

**COMPARATIVE STUDY ON PORTFOLIO MANAGEMENT OF
KUMARI BANK LTD. AND EVEREST BANK LTD.**

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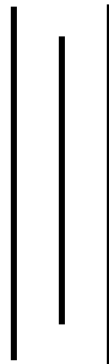
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RECOMMENDATION

This is to certify that the Thesis

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**COMPARATIVE STUDY ON PORTFOLIO MANAGEMENT OF
KUMARI BANK LTD. AND EVEREST BANK LTD.**

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DECLARATION

I hereby declare that the work reported in this thesis entitled “**Comparative Study on Portfolio Management of Kumari Bank Ltd. and Everest Bank Ltd.**” 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 Degree in Business Studies (MBS) under the supervision of **Asso. Professor Kishor Maharjan** of Shanker Dev Campus.

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ABBREVIATIONS

a	=	Constant of Regression
b	=	Coefficient of Regression
CD	=	Cash Deposit Ratio
CML	=	Capital Market Line
CRR	=	Cash Reserve Ratio
CV	=	Coefficient of Variation
EBL	=	Everest Bank Limited
EPS	=	Earning Per Share
KBL	=	Kumari Bank Limited
LC	=	Letter of Credit
LRR	=	Liquidity Reserve Ratio
NRB	=	Nepal Rastriya Bank
P/E Ratio	=	Price Earnings Ratio
PE	=	Probability of Error
r	=	Coefficient of Correlation
R ²	=	Coefficient of Determination
ROA	=	Return on Assets
ROE	=	Return on Equity
SD	=	Standard Deviation
SDC	=	Shankar Dev Campus
SML	=	Security Market Line
T.U.	=	Tribhuvan University

CHAPTER - I

INTRODUCTION

1.1 Background of the Study

Nepal is one of the least developed countries characterized by high population growth rate, low per capita income, and low rate of capital formation having unlimited resources. Therefore, Nepal like other developing countries has been facing the problem of accelerating the pace of economic development and Nepal is not exception.

A sound banking system is precondition for healthy economy and economic policy formation. An efficient banking system becomes a top priority as country moves toward free market economy which allows private sectors saving to be retained in the country for the promotion of investment needed for the growth.

Capital formation and its proper utilization are two important aspect of economic development of a country. Private investment can be the significant contributor to economic growth and employment generation in the developing country. “Economic development demands the transformation of saving into actual investment and it is the financial institutions that transfer funds from surplus spending units to deficit units” (NRB, 1996:4). Economic development is supported by financial infrastructure of the country.

Banks are the principal source of credit for millions of individuals and families and for unit of government. Moreover, for small local businesses ranging from grocery stores to automobile dealers, banks are often a major source of credit to stock the shelves with merchandise. Banks grant more installment loans to consumer than any other financial institutions.

In most years, banks are the leading buyers of bonds and notes issued by government to finance public facilities ranging from hospital and football stadium to airports and highways. Moreover, banks reserve the principal channel for the government economic policy to stabilize the economy. And banks are also the most important sources of short-term working capital needed for the businesses. They have become increasingly active in recent years in making long-term business loans for new plant and equipment. When businesses and consumers must make payments for the purchase of goods and services, more often they use bank provided cheques, credit or debit cards or electronic accounts connected to the computer network. It is the banker to whom they turn most frequently for advice and counsel when they need financial information and financial planning. An investment in any funds is made to have some positive rate of return. Nobody is ready to bear risk without any return but to have returned one must be ready to face some risk. To minimize the risk at the given rate of return the concept of portfolio diversification is necessary. Portfolio is simply a collection of securities gathered to achieve certain investment goals. "Investment positions are taken with the goal of earning some expected rate of return. Diversification is essential to the creation of an efficient investment because it can reduce the variability of returns around the expected return" (Francis, 2003: 228).

The growth of any commercial bank depends upon its financing and investment policy. A sound financing and investment policy attracts both borrowers and lenders, which helps to increase the volume and quality deposits and investment. Both the depositors and creditors are customers of the banks. Banks offer various products for deposit mobilization and disburse the credit products as per the portfolio management. Customers as per their need purchase different types of products offered in the market. Deposit products offered to the customers are categorized into general products and special products. Mobilization of the deposit simply by increasing the rate of interest is termed as general products and special

products are developed in terms of schemes generally refundable at longer period of time. Customers choose the respective better general products and special products from among the products available in the market. Special products focus on some specific value and needs of the customers. Under this comes the education scheme for the children, daughter's marriage scheme and retirement pension scheme and others.

A systematic investment process should be followed to win the stock market. Investment process describes how an investor should go about making decisions with regard to what marketable to invest in, how extensive the investment should be and when the investment should be made. A five step procedure for making these decisions from the basis of investment process (Baily, 1995:9).

-) Set investment Policy
-) Perform Security Analysis
-) Construct a Portfolio
-) Revise the portfolio
-) Evaluate the Portfolio

Loans are essential aspect of the commercial banking function. “First income from loan contributes substantially to the revenues and profit of the bank. Second, lending money to people in the community strengthens the community-bank relationship. Third, lending money spurs business development and supports a growing economy” (Edmister, 1980:82). Credit being the most important functions of the commercial banks, affects overall development of the country. So far as pace if the economic development is considered, it is directly related to the quantity of the credit, which is derived from various financial institutions especially commercial banks of Nepal.

Investment operation of commercial banks is very risky one. For this, commercial banks have to pay due consideration while formulating investment policy. A rapid development of any commercial bank depends upon its investment policy. A sound investment policy attracts both borrowers and lenders, which helps to increase the volume and quality deposits and investment.

1.2 Focus of the Study

In any firm, portfolio management is taken as major financial decision, which affects the value of firm. The performance of any business organization largely depends upon its investment policy. Furthermore, investors invest their money analyzing the investment policy of business organization. Therefore, investment policy is regarded as an important decision with respect to management and investors.

A bank always puts its effort to maximize its profitability. The profit is excess of the income over expenses. To maximize profit income should reasonably be excess over expenses. The major source of income of bank is interest income from loans, investment and fee based income. As loan and advances dominate the asset side of the balance sheet of any bank, earnings from such loan and advances occupy a major space in income statement of the bank. However, it is very important to be reminded that the most of the bank failures in the world are due to shrinkage in the value of loan and advances. Hence, loan is known as risky asset and investment operation of commercial banks is very risky one. Risk of non-performing loans erodes even existing capital. Considering the importance of lending to the individual banks and also to the society it serves, it is imperative that the bank meticulously plans its credit operations; sound credit policy has following objectives:

-) To have Performing Assets
-) To give guidance to lending officials

-) To establish a standard for control
-) To contribute to economic development.

Considering these facts, this study mainly focuses on the portfolio Management practices of Kumari Bank Ltd. and Everest Bank Ltd.

1.3 Statement of the Problem

Portfolio Management is a relatively new concept in Nepalese Context. Many companies still have no awareness towards it. The study proposes to the investor's awareness about the portfolio management of the financial institutions while investing.

Investors can be classified into three categories on the basis of risk and return. First type of investors is risk seeker who becomes ready to face high risk in the hope of high return. The second type of investors is risk averters who try to avoid risk and ready to be satisfied on the low return. The third type of investors comes along in between these two investors called risk neutral. These investors are ready to bear medium risk and have medium return.

The major problem in almost all underdeveloped countries and Nepal is no exception, is that of capital formation and proper utilization. In such countries, the commercial banks have to shoulder more responsibilities and acts as development banks, due to lack of other specialized institutions.

Thus, in the scenario of Nepalese commercial banking sector, this study mainly seeks the answers the following specific problems related to portfolio management practices of Kumari Bank Ltd. and Everest Bank Ltd.

-) What is the proportion of non-performing asset o total loans and advances of the bank?

-) What is the portfolio behavior of the bank?
-) Are the banks' funds mobilization and portfolio management effective and efficient?
-) Is there any stability in fund mobilization policy or not?
-) What is the relationship of investment and loans and advances with total deposit and net profit?

1.4 Objective of the Study

The main objective of the study is to compare the Portfolio Management practices of Kumari Bank Ltd. And Everest bank Ltd. However the specific objectives are:

-) To compare the liquidity management, asset management efficiency, profitability position, risk position, investment practices of aforesaid banks.
-) To find out the relationship between deposit and total investment, deposit and loans and advances and net profit.
-) To find out the non-performing asset position of the banks.
-) To analyze the risk return ratios of investment of the banks.
-) To evaluate the portfolio management of the banks.

1.5 Significance of the Study

Commercial banks in the developing countries like Nepal have the greatest responsibilities towards the economic development of the country. In modern times, since credit or bank money constitutes bulk of the economy's aggregate money supply, it mostly changes the volume of bank money or credit rather than changes in the total supply of the high powered money issued by the reserves held by the bank against their deposit liabilities that account for changes in the aggregated money supply. The main goal of the bank as a commercial organization is to maximize the surplus by the efficient use of its finds and resources. In spite of being commercial institution, it too have a responsibility

(Obligation) to provide social service oriented contribution for the social economic development of the country by providing specially considered loans and advances towards less privileged sectors.

Hence the study is needed to examine the overall performance of KBL and EBL especially in collection of deposits and utilization. The main study will have to know the overall performance of KBL and EBL. So, it will be useful for different stakeholders.

1.6 Limitations of the Study

This study has the following limitations:

-) This is a comparative study of KBL and EBL. So the findings of the study can't be generalized.
-) The study is based on the secondary data published on annual reports of the respective banks.
-) Among many factors affecting the investment decision, only certain factors i.e. Liquidity, profitability, diversification, growth etc. have been considered.

1.7 Organization of the Study

The whole study has been divided into five chapters as:

Chapter I: Introduction: This chapter deals with the background of the study, focus of the study, introduction of banks under study, statement of problem, objectives of the study, significance of the study, limitations of the study and organization of the study.

Chapter II: Review of Literature: This chapter includes the conceptual review and review of related studies.

Chapter III: Research Methodology: This Chapter Includes the research design, sources of data and data analysis tools.

Chapter IV: Presentation and Analysis of Data: This chapter includes the liquidity ratios, asset management ratios, activity ratios, profitability ratios, growth ratios, correlation coefficient analysis, trend analysis and major findings of the study.

Chapter V: Summary, Conclusions and Recommendations: This chapter includes summary, conclusions and recommendations of the study.

CHAPTER - II

REVIEW OF LITERATURE

This chapter mainly concerned with the competent exploration of the background to the work and comprehensive review of recent and relevant literature. In this regard, an effort has been made to grasp the knowledge and information that is available from libraries, document collection centers, other information managing bureaus and concerned commercial banks. This chapter helps to take adequate feedback to broaden the information base and inputs to the study. The conceptual framework given by the different researchers, authors, practitioners, scholars etc is reviewed from research papers, books, annual reports and articles.

2.1 Conceptual Review

A commercial bank is a business organization that receives and holds deposits of funds from others, provides loans or extends credits and transfers funds by written order of deposits. Commercial Bank Act of Nepal (1974) has defined that “ A commercial bank is such, which exchanges money, deposits money, accept deposits, grant loans and performs commercial banking functions and which is not a bank meant for co-operative, agriculture and industries or for such specific purpose”.

American Institute of Banking (1972) has defined commercial bank as a corporation, which accepts demand deposits subject to check and makes short-term loans to business enterprise, regardless of the scope of its other services.” This act has laid emphasis on the functions of commercial bank while defining it. Commercial banks provide short-term debts necessary for trade and commerce. They take deposits from the public, and grant loans in different forms. They

discharge various functions on behalf of their customers and are paid for their services.

Commercial banks, as financial institutions, perform a number of internal functions. Among them, providing credit is considered as most important one. According to H.D. Crosse (1963), “Commercial banks are very risky one. For this, commercial banks have to pay due consideration while formulating investment policy regarding loan investment. Investment policy is one facet of the overall spectrum of policies that guide banks investment operations”.

“A bank’s marketing starts with proper relationship with customers either to attract saving or fro the loan disbursement. Both the depositors and creditors are customers of the bank. Banks offer various products for deposit mobilization and disburse the credit products as per the portfolio management. Customers as per their need, purchase different types of product offered in the market. Deposit products offered to the customers are categorized into general products and special products. And credit products can be bifurcated into fund based products and non-fund based products” (NRB, 2007:1). The fund based products in practice are developed from the credit products generally known as overdraft, working capital, loan, term loan, bill purchase or negotiation, export and import bills, import/trust receipt loan, export credit, loan against fixed deposit receipt, loan against shares, loan against securities, loan against bank guarantee and deprived sector loan. The term loan used in practice generally addresses short term loan, medium term loan and long term loan to be advanced in various forms such as housing loan, hire purchase loan and bridge financing. The non-fund based product is composed of letter of credit (LC) and bank guarantee in different forms (bid bonds, performance bonds etc.).

