\text{Coefficient of Correlation (r)} = \frac{\sum xy}{N\sigma_1\sigma_2}$$

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

$y = Y - \bar{Y}$

σ_1 = Standard series of X

σ_2 = Standard series of Y

N = Number of pairs of Observations

The Karl Pearson coefficient of correlation always falls between -1 to +1. The value of correlation in minus signifies the negative correlation and in plus signifies the positive

correlation. As the value of correlation reaches to the value of zero, it is said that there is no significant relationship between the variables.

3.5.4 The Model

Regression analysis is the quantitative research method which is used when the study involves modelling and analyzing several variable where the relationship includes a dependent variable and one or more independent variables. The regression modals used in the study have been outline as follows,

$$ROE_{it} = \beta_0 + \beta_1 QR_{it} + \varepsilon_{it} \quad (1)$$

$$EPS_{it} = \beta_0 + \beta_1 QR_{it} + \varepsilon_{it} \quad (2)$$

Where:

ROE = Return on Earning

EPS = Earning per Ratio

β_0 = Intercept of regression

β_1 = Slop of the regression

QR_{it} = Quick Ratio

ε_{it} = Error term

CHAPTER- IV PRESENTATION AND ANALYSIS OF DATA

In the process of fulfilling objectives of this research, data revealed are tabulated and presented followed by analysis and interpretation in this chapter. Furthermore, the findings of this research are also presented at this chapter.

4.1 Profitability Position of Selection Commercial Banks

Profitability ratios are used to indicate and measure the overall efficiency of the firms in the term profit and financial performance. For better performance Profitability ratio of firm should be higher. Under this following profitability ratio will be computed.

4.1.1 Return on Equity (ROE)

Net worth refers to the owner's claim of a bank. The excess amount of total assets over total liabilities is known as net worth. The ratio measures how efficiently the bank has used fund of total shareholder. The ratio can be computed by dividing net profit by total equity capital (net worth).

Table 4.1

Return on Equity (ROE) in %

Fiscal Year	SCBL	EBL
2007/08	32.85	28.54
2008/09	33.58	28.96
2009/10	32.22	30.17
2010/11	30.43	25.57
2011/12	28.36	27.15
2012/13	26.38	31.52
2013/14	26.27	29.04
2014/15	21.69	23.25
2015/16	17.18	20.61
2016/17	11.98	17.5
Mean	26.09	26.23
SD	7.16	4.5

Kurtosis	0.1	-0.05
Skewness	-0.97	0.92
Range	21.6	14.02
Maximum	11.98	17.5
Minimum	33.58	31.52

(Source:- Annex – 2 & calculate using Microsoft Excel 2007)