Among different banking products available in the market, the product with high demand are consumer credit, export and import credit, term loan, project loan and

syndicate loan. All banks and financial institution on the basis of their capital base and liquidity position offer these credit products but none of them so far as have been found to have expertise in any one of them for marketing. Relying on any one product by portfolio seems more risky. Banks in foreign Countries are known to bring out numerous products. As an example, the bank of America has the vast range of banking business, serving individuals and small firms and a big share of loan syndicate market” (Economist, 2006:10). It means markets are there for some products and it is created for others. Banks in Nepal are weak in locating the existing market and creating new markets too.

“Loan disbursement is a trade of win-win game lenders and burrowers both get benefited out of it. Customers are the ultimate source of income not products. For the analysis of customers several questions need to be answered. These include questions such as who buys the product and how they use it, where do they buy the products, when do customers buy, how do customers choose, why they prefer that product, how they respond, and will they buy it again? All these data available in the respective files of the customer make the marketing activities quite easier and effective” (NRB, 2007:3).

Market makers play an important role in the contract between the burrowers and the bank. In the principle, it is the duty of the consultant to sell the project on behalf of the burrower to the bank. The rejection of the product can raise a question about the knowledge and quality of the consultant. But in Nepal, after the preparation of the project, the duty of the consultant gets over. And it id the burrower who exercises his personal contact to get the project approved.

Each bank follows some process and system for loan approval and for accepting deposits. At first, the banks demand a detailed proposal of a project along with an application for loan. The respective loan officer accesses the proposal submitted to

the bank and recommends for approval if the proposal is found viable. Normally, only feasible projects are accepted. The preparation of the project proposal is a professional job assigned to any consulting firm or organization. To get the bank credit properly and effectively, there is a network of parties involved in the burrowing. These parties are: a) burrower, b) Consulting firm for the project preparation, c) bank and d) consulting firm for collateral valuation.

2.1.1 Concept of Portfolio

A portfolio is the holding of a collection of investment. For some individuals and institutions, it is the entire holdings consisting of both assets and liabilities. An investment held as part of portfolio is less risky than the same investment held individually. Therefore,, every individual and institutions should manage the portfolio by which the individuals and institutions get maximum return. The concept of portfolio comes from “NOT PUTTING ALL THE EGGS IN ONE BASKET.”

2.1.2 Concept of Portfolio Management

The management of portfolio is called portfolio management. Portfolio theory evaluates the reduction of non-systematic or diversifiable risks through the selection of securities or other instruments in to a composite holding or efficient portfolio. Efficient portfolio means that a portfolio would offer lower risks or more stable returns for targeted return level. Instruments that have independent returns lower non-systematic risks. In addition, instruments that are inversely related on a return basis reduce the diversifiable risks.

2.1.3 Assumptions of Portfolio Management

The basic theory assumes that the returns are independent, investors expectations are homogeneous and that normalizes probability distributions are stable.

2.1.4 Objective of Portfolio Management

The portfolio manager's task is to select the investment weights that will result in dominant investment. Hereafter, dominant assets will be called “efficient portfolios” whether they contain one or many assets. An efficient portfolio is any asset or combination of assets that has (1) the minimum expected return in its risk class or conversely, (2) the minimum risk at its level of expected return.

Investment positions are undertaken with the goal of earning some expected rate of return. Investors seek to minimize inefficient deviations from this expected rate of return. Diversification is essential to the creation of an efficient investment because it can reduce the variability of returns around the expected return.

A healthy development of any bank depends heavily upon its investment policy. A sound and viable investment policy can attract both borrowers and lenders which help to increase volume and quantity of deposits, loans and investments. The loan provided by commercial bank is guided by fundamental principles such as length of time, their purpose, profitability, safety and so on. These fundamental principles are fully considered while making investment policy. Emphasizing upon this H.D. Crosse stated, “The investment policy should be carefully analyzed.” Commercial bank should ensure minimum risk and maximum profit from lending.

“Commercial bank should consider the national interest followed by borrower's interest and the interest of the bank itself, Before investing to the borrowers.” to further pursue his views bank lending must be for such purpose of the borrowers that are in keeping with the national policy and bank's overall investment policy” (Clemens, 1994:29).

Optimal investment decision plays a vital role in each and every organization. But especially for the commercial banks and other financial institutions the sound

knowledge of investment is the most because the subject is relevant for all surrounding that mobilize funds in view of return. As it is concerned to the commercial banks and other financial institutions, they must mobilize (I.e. Investment in different sectors) their collections (deposits) and other funds towards the profitable, secured and marketable sectors so that they will be in profit. For this purpose the banks and financial institutions should gather the sufficient information about the firm (Clint) to which supposed to be invested. The information include as financial background, nature of the business as well as its ability to repay the loan back. These all information should be gathered from the viewpoint of security.

2.1.5 Portfolio Diversification

Portfolio diversification helps to minimize risk and different diversification techniques have been developed for reducing portfolio risk.

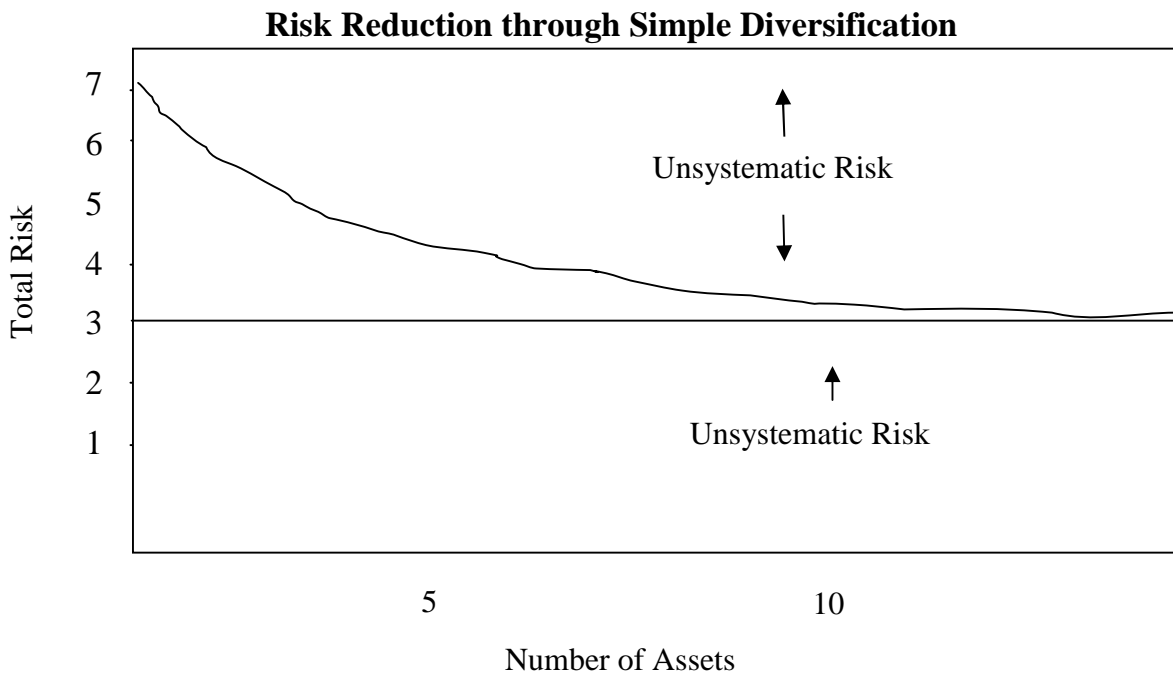
2.1.5.1 Simple Diversification

Simple diversification is defined as not putting all the eggs in one basket. Under this diversification securities are selected and are provided equal weight. The portfolio of randomly selected securities can reduce risk. Further, it is not necessary to include too many securities in the portfolio. A portfolio consisting of 10 to 15 randomly selected securities can eliminate almost all diversifiable risk.

The following figure clarifies more about it.

Portfolio Risk

Figure 2.1



The X-axis and Y-axis in the figure represents the number of securities in the portfolio and standard deviation of the portfolio respectively. From the figure, we can see that randomly combining 10 to 15 stocks reduce a portfolio's un-diversifiable risk. Further, spreading portfolio's assets randomly cannot be expected to reduce risk any further.

2.1.5.2 Diversification across Industries

Some investment counselors advocate selecting securities from different industries to achieve better diversification. It is certainly to better to follow this advice than to select all securities in the portfolio from one industry. But empirical research has shown that diversifying across industries is not much better than simply selecting securities randomly.

2.1.5.3 Superfluous Diversification

If 10 to 15 different assets are selected for a portfolio the maximum reduction benefit from simple diversification have most likely been attained further spreading of the portfolio's assets is superfluous diversification and should be avoided. Because it will usually result in the following portfolio management problems like high research cost, high transaction cost, impossibility of good portfolio management etc. The performance of portfolio will not improve and will lower the net return to the investor.

2.1.5.4 Simple Diversification across Quality Rating Categories

Simple diversification reduces risk within categories of stocks that all have same quality rating. It suggests that portfolio managers can reduce portfolio risk to levels lower than those attainable with simple diversification by not diversifying across lower-quality assets.

2.1.5.5 Markowitz Diversification

“Markowitz diversification is named after Harry Markowitz who first explored it. Markowitz diversification may be defined as combining assets which are less than perfectly positively correlated in order to reduce portfolio risk without sacrificing portfolio return. It is more analytical than simple diversification and considers assets correlation and covariance in portfolio formation. It shows that lower the correlation between assets, the more that the diversification is that there should be combined assets having less than perfectly positively correlated securities” (Bhatara, 2005:115).

2.1.6 Capital Market Theory

Capital market theory provides the framework for determining the pricing of all the assets. Capital market theory deals with an equilibrium model of assets prices.

Specially, capital market theory postulates the exe-ante risk-return relationship in individual assets as well as portfolios under equilibrium conditions.

2.1.7 Capital Assets Pricing Model (CAPM)

“Harry M. Markowitz laid down the foundation of modern portfolio theory in 1952. The CAPM was developed 12 years later by William Sharpe, John Linter and Treynor.

Capital assets are the long term financial as well as real assets and CAPM is based on the pricing of these assets. Modern portfolio theory of Markowitz suggests that the investment decision should be based on the total risk and the price of assets should also be determined on the basis of the total risk. But the CAPM suggests that, any investor can create a portfolio of assets that will eliminate virtually all diversifiable risk, the only relevant risk is non-diversifiable risk, and therefore, the investment decision and the pricing of capital assets should be based on the un-diversifiable risk. This is the primary importance of selecting that the price of capital assets should be determined in a way that compensates the systematic risk” (Bhattacharai, 2005:146).

These assumptions are as follows.

-) All investors have the same one period investment horizon.
-) No taxes and no transaction costs for buying and selling securities exist.
-) No inflation and no change in the level of interest rates exist.
-) The capital market is in equilibrium.
-) All investments are infinitely divisible, fractional shares may be purchased in any portfolio or any individual asset.
-) All investors are Markowitz efficient diversifier who delineate and seek to attain the efficient frontier.

An infinite amount of money can be borrowed or lent at the risk-free interest rate.

The CAPM reduces the situations to an extreme case. Everyone has the same information and agrees about the future prospects for securities. This means that investors analyze and process information in the same way. There are perfect markets for securities because potential impediments such as finite divisibility, taxes, transaction costs and different risk free borrowing and lending rates have been assumed away. This approach allows focusing to shift from how an individual should invest to, what would happen to security prices if everyone invested in similar manner. By examining the collective behaviors in the market place, the nature of the resulting equilibrium relationship between each securities risk and return can be developed. The following features of CAPM are described as follows.

2.1.8 Capital Market Line

The CAPM assumes that investors can lend or borrow at the same risk-free rate of interest. In reality, such borrowing is likely to be either unavailable or restricted in amount. If there are no opportunities to borrow or lend at the risk free rate, the efficient set would be curve and many combinations of risky securities would be efficient. All the investors face the same efficient set. The different investors will choose different portfolios from the same efficient set because they have different preference toward risk and return. The feature of CAPM is often referred to as separation theorem.