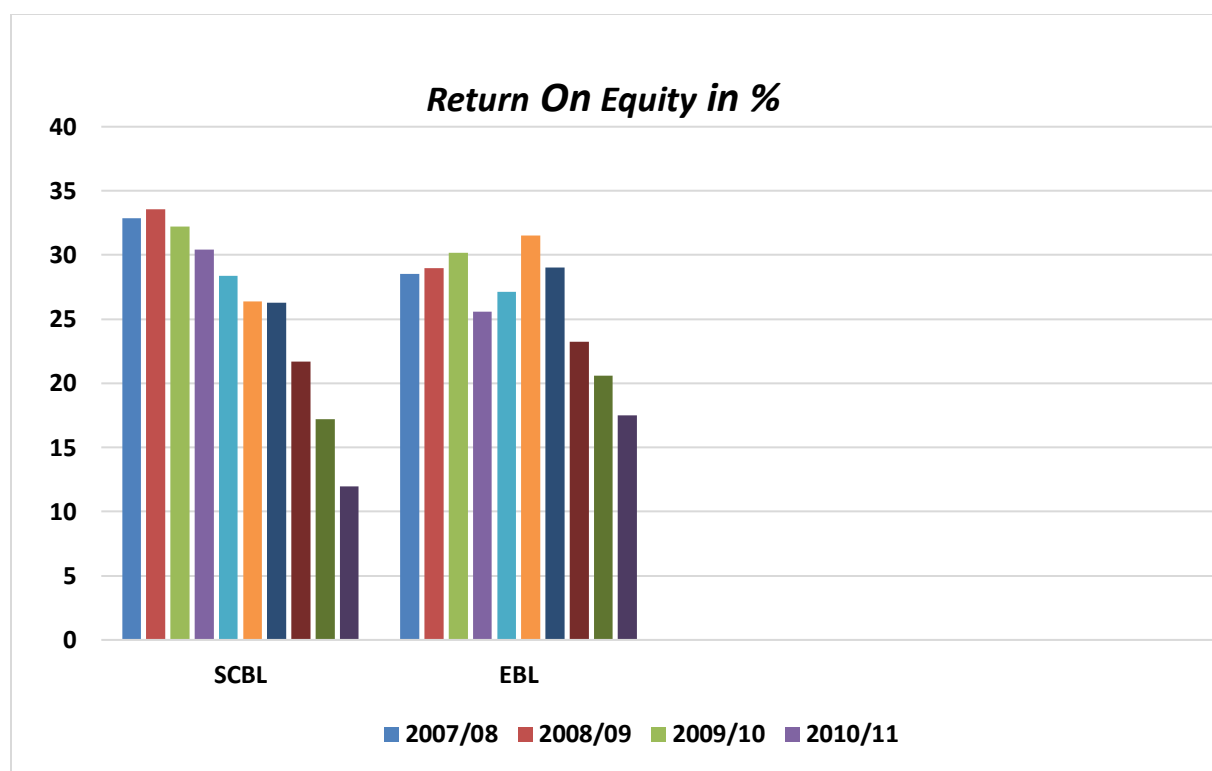


Figure 4.1

The table 4.1 shows that the Return onEquity of Standard Charted Bank (SCBL) and Everest Bank Limited (EBL) are fluctuating. The table indicated the efficiency of bank in generating profit through mobilizing the shareholders property. The table shows that the return equity of SCBL was highest 32.85%, 33.58%, 32.22%, 30.43%, & 28.36% till than EBL on fiscal years 2007/08, 2008/9, 2009/10, 2010/11 & 2011/12. And SCBL was lowest return on shareholder

equity 31.52%, 29.04%, 23.25%, 20.61% & 17.5% than EBL on fiscal years 2012/13, 2013/14, 2014/15, 2015/16 & 2016/17. The average of the ROE in SCBL was 26.09% in EBL was 26.23. Comparing the banks, it can be concluded that EBL was effective in optimally mobilizing the shareholder equity, since ROE of EBL (26.26%) was highest in comparison with that of SCBL (26.09%).

4.1.2 Earning per Share (EPS)

Earnings per share are the portion of company's profit that is allocated to each outstanding share of common stock. EPS is calculated by dividing the common's net income with the total number of shares. The higher the earning per share of a company, the better is its profitability. While calculating EPS, it's advisable to use the weighted ratio as number of share outstanding can change overtime. EPS is computed following formula.

Table 4.2

Earnings per Share (EPS in Rs.)

Fiscal Year	SCBL	EBL
2007/08	131.92	91.82
2008/09	109.99	99.99
2009/10	77.65	100.16
2010/11	69.51	83.16
2011/12	72.6	88.55
2012/13	65.7	91.88
2013/14	65.46	86.04
2014/15	57.38	78.04
2015/16	45.96	65.97
2016/17	35.49	44.32
Mean	73.17	82.99
Standard Deviation	28.61	16.97
Kurtosis	1	2.26

Skewness	1.03	-1.46
Range	96.43	55.84
Minimum	35.49	44.32
Maximum	131.92	100.16

(Source:- Annex – 2 & calculate using Microsoft Excel 2007)