2.1.8.1 Separation Theorem

The optimal combination of risky assets for an investor can be determined without any knowledge of the investor's preference towards risk and return. In other words, the optimal combination of risky assets can be determined without any knowledge of the shape of an investor's indifference curves.

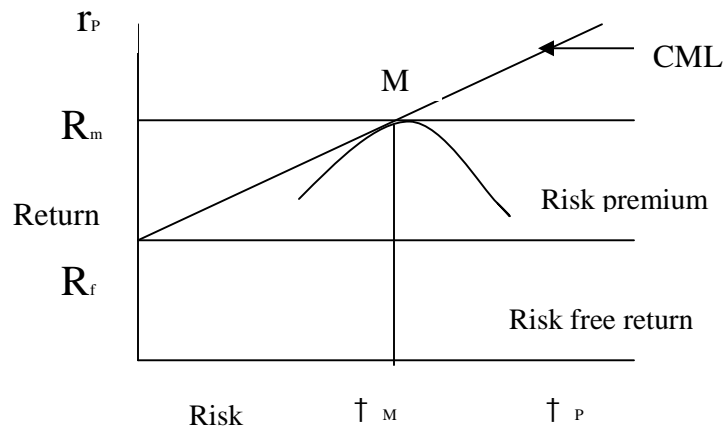
2.1.8.2 Market Portfolio

The market portfolio is a portfolio consisting of all the securities where the proportion invested in each security corresponds to its relative market value. The relative market value of a security is equal to the aggregate market value of the security divided by the sum of aggregate market values of all securities. It plays a central role in the CAPM because the efficient set consists of an investment in the market portfolio, coupled with a desired amount of either risk free borrowing or lending.

2.1.8.3 Efficient Set

In the CML it is simple to determine the relationship between risk and expected return for efficient portfolio. The Fig. 2.2 Clarifies More about it.

Figure 2.2
Capital Market Line (CML)



Point M represents the market portfolio and R_f represents the risk free rate of return. Efficient portfolio plots along the line starting at R_f and going through M and consist of alternative combinations of risk and return. The linear efficient set of CAPM is known as capital market line (CML). All portfolios are other than those using the market portfolio and risk free borrowing or lending lie between the

CML. It has an intercept of R_f and a slope $[E(R_m) - R_f] / \sigma_m$. Therefore, the equation may be expressed as follows.

Symbolically,

$$E(R_p) = R_f + \left[\frac{R_m - R_f}{\sigma_m} \right] \sigma_p$$

Where,

R_f = Risk free asset.

R_m = Expected return on market portfolio

σ_m = Standard deviation on market portfolio

σ_p = Portfolio risk on efficient

For a portfolio on the CML, the expected return is equal to the risk free rate plus a return proportional to the total risk of portfolio. The slope of the CML is the same for all portfolios on the CML and is the market price of the risk.

$$\text{Slope of CML} = E(R_m) - R_f / \sigma_m$$

Since each of the portfolios on the CML is perfectly diversified, these portfolios have an expected return about the risk free rate proportional to their own total risk.

2.1.9 Security Market Line (SML)

The capital market line (CML) is the relationship between total risk and portfolio, σ_p and the expected portfolio return, $E(R_p)$ which consists of the total risk free asset and the market portfolio. However, the total risk of an individual asset should not be used to measure its riskiness. Because some of the risk as reflected in total risk can be eliminated by diversification. Therefore, since its beta reflected risk diversification benefits into account, β_i rather than σ_i is used to measure individual assets' riskiness to investors. The relationship between individual assets' riskiness and their required return is set forth in the security market line (SML).

The line is drawn in expected return and beta space. It is linear and positively sloped. Irrespective of whether investors can borrow or lend at the risk free rate, all individuals' securities and portfolios are positioned on the security market line. The relationship between an asset return and its systematic risk can be expressed by SML. The equation for the AML is,

Symbolically,

$$E(R_j) = R_f + [E(R_m) - R_f] \beta_j$$

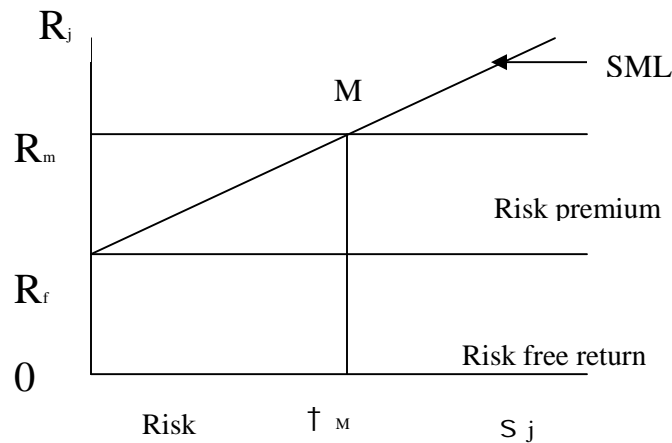
Where,

$E(R_j)$ is the expected return for an assets,

R_f is the risk-free rate (usually assumed to be a short term T-bill rate) equals the expected market return (usually based on NEPSE index) and

β_j denotes the assets' beta. It is measure of sensitivity of a stock's return to changes in the average market returns.

Figure 2.3
Security Market Line



Here, SML starts from the risk free asset (R_f) and moved ahead linearly with beta (β_j), if the securities beta is greater than 1. Then, it implies that the securities returns fluctuate more than the market returns. If the beta is less than 1, the securities returns are less sensitive to the changes in the market. The CAPM theory

indicates that how much required rate of returns of individual securities for bearing the systematic risk.

2.1.10 Empirical test of the CAPM

CAPM was developed on the basis of a set of assumptions. If those assumptions were all true, then CAPM would have to be true. However, all the assumptions are not completely correct. The basic SMC equation, $K_i = (K_m - f)$ might or might not represent an accurate description of how investors behave and how rates are established in the market place.

If many investors are not fully diversified, hence they have not eliminated all diversifiable risk from their portfolio. Then beta would not be an accurate measure of risk and the SML would not fully explain how required return is set. If the interest rate that the investors must pay to borrow money is greater than the risk-free rate, then the CML would not continue in a straight line. For all these reasons, it is entirely possible that the CAPM is not completely valid. Therefore, CAPM must be tested empirically and validated before it can be used with real confidence.

2.1.10.1 Test of the stability of Beta Coefficients

According to the CAPM, the beta used to estimate a stock's market risk should reflect investor's estimates of the stock's future volatility in relation to that of the market. Robert Levy, Marshall Blume and others have studied the questions of beta stability in depth. Levy calculated betas for individual securities as well as portfolios of securities. He concluded that:

The betas of individual stocks are unstable; hence the past betas for individual securities are not good estimators of their future risk.

The beta of the portfolio of ten or more randomly selected stocks is reasonably stable; hence the past portfolio betas are good estimators of future portfolio volatility.

2.1.10.2 The Fama French Study

A recent study by Eugene F. Fama and Kenneth R. French of the University of Chicago seriously challenges the CAPM. Fama and French examined the relationship between betas and returns on thousands of stocks over the past 50 years. According to the CAPM, high beta stocks should provide higher returns than the low beta stocks. However, the Fama French study revealed no relationship between historical betas and historical-low beta stocks provided about the same returns as high beta stocks provided. About the same returns high-beta stocks. It will take more research to decide whether the Fama French study truly invalidates the CAPM. The CAPM is purely an expectation model, and its logic is sound.

Therefore, it again requires a lot of research to decide whether there actually is no relationship between beta coefficient of any stocks and its return. Since CAPM is purely an expectation approach it may not be valid in actual life. However, there is no strong reason to believe that there is no relationship between the return of the stock and its beta; therefore, we cannot conclude that it is not better to use SML equation for the calculation of required rate of return (Fama and French, 1998:246-273).

2.2 Review of Related Studies

2.2.1 Review of Research Papers

Under this heading, the review of research papers of researchers is analyzed to find out the investment policies of commercial banks.

Govinda Bahadur Thapa (1994), expresses his view in his research paper “Financial system of Nepal” that the commercial banks including foreign joint venture banks seems to be doing pretty well in mobilizing deposits. Likewise, loans and advances of these banks are also increasing. But compared to high credit needs particularly by newly emerging industries, the banks still seems to lack adequate funds. The banks are increasing their lending to non-traditional sectors with the traditional sectors. Out of all commercial banks (excluding two recently opened regional commercial' banks), Nepal Bank Ltd. and Rastriya Banijya Bank are operating with the nominal profit, the later turning towards negative from time to time. Because of growing competition and limitation of investment sectors, the spread between interest income and interest expenses is declining. These banks have not been able to increase their income from commission and discount. On contrary, they have got heavy burden of personnel and administrative overheads. Similarly, due to the accumulated overdue and defaulting loans, profit position of these banks has been seriously affected. On the other hand, the foreign joint venture banks have been functioning in an efficient way. They are making profit year after year and have been distributing bonus to their employees and dividends to their shareholders.

He concludes that by its very nature of public sector, these two domestic banks could not compete with the private sectors banks, so only remedy to the problems of these banks, as he government decided, is to handover the ownership as well as the management of these banks to the private hands (Thapa, 1994:29-37).

Radhe S. Pradhan (2003) in his research paper, “Role of Saving, Investment and Capital Formation in Economic Development, A case of Nepal”, has studied about the strong role and impact of saving, investment and capital formation on economic development of Nepal. This study is based on secondary data only. The necessary data on saving, investment, capital formation and gross domestic

product has been collected for the period of 1974/75 to 2000/01. The role and impact of saving, investment and capital formation on economic development were analyzed by using various regression equations used in his study have been estimated as current prices as well as in real terms with the entire study period divided into different sub periods.

The result presented in this paper, suggests that in all cases, GDP is significantly associated with saving, investment and capital formation both at current prices and in real terms. The results of the empirical analysis led to three important conclusions: First, saving, investment and capital formation have positive impact on economic development. Second, the current values and past values of saving, investment and capital formation have positive impact on economic development but the current values have the largest impact. Third, there is strong role played by saving and capital formation on economic development while weak role played by investment (Pradhan, 2003:123-133).

2.2.2 Review of Thesis

Several thesis works have been conducted by various students regarding the various aspects of commercial banks such as lending policy, investment policy, investment planning, and liquidity and invest position, trend of saving investment and capital formation, investment in priority sectors etc. Some of them as supposed to be relevant for the study are presented below:

Shrestha (1993), has conducted a study on “*Investment Planning of Commercial Banks in Nepal*” with the objectives:

-) To evaluate the financial performance of commercial banks in Nepal
-) To examine the investment of commercial banks of Nepal with reference to securities, loans and advances.
-) To establish the relationship of bank’s portfolio variables with the national

income and interest rate

The research findings of the study are summarized as:

-) The general trend of commercial banks asset holding is growing. Deposits have been a major source of funds. The excess reserve level of the banks allows idle money and loss of opportunity. Debt equity ratios are very high, greater than 100%.

-) The return ratios are on the average higher for foreign joint venture banks than for the Nepalese bank but return of asset found to be statistically same. Risk taking attitude is higher in the foreign joint venture banks. The total management achievement index is higher in case off foreign banks in comparison to the Nepalese banks.

-) The hypothesis that the commercial banks have non-professional style of decision making in investment has been accepted. The investment of commercial banks in shares and securities is normal and not found to have strategic decision towards investment in shares and securities. Yield from the security has been found to be satisfactory.

-) Investment in various economic sectors shows individual and commercial sectors taking higher shares of loan till 1990.

-) Investment in various sectors has a positive impact on the national income from their respective sectors.

-) Lending in priority sector showed cottage and small industry sector sharing higher loans.

The secured loan analysis showed commercial loan as being very important followed by social and industrial loans. The loan loss ratio has been found to be increased with low recovery of loan. Demand of bank credit has been found to be affected by the national income and lending and treasury bill rate. The investment

of commercial banks on government securities have been observed to be affected by total deposit, cash reserve requirements and Treasury bill and lending rates. Interest rates, lending rate, deposit rate were found to constitute a set of significant variables affecting the bank portfolio composition.

Wagle (2000), study in his thesis paper “*A study of Trends of Saving, Investment and Capital Formation in Nepal*”, he concluded that in Nepal there is large gap between investment and saving rate. The low saving rate implies that majorities of people are poor. Low rate of saving and investment has been continuing character of Nepalese economy as compared to some selected Asian countries. The need for improving internal savings and investment performance in the country has been high in the agenda of Nepalese policy declarations but the performance has remained poor. The rate of investment and capital formation is low in Nepal because of low saving. He has recommended that the government should review existing restriction on foreign direct investment.

Sapkota (2000), has studied on “*Risk and Return Analysis in Common Stock Investment*”. In his study, he has included eight commercial banks. Sapkota in his study has concluded commercial stock is the most risky security and lifeblood of stock market because expected common stocks attract more investors. Private common stock holders are the passive owners of the company. But the private investors play a vital role in economic development of the nation by mobilizing the scattered capital remained in different form in the society. As overall economy, Nepalese stocks market is in emerging state. Its development is accelerating since the political change in 1990 in effect of openness liberalization in national economy. But the lack of information and poor knowledge, Nepalese private investors cannot analyze the securities as well as the market properly. Still most of the Nepalese private investor invests in single security. Some of the investors use

their fund on two or more securities but they are not able to make and analyze of any portfolio.

Lamichhane (2001), in his thesis, “*Investment policy of the Joint Venture Banks in Nepal*” had analyzed between investment policy and different variables like deposits, commission and discount, net profit, interest on loan and investment. He applied correlation, ratio analysis, t-test, and standard deviations.

He concluded that there is significant relationship between deposit and loan and advances as well as outside assets and net profit but not deposits and total investment in case of Nabil and other joint venture banks. Most of the joint venture banks have focuses their banking services especially to big clients such as to purchase shares and debentures of other financial and non-financial companies.

Loudari (2003), conducted a study on, “A study on investment policy of Nepal Indosuez Bank Ltd. In comparison to Nepal SBI Bank Ltd.” with the objectives of:

-) To examine the liquidity, asset management and profitability position and investment policy of NIBL, in comparison to Nepal SBI Bank Ltd
-) To study the growth ratios of loans and advances and investment to total deposit and net profit of NIBL in comparison to Nepal SBI bank Ltd.
-) To analyze the relationship between deposit and investment, deposits and loan and advances, net profit and outside assets of Nepal Indosuez Bank Ltd. in comparison to Nepal SBI Bank Ltd

The research findings of the study are as follows:

-) Current ratios for both the banks are satisfactory.
-) Although cash reserve ratio is managed by both banks as per Nepal Rastra Bank directives, both banks have not paid sufficient insight towards cash management. Their cash reserve has fluctuated in a high degree.

-)] Nepal SBI Bank Ltd. Has increased investment in government securities where as NIBL has decreased.
-)] NIBL has maintained both current ratio and cash ratio better than SBI Bank ltd. But its cash and bank balance, investment in government securities and loan and advances in comparison to current assets are lower than that of Nepal SBI Bank Ltd.
-)] Deposit utilization of NIBL is less effective than that of Nepal SBI Bank Ltd. Further NIBL has invested lesser amount on government securities and shares and debentures than that of Nepal SBI Bank Ltd.
-)] NIBL did a better performance in return on total assets and loan and advances and interest earning, but it paid lower interest amount to working fund.
-)] The analysis of growth ratios shows that growth ratios of total deposit, loan and advances, total investment and net profit of NIBL are less than that of Nepal SBI Bank Ltd.
-)] The trend value of loan and advances to total deposits ratio is decreasing in the case of both banks. The trend value of total investment to total deposits ratio is also decreasing in case of both banks.

Poudel (2004), in his thesis paper, "*Liquidity and Investment Position of Joint Venture Commercial Bank in Nepal*" had made an attempt to evaluate liquidity and investment of joint venture banks, special reference to Everest Bank Ltd. and Nabil Bank Ltd. He has concluded that liquidity position of EBL is comparatively better than Nabil. Growth rate of investment is higher in EBL than Nabil. He further found the banks do not have constant and consistent liquidity and investment policy. There is no standard and uniform rate or ratio for maintaining liquid assets by commercial banks. A commercial bank at its own judgment may

decide to maintain appropriate level of liquid assets. So he has recommended exploring such investment and to increase its investment on shares and debentures and the bank should have laid down policy for timely review of portfolio and to maintain risk and return.

Pandit (2005), in his thesis, “*A study o n the investment policy analysis of Standard Chartered Bank Nepal Ltd.. in comparison to Nabil Bank Ltd.. and Nepal Bangladesh Bank Ltd.*” has mainly found that SCB's loan and advances to total deposits ratios are significantly lower than that of Nabil and NB Bank, SCB is recommended to follow a liberal lending policy, invest more portion of deposit, loan and advances. He has further stated that besides giving priority of investing on government securities, SCB is recommended to invest its fund in the purchase of shares and debentures of other financial, non-financial companies, hotels and government companies. This also helps in the maintenance of a sound portfolio of banks.

Joshi (2008), has conducted a study entitled “*Risk and Return Analysis of Common Stock of Five Listed Commercial Banks.*” The major objectives of the study are to calculate and analyze the risk and return of banking sector, to evaluate common stock of listed commercial banks and to analyze whether the common stock of commercial banks are correctly priced or not etc.

The major findings of his study are summarized below:

- J Regarding the market capitalization of selected companies, SCBL has the maximum market capitalization and NBBL has the minimum market capitalization.
- J Regarding the market capitalization of the inter industry, Banking sector has 65%, Insurance & Finance has 14%, Manufacturing & Processing sector has 13%, Hotel sector has 7%, Trading sector has 1% and Other sector has negotiable proportion of share in over all market capitalization.

Joshi further concludes that the considering return, the return of SCBL is maximum (i.e.73.30%) but its risk also maximum but if risk is taken into account for consideration, NIBL has the minimum risk of 43.82%. In industry wise analysis, the expected return of finance and insurance has a maximum expected return (i.e. 27.70%), while other sector has a minimum expected return (i.e.16.61%). If the risk is assessed in term of C.V., Banking sector has minimum C.V. like 1.66, which indicates that it is better to invest on the shares of banking sector.

Theme of Joshi's study is summarized as below:

- J As analyzing the Coefficient of variation, he suggests that the banking industry is the best one for investment. Similarly, while analyzing individual securities, SCBL is the best for investment due to highest return and lowest C.V.
- J Based on the findings and conclusion of the study, it is recommended to the investor that if they wish to generate higher return, then they should bear higher risk and invest in the shares of SCBL. But if they are risk averters and they want to invest in single assets, then they can invest in the share of NIBL or HBL because these two stocks have lower risk than that of portfolio risk.
- J Portfolio analysis shows that the portfolio investment can reduce risk significantly. Thus, portfolio investment is recommended to receive high return at minimum risk.

Pokharel (2008), has under taken a study entitled "*Risk & Return on Common Stock Investment of Commercial Banks, With Reference to Six Commercial Banks.*" Among various objectives of his study, some majors basic objectives of his research are to analyze, whether the common stock of commercial banks are correctly priced or not, by analyzing the required rate of return and to study

systematic and unsystematic risk associated with securities of the commercial banks.

Majors finding of his study are given below:

- J Among the six commercial banks, NABIL bank has highest expected rate of return on common stock (i.e.14.03%) and NIB bank has negative expected rate of return on common stock (i.e.-3.9698%). Similarly, The common stock of BOKL is most risky asset, which has highest standard deviation (i.e.52.15%) and HBL's stock is less risky due to lowest standard deviation (i.e.19.49%).
- J Regarding the market capitalization of six selected companies, SCBNL has the maximum market capitalization (i.e.31.36%) and the market capitalization of BOKL is low by 7.11%.
- J Considering the different investment sectors, the expected return of other sector is maximum by 34.53% and the processing sector has very low expected return (-12.076%). Similarly, considering coefficient of variation of different sectors, the trading sector has maximum by 18.49 units, which indicate that to earn 1 unit of return, the investor has to bear 10.49 units of risk. The coefficient of variation on manufacturing & processing is 3.1349 and -3.28 (negative) respectively.
- J On the basis of required rate of return and expected rate of return, the study shows that RRR of NIBL, NABIL, SCBNL, HBL, EBL & BOKL is 0.0175, -0.0677, -0.0174, 0.0099, -0.0526, and -0.0903 respectively. The ERR of NIBL, NABIL, SCBNL, HBL, and BOKL is -0.0396, 0.1403, 0.2264, 0.1158, 0.1312 and 0.0021 respectively. As his study shows that the common stock of NIBL is overpriced and rest of all's common stocks are under priced. At the end of study, Pokharel recommended that before making investment decision, the investor should visit and discussion with investment Companies, with expert and researchers because sharing experience, idea and

view of export will provide grater help. Also advice that the investors need to diversify their investment to reduce risk. Proper construction of portfolio never takes any considerable loss.

Mainali (2009), has performed another study entitled “*Risk and Return Analysis on Common Stock Investment*”. In this study performed an analysis of risk and return on common stock investment with special reference to banking industry. In this study, his writs, the main objective of the study is to determine whether the shares of selected commercial banks are over-priced, under-priced or correctly valued by analyzing the risk and return. Others objectives of the study are evaluate the common stock, to analyze the risk and return and to provide relevant suggestion to concerned authority based on analysis of data. His major findings on his study are given below in details:

- J Among the selected commercials banks, he writs that the SCBNL has highest (i.e.32%) market capitalization which indicates that the size of the stock market of SCBNL is grater one.
- J Regarding the expected rate of return among the selected commercial banks, the highest expected rate of return of SBI is 19.9% and lowest expected return on common stock of NBBL is -27.99%. So, it indicates that the investment in SBI will earn best return.
- J Among the selected banks, the highest C.V. on common stock of NABIL is 12.23 and lowest C.V. common stock of SCBNL is 3.0191. It indicates NABIL stock is more risky and SCBNL stock is less risky than other. Similarly, bet coefficient of SBI is highest (i.e.3.30) and the NIBL has lowest beta coefficient (i.e.0.5831). So, it means C.S. of SBI is most aggressive stock and C.S. of NIBL is most defensive stock than other.
- J At the last, he writs at major finding of his study that the correlation between NIBL and SBI is in negative. It indicates making portfolio investment in these two stocks will

Budhathoki (2009), in this study “*Risk and Return Analysis on Common Stock Investment*” (an analysis of listed commercial banks) concluded that majority of the stock investment has been taking place without base the logical financial evaluation, for most of the investors it is the blind game. Many people have unrealistically optimistic or pessimistic expectations about stock market investments or perhaps the fear of the unknown. This study enables investors to put the return they can expect and the risks they may take into better perspective.

Nepalese stock market is in emerging stage and very new phenomenon to majority of the people though in recent years they have shown participation in stock investment due to growing commercial banks in the country. Our stock market is not sensitive to international stock markets. Its development is getting acceleration after multiparty system in country, since 2046 B.S. It takes place after economic liberalization in national economy since 1992. But due to the lack of proper information and poor knowledge, Nepalese individual investors cannot analyze the securities as well as market properly. This study may helps to have some understanding about stock investment, returns and associated risk there on.

Shakya (2009), on “*Risk and Return Analysis of the Commercial Banks*” has made conclusion that the expected return of EBL and NABIL are highest among the sampled banks i.e. 56.7% and 52.79% respectively. however, SCBL has lowest expected rate of return which is 28.26% followed by HBL with 29.52% expected rate of return. Analyzing the standard deviation of the sampled banks, SCBL is in the best position with standard deviation of 0.33. NABIL is in the worst position with standard deviation as high as 0.91. The coefficient of variance is worst for BOK which is 1.941. All the sampled joint-venture commercial banks have

positive expected rate of return. However, the commercial banking sectors have positive return together with market sector.

2.3 Research Gap

The review of relevant literature has contributed to enhance the fundamental understanding and knowledge, which is required to make the study meaningful and purposive. Various researches have been conducted on portfolio analysis, lending practice, financial performance and credit management of commercial banks. Some of the researches have conducted studies on portfolio analysis. Pandit has tried to attempt investment policy analysis of SCB in comparison with Nabil and NB Bank but the research work had not been completed. First of all, the researcher used financial tools like liquidity ratio capital structure profitability and activity ratio only. But they have not used management quality ratio, asset management ratio in his analysis. Poudel has conducted research on investment position of commercial banks in Nepal. Research does not consider capital adequacy ratio. Other researchers Lamichhane, Loudari, Bajracharya have based their study on financial ratio analysis.