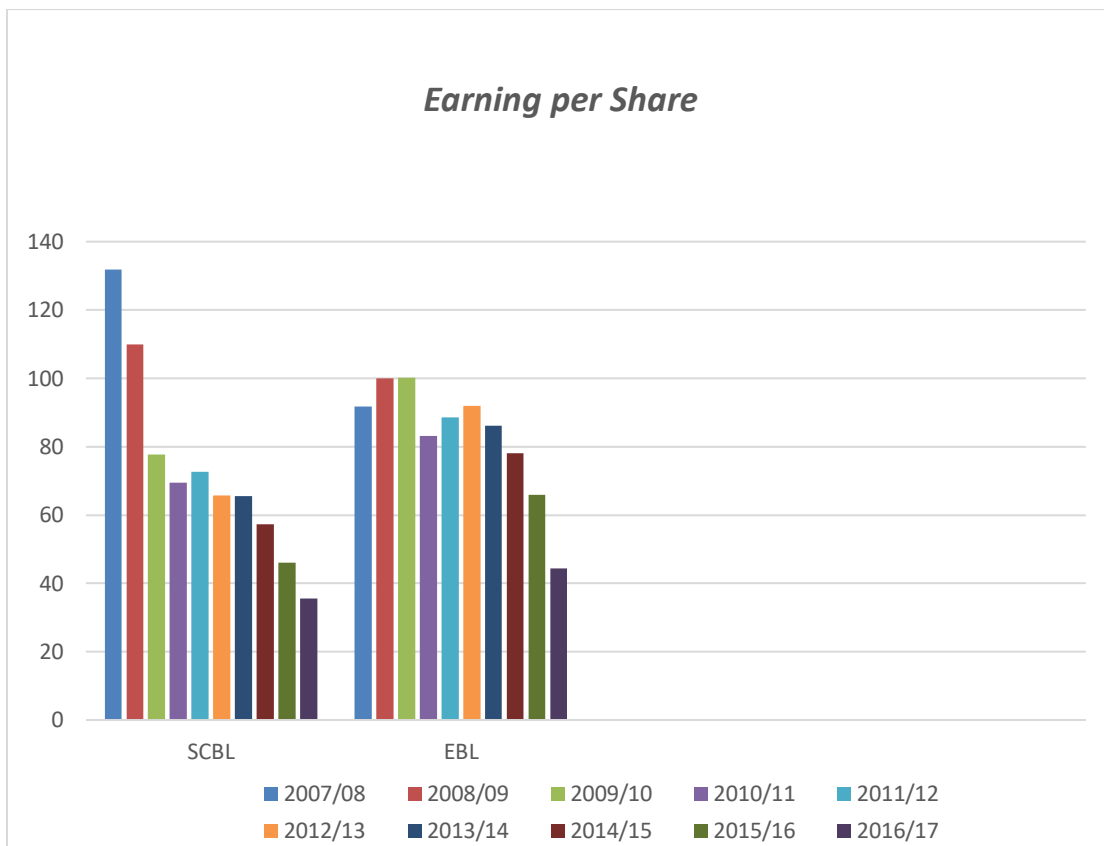


Figure 4.2

The table 4.2 shows that the earning per share (EPS) of SCBL and EBL. The EPS SCBL first two year 2007/08 and 2008/09 is higher than EBL Rs.131.92 and Rs.109.99. The EPS of SCBL is lowest than EBL on the fiscal year 2009/10, 2010/11, 2011/12, 2012/13, 2013/14, 2014/15, 2015/16, 2016/17 of Rs.100.16, Rs83.16, Rs88.55, Rs98.88, Rs86.04, Rs78.04, Rs65.97, Rs44.32. The average the EPS in SCBL was Rs73.17 and in EBL was Rs.82.99. Comparing the

banks, it can be concluded that EBL was effective in optimally mobilizing the shares, since EPS of SCBL (Rs.73.17) lowest comparison with that EBL (Rs.82.99).