Basically this research work is different from previous research studies because the researcher had tried to attempt all factor of comparative portfolio analysis with reference to different important ratios. In addition, the researcher has tried to analyze quantities as well as qualitative analysis according to available information. Therefore, the researcher has made attempts to study in the area.

CHAPTER - III

RESEARCH METHODOLOGY

The topic of the study has been selected as ' The comparative Study on Portfolio Management of Kumari Bank Ltd. and Everest Bank Ltd.”. The sole objective of his study is to compare the portfolio management practices of Kumari Bank Ltd. and Everest Bank Ltd.

In order to reach and accomplish the objectives of the study, different activities will be carried out. For this purpose, the chapter aims to present and reflect the methods and techniques that are carried out and followed during the study period. The research methodology that is adopted for the present study is mentioned in this chapter which deals with research design, sources of data, data collection, processing and tabulating procedure and methodology.

3.1 Research Design

To achieve the objective of this study, comparative and descriptive research designs have been made.

3.2 Population and Sample

The objective of the study is to explore and describe the portfolio management in Nepal from the investors' point of view. However, with regard to the availability of the financial information, two samples were identified purposefully from the banking sector, which comprise of listed commercial banks. The sample represents reputed two commercial banks of the entire listed commercial banks.

3.3 Data Collection Procedure

Different tools and techniques were adopted while collecting the data for this study. Collected secondary information was analyzed during the course of the desk work. However, during the desk study, an information gap was found. This gap was fulfilled by the discussion with the thesis advisor and the finance experts of the security board and the NEPSE.

3.4 Sources of Data

The data are collected from the secondary source (i.e. Annual reports) of the concerned banks to achieve the objective of the study and also referred the websites for the purpose to complete thesis.

3.5 Data Analysis Tools

Presentation and analysis of the data is one of the important part of the research work. The collected raw data will first be presented in systematic manner in tabular form and then will be analyzed by applying different financial and statistical tools to achieve the research objectives. Besides these some graph charts and tables will be presented to analyze and interpret the findings of the study. The tools applied are:-

3.5.1 Financial Tools

3.5.1.1 Liquidity Ratios

This ratio measures the liquidity position of the firm. It measures the firm's ability to meet its short-term obligations. As a financial analytical tool, following liquidity ratios will be used.

a. Current Ratio

The ratio shows the bank's short term solvency. It shows the ration of current assets over the current liabilities. The ratio can be computed by dividing the total current assets by total current liabilities which can be presented as:

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

Higher ratio indicates the strong short-term solvency position and vice-versa.

b. Cash and Bank Balance to Total Deposit Ratio

Cash and bank balances are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositor. This ratio can be computed by dividing cash and bank balance by total deposit and can be presented as:

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

Cash and Bank Balance includes cash in hand, foreign cash in hand, cheques and other cash items, balance with domestic and foreign banks. The total deposit includes deposit made by customers through different accounts like current (demand deposit), saving, fixed deposit, call deposit and other deposit accounts.

c. Cash and Bank Balance to Current Ratio

This ratio measures the proportion of most liquid assets viz. cash and bank balances among the total current assets of the bank. Higher ratio shows the bank's ability to meet its demand for cash. The ratio is computed by dividing cash and bank balance by current assets, presented as under:

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

d. Investment on Government Securities to Total Current Ratio

The ratio is calculated to find out the percentage of current assets invested on government securities viz. treasury bills and development bonds. The ratio is stated as:

Investment on Government Securities to Total Current Ratio

$$= \frac{\text{Investment on Govt. Securities}}{\text{Current Assets}}$$

3.5.1.2 Asset Management Ratio

Asset management ratio measures the proportion of various assets and liabilities in the balance sheet. The proper management of assets and liabilities ensures its effective utilization. The banking business converts the liability into assets by way of its lending and investing functions. The following are the various ratios relating to determine the efficiency of subjected bank in managing its assets and in portfolio management.

a. Loan and Advances to Total Deposit Ratio

This ratio is also called credit-deposit ratio (CD Ratio) which is calculated to find out how successfully the bank is able to utilize its total deposits on loan and advances for profit generating purpose. Greater ratio implies better utilization of total deposits. This ratio can be obtained by dividing loan and advances by total deposit as under:

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

b. Total Investment to Total Deposit Ratio

Investment is one of the major forms of credit creation to earn income. This implies the utilization of firm's deposit on investment on government securities, shares and debentures of other companies and banks. This ratio can be calculated by total investment divided by total deposit as:

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

c. Loan and Advances to Working Fund Ratio

Loan and advances is the another major component in total working fund(total assets), which indicates the ability of the bank to utilize its deposits in the form of loan and advances to earn high return, the ratio is computed by dividing loan and advances by total working fund, which is stated as under:

$$\text{Loan and Advances to Working Fund Ratio} = \frac{\text{Loan and Advances}}{\text{Total Working Funds}}$$

d. Investment on Government Securities to Total Working Fund Ratio

This ratio shows that bank's investment on government securities in comparison to the total working fund. This ratio can be computed by dividing investment on government securities by total working fund, which can be presented as:

Investment on Government Securities to Total Working Fund Ratio

$$= \frac{\text{Investment on Govt. Securities}}{\text{Total Working Fund}}$$

e. Total outside Assets to Total Deposit Ratio

Loans and advances and investment comprise the total outside asset of the bank. This ratio measures how well the deposits liabilities have been mobilized by the bank in income generation. This ratio is computed by dividing total loan & advances and investment by total deposits, which can be stated as under:

$$\text{Total outside Assets to Total Deposit Ratio} = \frac{\text{Total outside Assets}}{\text{Total Deposits}}$$

f. Loan and Advances to Total Outside Assets Ratio

This ratio measures the proportion of loans and advances of total outside assets. The proportion between investment and loans and advances measures the management attitude towards more risky assets and lower risky assets. This ratio is computed by dividing loan and advances by total outside assets as under:

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

g. Investment on Government Securities to Total Outside Assets Ratio

This ratio measures the proportion of the bank's investment in risky and risk free areas. This ratio is computed by dividing investment on government securities by total outside assets as under:

$$\text{Investment on Government Securities to Total outside Assets Ratio} = \frac{\text{Investment on Govt. Securities}}{\text{Total outside Assets}}$$

h. Total outside Assets to Total Assets Ratio

Loans and advances and investment are total outside assets of commercial banks. This ratio is calculated by dividing total outside assets by total assets which can be presented as under:

$$\text{Total outside Assets to Total Assets Ratio} = \frac{\text{Total Outside Assets}}{\text{Total Assets}}$$

This is the proportion of the assets employed by the bank for the purpose of income generation. This ratio shows the ability of the bank to utilize the funds into income generation assets.

3.5.1.3 Activity Ratios

Activity ratio measures the performance efficiency of an organization from various angles of its operation. These ratios indicate the efficiency of activity of an enterprise to utilize available funds particularly short-term funds. These ratios are used to determine the efficiency, quality and the contribution of loan and advances in the total profitability. The following activity ratios measure the performance efficiency of banks to utilize its funds.

a. Loan Loss Provision to Total Loans and Advances Ratio

This ratio describes the quality of the assets that a bank is holding. Nepal Rastra Bank has directed the commercial banks to classify its loans and advances into the category of pass, sub standard, doubtful and loss on the basis of the maturity of principal to make the provision of 1, 25, 50 and 100 percentages respectively. The provision for loan loss reflects the increasing probability of non-performing loans in the volume of total loans and advances. This ratio is calculated by dividing the loan loss provision by total loans and advances as presented here under:

Loan Loss Provision to Total Loans and Advances Ratio

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

b. Non-Performing Loans to Total Loans and Advances Ratio

This ratio measures the proportion of non-performing loans on total volume of loans and advances. This reflects the quantity of quality assets that the bank has. Higher ratio reflects the poor performance of bank in mobilizing loans and advances and bad recovery rate and vice-versa. This ratio is computed by dividing the non-performing loans by total loans and advances as under:

Non-Performing Loans to Total Loans and Advances Ratio

$$= \frac{\text{Total Non-Performing Loans}}{\text{Total Loans \& Advances}}$$

3.5.1.4 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 the firm should be higher. Under this, the following profitability ratios will be considered.

a. Interest Income to Total Income Ratio

This ratio measures the volume of interest income in total income of the bank. The high ratio indicates the high contribution made by lending and investing and vice-versa. This ratio can be computed by dividing interest income by total income presented as under;

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

b. Total Interest Earned to Total Outside Assets Ratio

This ratio measures the interest earning capacity of the bank through the efficient utilization of outside assets. Higher ratio implies efficient use of outside assets to earn interest. This ratio is calculated by dividing total interest earned by total outside assets and can be mentioned as under;

$$\text{Total Interest Earned to Total Outside Assets Ratio} = \frac{\text{Total Interest Earned}}{\text{Total outside Assets}}$$

The numerator includes total interest income from loans and advances and investment whereas the denominator comprises loan and advances, bills purchased and discounted and all type of investment.

c. Interest Expenses to Total Expenses Ratio

This ratio measures the portion of total interest expenses in the volume of total expenses. The high Ratio indicates the low operation efficiency and vice-versa. This ratio is calculated by dividing interest expenses by total expenses which can be presented as under.

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

d. Total Interest Earned to Total Working Fund Ratio

This ratio is computed to find out the percentage of interest earned to total assets (working fund). Higher ratio implies better performance of the banks in terms of interest earning on its total working funds. This ratio is computed by dividing total interest earned by total working fund presented as under:

$$\text{Total Interest Earned to Total Working Fund Ratio} = \frac{\text{Total Interest Earned}}{\text{Total Working Fund}}$$

e. Total Interest Paid to Total Working Fund Ratio

This ratio depicts the percentage of interest paid on liabilities with respect to total working fund which can be presented as under;

$$\text{Total Interest Paid to Total Working Fund Ratio} = \frac{\text{Total Interest Paid}}{\text{Total Working Fund}}$$

f. Total Income to Total Expenses Ratio

The comparison between total income and total expenses measures the productivity of expenses in generating income. The amount of income that a unit of expenses generates is measured by the ratio of total income to total expenses. The high ratio is the indication of higher productivity of expenses and vice-versa. This ratio is computed by dividing total income by total expenses presented as:

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

g. Total Income to Total Working Fund Ratio

This ratio measures how efficiently the assets of the business are utilize to generate income. It also measures the quality of the assets in income generation. This ratio is calculated by dividing total income by total assets as stated here under:

$$\text{Total Income to Total Working Fund Ratio} = \frac{\text{Total Income}}{\text{Total Working Fund}}$$

h. Return on Loan and Advances Ratio

This ratio indicates how efficiently the bank utilizes its resources in the form of loans and advances. This ratio also measures the earning capacity of its loans and advances which is computed by dividing net profit or loss by loans and advances presented as under:

$$\text{Return on Loan and Advances Ratio} = \frac{\text{Net Profit (Loss)}}{\text{Loans \& Advances}}$$

i. Return on Total Working Fund Ratio (ROA)

This ratio measures the overall profitability of all working fund i.e. total assets. It is also known as return on assets (ROA). This ratio is calculated by dividing net profit (loss) by total working funds. This can be expressed as;

$$\text{Return on Total Working Fund Ratio (ROA)} = \frac{\text{Net Profit (Loss)}}{\text{Total Working Fund}}$$

The numerator indicates the portion of income left to the internal equities after deduction all costs, charges and expenses.

j. 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. The ratio can be computed by dividing net profit by total equity capital (net worth). This can be calculated as;

$$\text{Return on Equity (ROE)} = \frac{\text{Net Profit (Loss)}}{\text{Total Equity Capital}}$$

Here, total equity capital includes shareholder's reserve including profit and loss account, general loan loss provision and share capital i.e. ordinary share and preference share capital.

k. Earning Per Share (EPS)

EPS refers to net profit divided by total numbers of share outstanding. The amount of EPS measures the efficiency of a firm in relative terms.

The ratio is calculated as;

$$\text{Earning Per Share (EPS)} = \frac{\text{Net Profit (Loss)}}{\text{Total Number of Share Outstanding}}$$

l. Net Interest Margin

Net interest margin in general term is the difference between the interests received from investment and loan & advances and interest paid on deposits collected by bank. It shows the bank's efficiency to earn high profit to meet various costs. Higher ratio shows the higher profitability and vice-versa. This ratio is computed by dividing the difference between interest revenues from earning assets and interest costs on borrowed funds by total earning assets which can be expressed as;

Net Interest Margin

$$= \frac{\text{Interest Revenues from Earning Assets} - \text{Interest Cost on Borrowed Funds}}{\text{Total Earning Assets}}$$

Here, interest revenue from earning assets is total interest income of the bank and interest cost on borrowed funds is total interest expenses of the bank. Total loan & advances comprises the total earning assets of the bank.

3.5.1.5 Growth Ratio

To examine and analyze the expansion and growth of the banking business, following growth ratios will be calculated.

-) Growth Ratio of Total Deposits
-) Growth Ratio of Loans & Advances
-) Growth Ratio of Total Investment
-) Growth Ratio of Net Profit

3.5.2 Statistical Tools

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.

3.5.2.1 Mean

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

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

Where,

\bar{X} = Mean of the values

$\sum X$ = Summation of values

N= Number of observations

3.5.2.2 Standard Deviation

The standard deviation measures the absolute dispersion. It is said that higher value of standard deviation the higher the variability and vice-versa. Karl Pearson introduced the concept of standard deviation in 1823 A.D. and this is denoted by small Greek letter (pronounced sigma). The formula to calculate the standard deviation is given below;

$$\sigma = \sqrt{\frac{\sum x^2}{N}}$$

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

3.5.2.3 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.

$$\text{Coefficient of Variation (C.V.)} = \frac{\sigma}{X} \times 100$$

3.5.2.4 Measure of Correlation

We examine the relationship 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 relationship between two variables increase or decrease with the increase or decrease in another, then such variables are correlated variables. The reliability of 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 analyzes the relationship between those variables by which it is helpful to make appropriate investment policy for profit maximization. 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 Deviation of X

σ_2 = Standard Deviation 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.

3.5.2.5 Trend Analysis

Among the various methods of determining trend of time series, the most popular and mathematical method is least square method. Using this least square method, it has been estimated the future trend values of different variables. For the estimation of linear trends line following formula can be used;

$$y = a + bx$$

Where,

y=Dependent Variables

x=Independent variables

a=Y-intercept

b=slope of the trend line.

With the help of the given equation, the trend in deposit collection, investment, profit etc can be easily obtained for the future period based on given variables and certain assumptions. The trend analysis is a type of projections based on certain assumptions which may or always true. However, with the help of the trend analysis, any investor can judge the future financial positions of the banks and financial institutions.

CHAPTER – IV

PRESENTATION AND ANALYSIS DATA

This chapter has presents analysis and measures of the financial performance analysis practices of KBL and EBL. The presentation and analysis of the various investment aspects of the banks are as follows:

4.1 Liquidity Ratios

Liquidity ratios measure the firm's ability to meet its current obligation. The following ratios which measure the liquidity position of banks are calculated.

Table 4.1
Liquidity Ratios

F.Y.	KBL				EBL			
	1	2	3	4	1	2	3	4
2061/062	1.07	0.07	0.06	0.15	0.08	0.10	0.09	0.18
2062/063	1.06	0.05	0.05	0.13	1.04	0.12	0.10	0.23
2063/064	1.05	0.06	0.06	0.11	1.05	0.13	0.11	0.23
2064/065	1.04	0.07	0.04	0.10	1.03	0.11	0.10	0.18
2065/066	1.03	0.11	0.06	0.03	1.02	0.18	0.19	0.16
Mean	1.05	0.07	0.05	0.10	1.04	0.13	0.12	0.20
S.D. ()	0.01	0.02	0.01	0.04	0.02	0.03	0.04	0.03

(Source: Appendix I-IV)

Where,

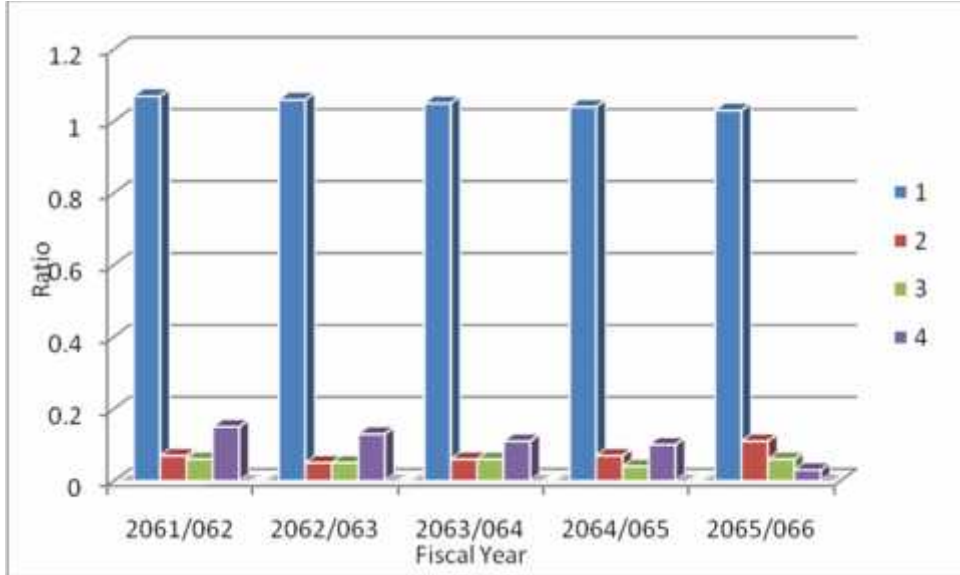
1 = Current Ratio

2 = Cash and bank balance to total Deposit Ratio.

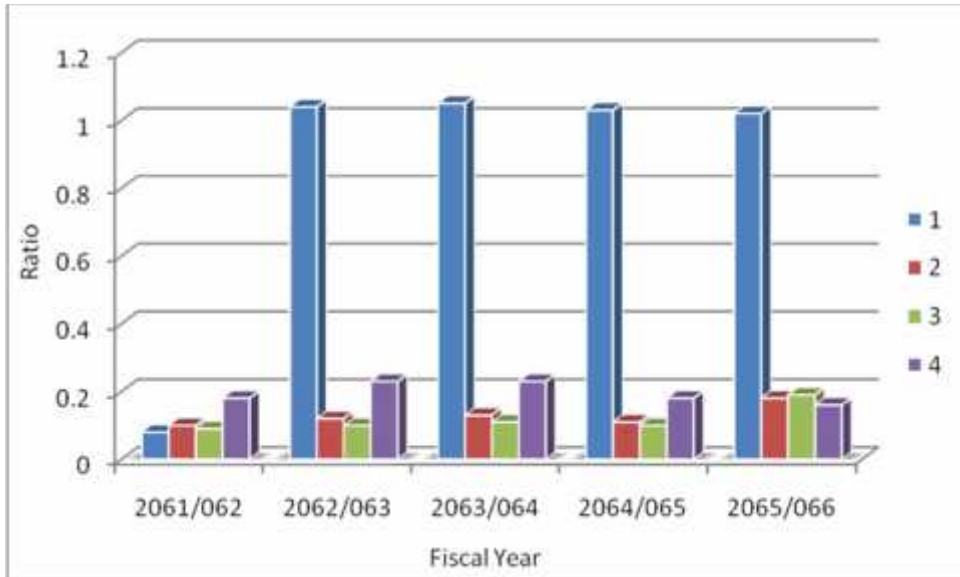
3 = Cash and bank balance to current Assets Ratio.

4 = Investment on Govt. securities to total CA Ratio.

Figure 4.1
Liquidity Ratio
Kumari Bank Limited



Everest Bank Limited



A. Current Ratio

This ratio shows the bank's short term solvency. It shows the ratio of current assets over the current liabilities. Higher ratio indicates the strong short term

solvency position and vice-versa. As being the commercial organization and dependent upon the deposits of the customers, the organization use to maintain the ratio just as the directives of the NRB.

In the above table, the current ratios of KBL are 1.07, 1.06, 1.05, 1.04 and 1.03 for five years starting from FY 2061/062 till 2065/066 respectively with the mean ratio of 1.05 and S.D. 0.01. But in case of EBL the ratios are 1.08, 1.04, 1.05, 1.03 and 1.02 of the same period with the mean of 1.04 and S.D. 0.02. The bank is regarded as the good since it can meet its current obligations. In the periods, the ratio is slightly fluctuated over the periods.

B. Cash and Bank Balance to Total Deposit Ratio

Cash and bank balances are the most liquid current assets. This ratio measures the percentage of most liquid fund with the bank to make immediate payment to the depositor. Higher ratio shows the bank's ability to meet its demand for cash. This ratio can be regarded as the combination of the CRR and LRR. CRR means the Cash Reserve Ratio and LRR means the Liquidity Reserve Ratio. CRR is the amount that is deposited in NRB and LRR is the cash with the bank in its vault. Currently, the CRR fixed by the NRB is 5% of the total deposit.

In the above table, this ratio of KBL is 0.07, 0.05, 0.06, 0.07, and 0.11 in the years starting from FY 2061/062 till 2065/066 respectively with the mean ratio of 0.07 and S.D. 0.02. But in case of EBL the ratios are 0.10, 0.12, 0.13, 0.11 and 0.18 respectively with the mean ratio of 0.13 and S.D. 0.03.

C. Cash & Bank Balance to Current Assets Ratio

This ratio measures the proportion of most liquid assets viz. cash and bank balance among the total current assets of the bank. Higher ratio shows the bank's ability to meet its demand for cash. This ratio should be adequately managed by the bank;

neither too high nor too low since high ratio doesn't yield much interest and low ratio is failure to meet the request of the customers.

In the table above, this ratio of KBL is 0.06, 0.05, 0.06, 0.04, and in the subsequent years starting from the FY 61/62 with the mean ratio of 0.05 and S.D 0.01 and the Ratio of EBL is 0.09, 0.10, 0.11, 0.10 and 0.19 in the same order as in KBL has been presented with the mean ratio of 0.12 and S.D. 0.04. Here, this ratio of EBL bank is slightly fluctuated in fly 2065/066 which is not good as it has been fluctuated.

D. Investment on Govt. Securities to Total Current Assets Ratio

This ratio shows the proportion of government securities of commercial banks in its current assets. The commercial banks invest their funds to various types of government securities such as treasury bills, development bonds and national saving bond. Government securities are not liquid able as much as cash and bank balance. The main objective of the ratio is to examine the portion of government in current assets.

In table above, this ratio of KBL is: 0.15, 0.13, 0.11, 0.10, and 0.03 in the years starting from FY 2061/62 respectively with the mean ratio of 0.10 and S.D 0.04 and the ratio of EBL is: 0.18, 0.23, 0.23, 0.18 and 0.16 as in the order of KBL is presented with the mean ratio of 0.20 and S.D 0.03.