4.2 Liquidity Position of Selected Commercial Banks

Quick ratio establishes a relation between quick assets and current liabilities. An assets is liquid if it can be convert in to cash immediately or reasonably soon without a loss of original value. Cash is most quick assets. Other assets which are considered to be relatively liquid and include in quick assets and book debt and marketable securities. For quick ratio cash and bank balance and government securities are included in quick assets. The ratio can be found by dividing the total of quick assets by total liquid liabilities.

Table 4.3

Quick Ratio of commercial Bank

Year	SCBL	EBL
2007/08	0.142393	0.125448
2008/09	0.144464	0.184167
2009/10	0.102029	0.210876
2010/11	0.190638	0.148694
2011/12	0.235556	0.020698
2012/13	0.238234	0.192998
2013/14	0.369853	0.210836
2014/15	0.409755	0.301001
2015/16	0.179202	0.243083
2016/17	0.337014	0.223756
Mean	0.234914	0.186156
Standard Deviation	0.10471	0.00471
Kurtosis	-0.998278	-0.000278
Skewness	0.57198	0.57198
Range	0.307726	0.307726
Minimum	0.102029	0.102029

Maximum	0.409755	0.409755
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(Source:- Annex – 3 & calculate using Microsoft Excel 2007)

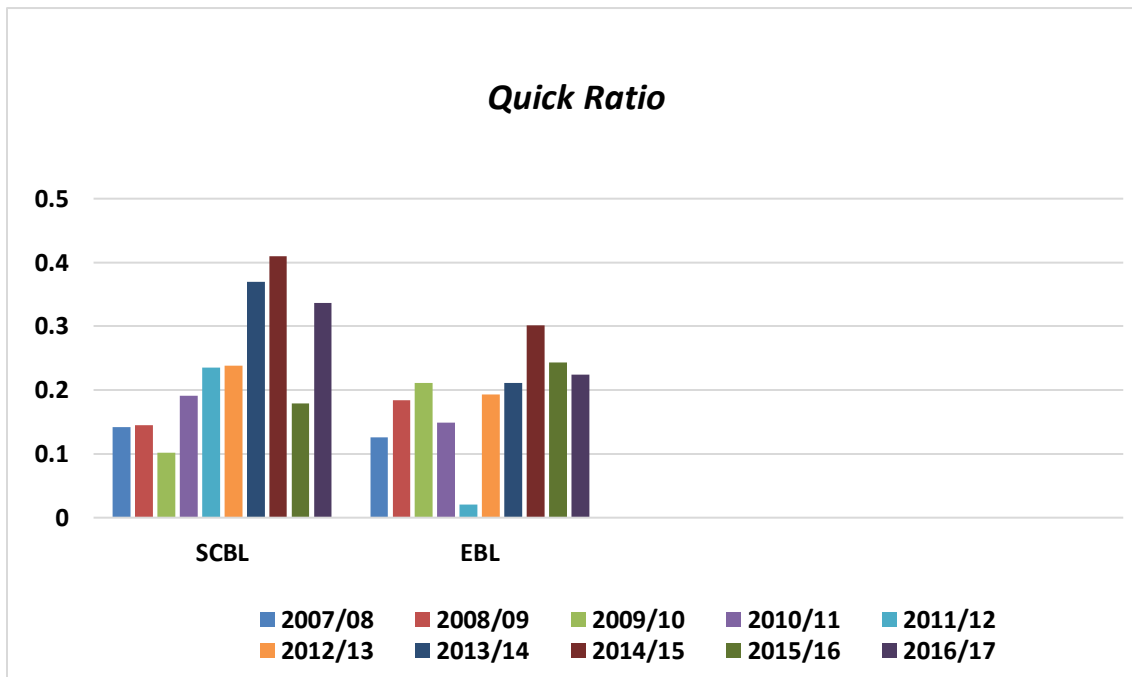


Figure 4.3

The table 4.3 shows that quick ratio of Standard Bank Limited (SCBL) and Everest Bank Limited (EBL). The ratio of SCBL is highest (0.369853) in the year 2010/11 and lowest (0.102029) in 2009/10. And the quick ratio of EBL is highest (0.301001) in the 2014/15 and lowest (0.020698) in the year 2011/12. The average quick ratio of SCBL is (0.234914) and EBL is (0.186156). The average ratio of SCBL is higher than EBL. Above analysis help to conclude that the quick ratio of SCBL is better than EBL. It shoes better liquidity position of SCBL in comparison to EBL.