4.2 Assets Management Ratios

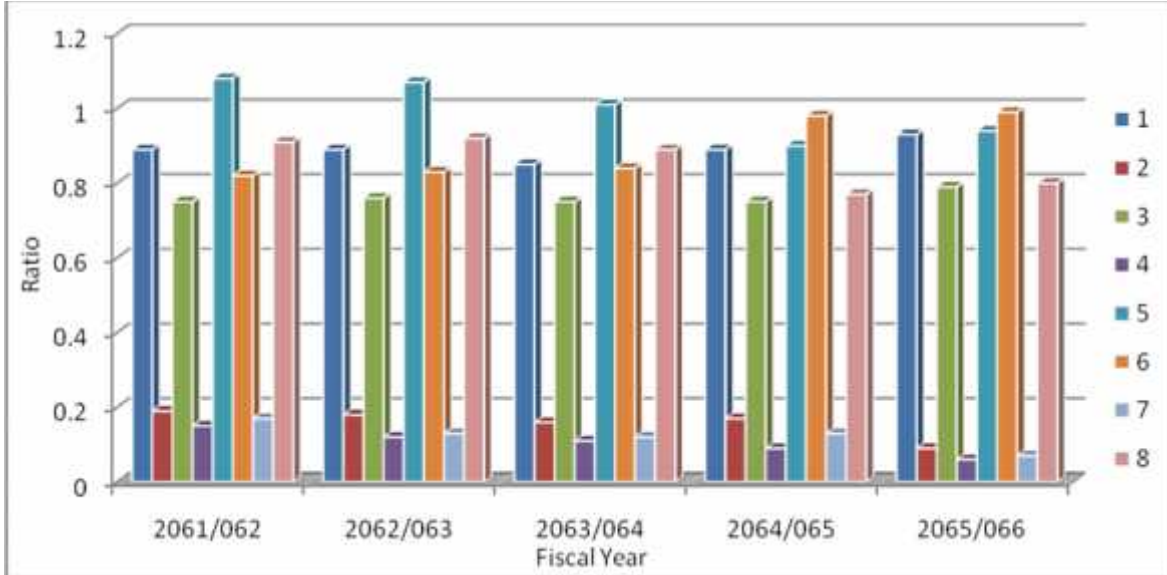
The assets management ratio is used to measure the efficiency of asset utilization of a bank. A commercial bank should be able to manage its assets to gain a sustainable profit so that it can survive in the competitive environment. It is used to measure the bank's efficiency towards its fund mobilization. Following ratios are used to measure the assets management efficiency:

Table 4.2
Assets Management Ratios

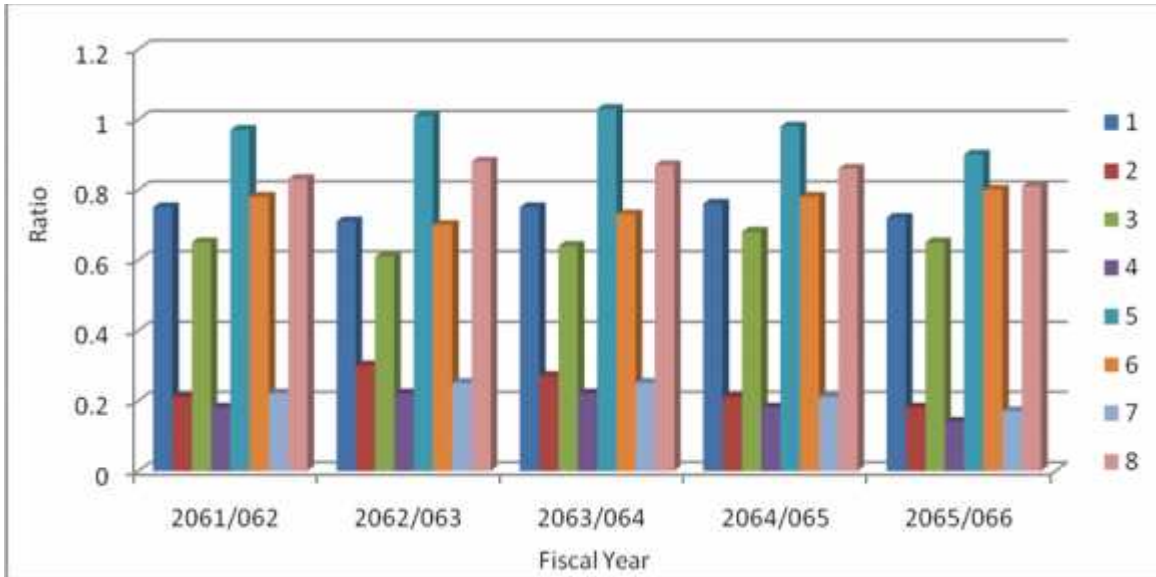
FY	KBL								EBL							
	1	2	3	4	5	6	7	8	1	2	3	4	5	6	7	8
2061/062	0.89	0.19	0.75	0.15	1.08	0.82	0.17	0.91	0.75	0.21	0.65	0.18	0.97	0.78	0.22	0.83
2062/063	0.89	0.18	0.76	0.12	1.07	0.83	0.13	0.92	0.71	0.30	0.61	0.22	1.01	0.70	0.25	0.88
2063/064	0.85	0.16	0.75	0.11	1.01	0.84	0.12	0.89	0.75	0.27	0.64	0.22	1.03	0.73	0.25	0.87
2064/065	0.89	0.17	0.75	0.09	0.90	0.98	0.13	0.77	0.76	0.21	0.68	0.18	0.98	0.78	0.21	0.86
2065/066	0.93	0.09	0.79	0.06	0.94	0.99	0.07	0.80	0.72	0.18	0.65	0.14	0.90	0.80	0.17	0.81
Mean	0.89	0.16	0.76	0.12	1.00	0.89	0.42	0.86	0.74	0.23	0.65	0.19	0.98	0.76	0.22	0.85
S.D.	0.03	0.04	0.02	0.03	0.07	0.08	0.30	0.02	0.02	0.04	0.02	0.03	0.04	0.04	0.03	0.03

(Source: Appendix V-VII)

Figure 4.2
Assets Management Ratio
Kumari Bank Limited



Everest Bank Limited



Where,

1 = Loan and advances to total Deposit Ratio.

2 = Total Investment to total Deposit Ratio.

- 3 = Loan and advances to total working Funds Ratio.
- 4 = Investment on Govt. securities to total working Funds Ratio.
- 5 = Total outside assets to total Deposit Ratio.
- 6 = Loan and advances to total outside Assets Ratio.
- 7 = Investment on Govt. securities to total outside Assets Ratio.
- 8 = Total outside assets to total Assets Ratio.

A. Loans & Advances to Total Deposit Ratio

This ratio measures the efficiency of the bank in mobilizing its deposits on loans and advances to generate the profit of the bank. A high ratio indicates the better the performance of the bank and vice-versa. But the every bank should manage capital adequacy for which the bank should balance between the loans and advances and total deposit. The ratio should be less than or equal to 90% as set by the NRB.

In the above table, this ratio of KBL is 0.89, 0.89, 0.85, 0.89 and 0.93 years starting from FY 061/062 till 065/066 respectively with the mean ratio of 0.89 and S.D. 0.03. But in case of EBL the ratio is: 0.75, 0.71, 0.75, 0.76 and 0.72 respectively with the mean ratio of 0.74 and S.D. 0.02.

B. Total Investment to Total Deposit Ratio

A commercial bank may mobilize its deposits by investing its fund in different securities issued by the government and other financial and non financial institutions. Now the efforts have been made to measure the efficiency of bank in mobilizing its deposits to its investing activities. A high ratio indicates the better performance of the bank in mobilizing its deposits in investment activities and vice-versa. The bank should maintain the balance between the return from the investment and the risk of liquidation from the investment.

In the above table, this ratio of KBL is 0.19, 0.18, 0.16, 0.17 and 0.09 years starting from FY 061/062 till 062/066 respectively with the mean ratio of 0.16 and S.D. 0.04. But in case of EBL the ratio is: 0.21, 0.30, 0.27, 0.21 and 0.18 respectively with the mean ratio of 0.23 and S.D. 0.04.

C. Loans & Advances to Total Working Fund Ratio

A commercial bank's working fund plays very significant role in profit generation actively. The ratio reflects the content to which the bank is successful to mobilize its total assets on loan and advances for the purpose of income generation. A high ratio indicates a better fund mobilization as loan and advances and vice-versa.

In the above, the ratio of KBL is: 0.75, 0.76, 0.75, 0.75 and 0.79 in the years starting from FY 2061/062 till 2065/066 respectively with the mean ratio of 0.76 and S.D. 0.02. But in case of EBL the ratio is 0.65, 0.61, 0.64, 0.68 and 0.65 respectively with the mean ratio of 0.65 and S.D. 0.02. In this regard the KBL is succeeding to mobilize its fund better than EBL.

D. Investment on Govt. Securities to Total Working Fund Ratio

This ratio presents the proposition of fund invested in government securities to total working fund of the bank. From liquidity viewpoint, higher the ratio of investment on government securities to total working funds higher the liquidity of the bank and vice versa. But higher the ratio also implies the bank's efficiency in investing in other high income generating investment activities. Therefore, the bank should maintain an optimum level of investment in government securities so that the balance between the liquidity and the return can be maintained.

In the above table, this ratio of KBL is 0.15,, 0.12, 0.11, 0.09, and 0.06 years starting from FY 061/062 till 065/066 respectively with the Mean ratio of 0.12 and S.D. 0.03. But in case of EBL the ratio is: 0.18, 0.22, 0.22, 0.18 and 0.14 respectively with the mean ratio of 0.19 and S.D. 0.03.

E. Total outside Assets to Total Deposits Ratio

The total outside assets of a bank includes its loan and advances and investment. They are the major fund utilization activity of the bank for generation its income. Loan & advances has return and high risk where as investment has comparatively low return and risk. Loan & advances and investment to total deposits show the firms fund mobilizing power in gross. The main sources of the banks fund its deposits. The ratio shows how the bank is efficient in utilizing its collected deposits in total outside activities.

In the above table, this ratio of KBL is 1.08, 1.07, 1.01, 0.90 and 0.94 years starting from FY 061/062 till 065/066 respectively with the mean ratio of 1 and 0.07. But in case of EBL the ratio is 0.97, 1.01, 1.03, 0.98 and 0.90 respectively with the men ratio of 0.98 and S.D. 0.04. In this regard KBL & EBL are capable in managing this ratio.

F. Loans & Advances to Total outside Assets Ratio

Loan and advances and investment made by the bank comprise the total outside assets of a commercial bank. This is the portion of assets employed by the bank for the purpose of income generation. This ratio measures the contribution made by loan & advances in total amount of loans and advances and investment. The proportion between investment and loans and advances measures the management's attitude towards the risky assets. Loans & advances are more risky and also generate more return in comparison to investments. The total mobilized fund i.e. loan and advances and investment in whole doesn't provide the quality of assets that the bank has created. Thus, this ratio measures the risk of the banking business also. The high ratio indicates the mobilization of funds in more risky area and vice-versa.

In the above table, this ratio of KBL is: 0.82, 0.83, 0.84, 0.96 and 0.99 years starting from FY 2061/062 till 2065/066 respectively with the mean ratio of 0.89 and S.D. 0.08. But in case of EBL the ratio is 0.78, 0.70, 0.73, 0.78 and 0.80 respectively with the mean ratio of 0.76 and S.D. 0.04. In this regard KBL has lent its funds in risky area as described above than EBL.

G. Investment on Govt. Securities to Total outside Assets Ratio

The total outside assets indicates composition of total risky and risk free assets. The investment on government securities is the risk-free risk free assets where the total outside assets is the composition of risky and risk-free assets or assets holding average risk. This ratio helps us to measure the risk of the bank's business. Higher the ratio lowers the bank's business and vice-versa. This also presents the management's attitude towards the risk. In the other hand, higher the ratio lowers the return and vice-versa. Here the bank should also maintain the optimum level of these two assets so that the ban should also maintain the optimum level of these two assets so that the balance between risk and return is maintained.

In the above table, this ratio of KBL is: 0.17, 0.13, 0.12, 0.13 & 0.07 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.42 & S.D. 0.30. But in case of EBL the ratio is: 0.23, 0.25, 0.25, 0.21 & 0.17 respectively with the mean ratio of 0.22 & S.D. 0.03.

H. Total outside Assets to Total Assets Ratio

Commercial bank's outside assets includes its loans & advances and investment. Total outside assets is the fund that in used for income generating purpose where as the total assets include all the income generating assets and non-income generating assets. A high ratio indicates better mobilization of funds in the form of income generating assets from the return viewpoint vice-versa.

In the above table, this ratio of KBL is: 0.91, 0.92, 0.89, 0.77 & 0.80 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.86 and S.D. 0.02. But in case of EBL the ratio is: 0.83, 0.88, 0.87, 0.86 & 0.85 respectively with the mean ratio of 0.85 & S.D. 0.03. Same as incase of 0.82, 0.85, 0.84, 0.83 and 0.84 respectively with the mean ratio of 0.84 & S.D. 0.01. All the banks have adequate ratios in every fiscal year.