4.3 Description Statistics

Description statistics aim to summarize sample rather than use of data from sample using index such as the mean or standard deviation and inferential statistics which draw conclusion data that are subject to random variation.

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

Table 4.4

Pearson Description Statistics Study

Variable	Mean	Standard Deviation	Minimum	Maximum	Percentile		
					25	50	75
ROE	26.162	5.820	11.980	33.580	22.081	27.574	30.365
EPS	78.080	23.440	35.490	131.920	65.520	77.845	91.865
QR	0.211	0.092	0.021	0.410	0.146	0.202	0.242

(Source:- Annex – 4 & calculate using Microsoft Excel 2007)

Above table mean of ROE is 26.162 and standard deviation is 5.820. And mean of EPS is 78.080 and standard deviation is 23.440. then mean osQR is 0.211 and standard deviation is 0.092.

4.4 Correlation Analysis

Correlation analysis is a method of statistical evaluation use to study the strength of a relationship between two numerically measured continuous variables. The particular type of analysis is useful when a researcher wants to established if there connection between variables.

Table 4.5

Pearson Correlation Coefficient of Study Variables (n=20)

	ROE	EPS	QR
ROE	1	.838**	-.498*
EPS	.838**	1	-.527*
QR	-.498*	-.527*	1

(Source:- Annex – 5 & calculate using Microsoft Excel 2007)

** . Correlation is significant at the 0.01 level (2-Tailed).

*.Correlation is significant at the 0.05 level (2-Tailed).

4.5 Regression Analysis

Regression analysis is the quantitative research method which is used when the study involves modelling and analyzing several variable where the relationship includes a dependent variable and one or more independent variables.

Table 4.6
Regression Result

	Dependent Variable: ROE			Dependent Variable: EPS		
	Coefficient	t-statistics	Sig	Coefficient	t-statistics	Sig
Constant	32.770	11.117	.000	106.223	9.127	.000
QR	-31.385	-2.438	.025	-133.673	-2.630	.017
	R Square =0.248, Adj. R Square =0.206, F-Stat. =5.944, F-sig. =0.025,			R square = 0.278 Adj. R Square =0.237 F-stat.= 6.917 F-sig. =0.017		

(Source:- Annex – 6 & calculate using Microsoft Excel 2007)

The table 4.6 shows that R^2 for model first is 0.248 meaning that about 25% variation in return equity is explained by quick ratio. Likely R^2 for model second is 0.278, which indicated that about 28% variations. In EPS is explained by quick ratio. The P-value of F- statistics in both models are less than 0.05, meaning that both regressions are valued statistically. Moreover that model first wherever dependent variable is ROE, the P-value of quick ratio is less than 0.05, which indicated that liquidity significantly affect profitability. However the coefficient is negative meaning that increase in liquidity reduces profitability of commercial bank. Likely EPS which is measure of profitability is also significantly negatively affected by liquidity.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

Establishment of commercial banks, especially joint venture banks, has continued in response to the economic liberalization policies of the Government. As a result, in Nepal there are 28 commercial banks at present competing with each other in their business. These joint venture banks have concentrated themselves on financing foreign trade, commerce and industry. As mentioned earlier, this study concentrates on the comparative analysis of working capital position of aforementioned banks Standard Charter Bank Nepal Limited (SCBL) and Everest Bank Limited (EBL). From the perspective of the researcher, these two banks are chosen for study mainly because of accessibility and availability of financial data for latest ten year period. To fulfill the objective, an appropriate research methodology has been developed, which includes ratio analysis as financial tool and trend analysis, correlation coefficient. The major ratio analysis consists of the composition of working capital, liquidity position, turnover position, capital structure position and profitability position. Under these, main ratios and their trend position are studied in the chapter four. In order to test the relationship between the various components of working capital, Karl Pearson's Correlation Coefficient r^2 is calculated and analyzed. Some null hypothesis formulated in chapter three is tested in appendices and results are analyzed in chapter four.

5.2 Conclusion

Profitability analysis shows that the overall profitability (i.e. ROE) of the sample banks has normally an increasing trend. The overall trend of liquidity ratios is not largely smooth. Fluctuating trend of the liquidity ratios does not make easy in increase trend of profitability of commercial banks in Nepal. There is a significant impact of SCBL and EBL on profitability of commercial banks in Nepal. This indicates that increase in these liquidity ratios boosts the bank profitability and vice-versa. This reveals that profitability has no relationship with those liquidity ratios.

The present study has covered only two commercial banks in Nepal established and excluded those set up in subsequent years. It has also studied data of only 10 fiscal years. Therefore, further studies should also cover as many more banks and years as possible to make their findings more valid and should use more scientific tools and analysis.

In conclusion, it can be said that working capital management is one of the most important parts of every financial institutions. Working capital is a crucial capital, which is often compared to lifeblood of the human being. After analyzing the two samples banks SCBL and EBL comparatively using various financial and statistical tools, various important conclusions have been derived from the study. The average return on equity and earning per share is higher in EBL than in SCBL. The networking capitals of only SCBL are positive in the first year of the study period. Comparatively, SCBL has higher net working capital than EBL. Both the banks are able to maintain adequate liquidity position to meet the short term or even instant obligations in that period. The liquid ratio of both SCBL and EBL are below the normal standard ratio of 2:1. However, the liquidity position of SCBL is slightly better than that of EBL. Although higher liquidity means lower risk as well as lower profit, but in commercial bank, higher liquidity is not always the cause of lower profitability. In case of profitability position, profitability in terms of interest earned to total assets ratio of EBL is slightly higher than that of SCBL. Therefore, EBL is more efficiently using its total assets (funds) to earn interest income. The net profit to total assets and the net profit to deposit ratios are also higher in SCBL than in EBL. Thus, it is

concluded that the average profitability ratio of SCBL is higher than that of EBL. Both the banks have constant level of growth in profitability during the study period. To acquire higher profits they should take strong steps for the better management, strong marketing and strategic development etc. The correlation coefficient of the variables selected for the statistical analysis shows that SCBL has significant relationship with quick assets and liquid liabilities. Similarly, EBL has significantly relationship with quick assets and liquid liabilities. Therefore, from above all, it can be concluded that both the banks are not of much difference. Comparatively, SCBL is financially steady and better than EBL. But it does not mean that EBL is not performing well. Both banks are striving for better performance by adopting various new strategic and providing additional services.

5.3 Recommendations

On the basis of the major findings drawn on the previous chapter and the conclusion made in this chapter, the following recommendations have been given for the enhancement of the liquidity and profitability position of the sampled banks;

- There is significant relationship between total return on equity and earning per share of SCBL and EBL.
- It can be concluded that the degree of relationship on return on equity of EBL is little high than the SCBL. This little correlation coefficient indicates that the bank has poor performed in order to generate shareholder equity.
- Thus, EBL should seek the high earning grant. For the purpose, the bank should develop an innovative approach to bank marketing and formulate new strategies of serving customers in a more convenient and satisfactory way by optimally utilizing the modern technology and offering new facilities to the customers at competitive prices.
- The bank is also required to explore new market areas. For this purpose, it is recommended to form a strong market department in its central level, which deals with the banking products, places, price and promotion.
- Return on Equity ratio and Earning per Share ratio of EBL is better than SCBL. It is the indication of better performance of EBL. And quick ratio SCBL is better than EBL. Thus EBL is utilizing the funds more efficiently for the profit generating purpose than SCBL.

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