4.3 Activity Ratios

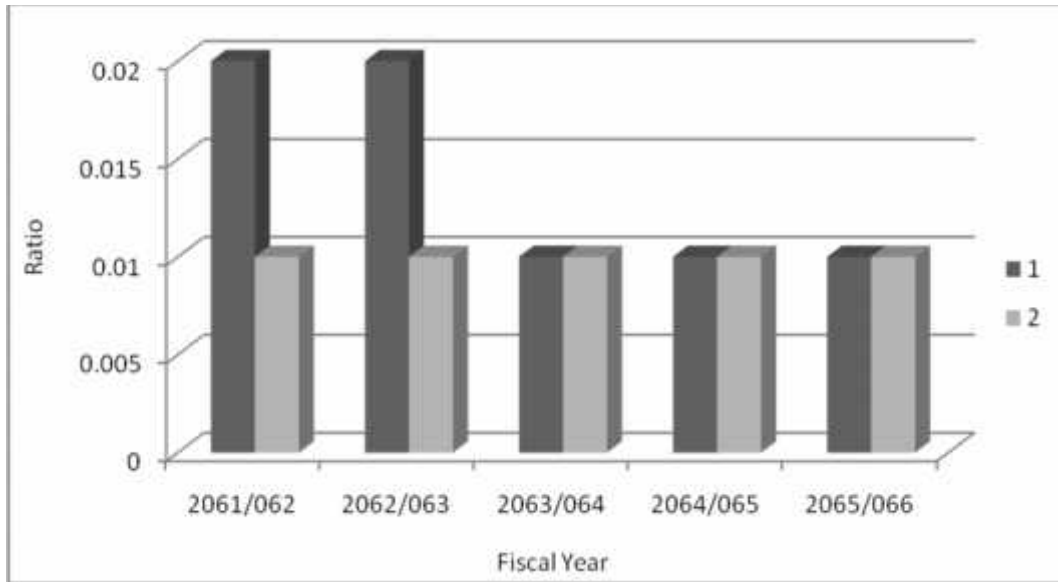
The activity ratio which is also called performing ratio is calculated to measure the lending efficiency in terms of quality and turnover. To measure the ratios of various relationships between balance sheet items and P/L items are established. The following ratios are calculated to measure the activity ratios, which are presented as follows:

Table 4.3
Activity Ratios

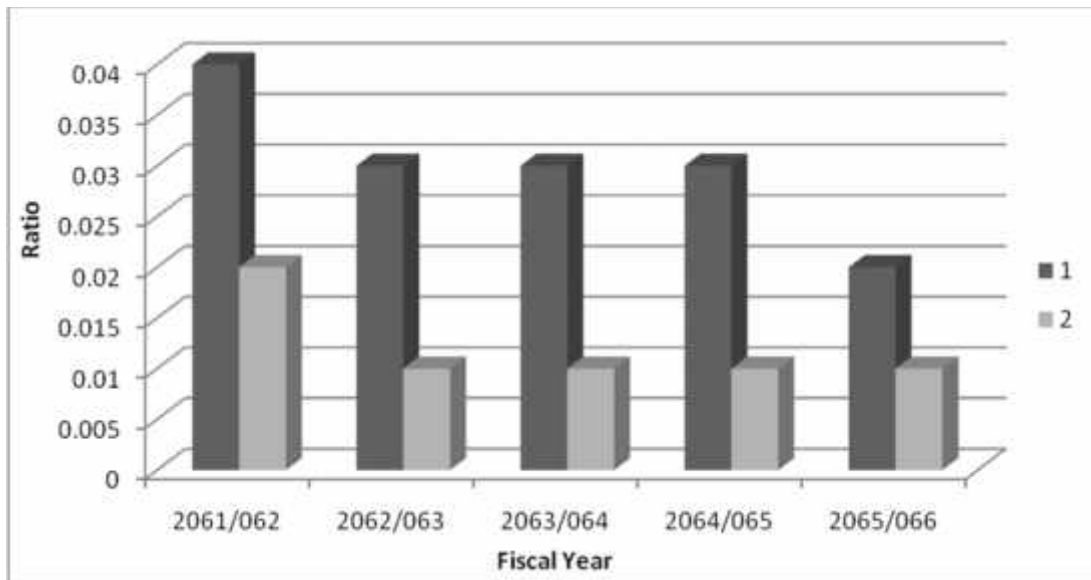
F.Y.	KBL		EBL	
	1	2	1	2
2061/062	0.02	0.01	0.04	0.02
2062/063	0.02	0.01	0.03	0.01
2063/064	0.01	0.01	0.03	0.01
2064/065	0.01	0.01	0.03	0.01
2065/066	0.01	0.01	0.02	0.01
Mean	0.01	0.01	0.03	0.01
S.D. ()	0.005	0	0.01	0

(Source: Appendix XIII-XIV)

Figure 4.3
Activity Ratios
Kumari Bank Limited



Everest Bank Limited



Where,

1 = Loan loss provision to total Loan and advances Ratio.

2 = Non-Performing loans to total Loans and advances Ratio.

A. Loan Loss Provision to Total Loans & Advances Ratio

The loan loss ratio shows how efficiently the bank manages its loans and advances and makes effort for timely recovery of loans & advances. NRB has directed the commercial banks to classify its loans & advances into the category of pass, substandard, doubtful, and loss of make the provision of 1%, 25%, 50% & 100% respectively. NRB has classified the pass loan as performing loan and other three types of loans as non-performing Assets (NPA) of the commercial banks. Loan loss provision set aside for performing loans is defined as general loan loss provision and loss provision set aside of non-performing is defined as specific loan loss provision. The higher the ratio indicates increasing probability of non-performing loans in the volume of loan & advances. On the other hand, loan loss provision signifies the cushion against future contingency crated by the default of

the borrowers. The high ratio signifies the relatively more risky assets in the volume of loans & advances.

In the above table, this ratio of KBL is: 0.02, 0.02, 0.01, 0.01 & 0.01 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.01 & S.D. 0.005. But in case of EBL the ratio is: 0.04, 0.03, 0.03, 0.03 & 0.02 respectively with the mean ratio of 0.03 & S.D. 0.01. This shows that the ratio of EBL is higher than that of KBL.

B. Non-Performing Loans to Total Loans & Advances Ratio

Non-performing loan includes the loan, which lies in the category of su-standard, doubtful, and bad loan. The ratio measures the proportion of non-performing loan on the volume of loan & advances. It shows the quality of lending of the bank. Higher the ratio indicates the poor performance of the bank in terms of collecting loan and vice-versa.

In the above table, this ratio of KBL is: 0.01, 0.01, 0.01, 0.01 & 0.01 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio 0.01 & S.D. 0. But in case of EBL the ratio is: 0.02, 0.01, 0.01, 0.01 & 0.01 respectively with the mean ratio of 0.01 & S.D. 0.

4.4 Profitability Ratios

Each and every business organization is established to earn profit. The main objective of commercial banks is to earn profit by providing different types of banking services to its customers. Profitability ratios are helpful to measure the overall efficiency of a bank. The profit of the bank is affected by the various activities of the bank such as: liquidity activity, assets management activity, and leverage activity. Therefore, profit is the major indicator of the efficiency of the operation of the bank. Higher profitability ratio shows the better efficiency of the

bank and vice-versa. The following ratios are calculated to measure the profitability ratios which are presented below:

Table 4.4
Profitability Ratios
Kumari Bank Limited

FY	1	2	3	4	5	6	7	8	9	10	11	12
2061/062	0.92	0.07	0.68	0.67	0.03	1.53	0.07	0.02	0.01	0.136	17.58	0.05
2062/063	0.65	0.07	0.69	0.07	0.04	1.93	0.10	0.02	0.01	0.120	16.59	0.04
2063/064	0.63	0.07	0.69	0.07	0.03	2.19	0.11	0.02	0.01	0.166	22.75	0.04
2064/065	0.54	0.08	0.75	0.06	0.03	2.65	0.12	0.02	0.01	0.128	16.197	0.04
2065/066	0.60	0.09	0.80	0.07	0.04	2.27	0.12	0.01	0.01	0.161	22.011	0.04
Mean	0.67	0.07	0.72	0.07	0.03	2.11	0.10	0.02	0.01	0.142	19.032	0.04
S.D. ()	0.13	0.01	0.05	0.00	0.00	0.37	0.00	0.00	0.00	0.018	2.793	0.00

(Source: Appendix XV-XXVI)

Everest Bank Limited

FY	1	2	3	4	5	6	7	8	9	10	11	12
2061/062	0.84	0.07	0.61	0.06	0.03	1.77	0.07	0.02	0.01	0.21	54.23	0.06
2062/063	0.58	0.06	0.65	0.06	0.03	2.55	0.10	0.02	0.01	0.25	62.78	0.05
2063/064	0.58	0.06	0.66	0.05	0.02	2.54	0.10	0.02	0.01	0.25	78.42	0.05
2064/065	0.52	0.07	0.62	0.06	0.02	2.92	0.11	0.02	0.02	0.24	93.32	0.05
2065/066	0.65	0.07	0.82	0.06	0.03	2.72	0.10	0.03	0.02	0.29	99.96	0.05
Mean	0.63	0.07	0.67	0.06	0.03	2.50	0.10	0.03	0.01	0.25	77.74	0.05
S.D. ()	0.11	0.01	0.08	0.00	0.01	0.39	0.01	0.00	0.01	0.03	17.40	0.00

(Source: Appendix XV-XXVI)

Where,

- 1 = Interest Income to Total Income Ratio
- 2 = Total Interest Earned to Total outside Assets Ratio.
- 3 = Interest Expenses to total Expenses Ratio.
- 4 = Total Interest Income to total Working Fund Ratio.
- 5 = Total Interest Expenses to total working fund Ratio.
- 6 = Total Income to Total Expenses Ratio.
- 7 = Total Income to Total Working Fund Ratio.

8 = Return on Loans & Advances Ratio.

9 = Return on Total Working Fund Ratio (ROA).

10 = Return to Equity (ROE).

11 = Earning per Share (EPS)

12 = net Interest Margin.

A. Interest Income to Total Income Ratio

Interest income is the major source of the bank's total income. It measures the proportion of interest income in total income of the bank. This ratio also indicates how well the bank is able to mobilize its fund in interest generating activity.

In the above table, this ratio of KBL is: 0.92, 0.65, 0.63, 0.54 & 0.60 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.67 & S.D. 0.13. But in case of EBL, the ratio is: 0.84, 0.58, 0.58, 0.52 & 0.65 respectively with the mean ratio of 0.63 & 0.55. This shows that the ratio of these banks is slightly fluctuating over the periods.

B. Total Interest Earned to Total outside Assets Ratio

The outside assets include loan & advances and investment of commercial banks. It is the sources of interest income of the bank. The ratio reflects the extent to which the bank is successful to earn interest as major income from the outside assets. A high ratio indicated high earning power of total outside assets and vice-versa.

In the above table, this ratio of KBL is: 0.07, 0.07, 0.07, 0.08 & 0.09 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.07 & S.D. 0.01. But in case of EBL the ratio is: 0.07, 0.06, 0.06, 0.07 & 0.07 respectively with the mean ratio of 0.07 & S.D. 0.01. This shows that the ratio of these three banks is slightly fluctuating over the periods.

C. Interest Expenses to Total Expenses Ratio

The ratio measures the proportion of interest expenses to total expenses. Higher the ratio means higher cost of funds of the bank.

In the above table, this ratio of KBL is: 0.68, 0.69, 0.69, 0.75 & 0.8 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.72 & S.D. 0.05. But in case of EBL the ratio is: 0.61, 0.65, 0.66, 0.62 & 0.82 respectively with the mean ratio of 0.67 & S.D 0.08. This shows that the ratio of KBL is more than EBL.

D. Total Interest Income to Total Working Fund Ratio

The ratio reflects the proportion of total interest income to total working fund. Higher the ratio indicates the bank has portion of interest income with respect to total working fund and vice-versa. The higher ratio shows the better efficiency of the bank.

In the above table, this ratio of KBL is: 0.07, 0.07, 0.07, 0.06 & 0.07 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio 0.07 & 0. But in case of EBL the ratio is: 0.06, 0.06, 0.05, 0.06 & 0.06 respectively with the mean ratio of 0.06 & S.D. 0 This shows that the ratio of both banks are slightly fluctuate over the periods.

E. Total Interest Expenses to Total Working Fund Ratio

The total interest expenses to total working fund ratio shows the proportion of total interest expenses to total working fund. It shows the efficiency of cost management relating to interest expenses with respect to total working fund. Higher the ratio indicates higher the interest cost of total working fund and vice-versa.

In the above table, this ratio of KBL is: 0.03, 0.04, 0.03, 0.03 & 0.04 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.03 & S.D. 0.01. But in case of EBL, the ratio is: 0.03, 0.03, 0.02, 0.02 & 0.03 respectively with the mean ratio of 0.03 & S.D. 0.01. This shows that the ratio of KBL and EBL is slightly fluctuate over the periods.

F. Total Income to the Expenses Ratio

The ratio shows the proportion of total with respect to total income with respect to total expenses. The profit of the business organization is affected by these two variables. The income increases the profit and loss decreases the profit of a business organization. It is the measurement of the productivity of the expenses in generating the income of a business organization. The amount of income that a unit of expenses generates is measured by the ratio of the total income to total expenses. The high ratio is the indication of higher productivity of expenses and vice-versa.

In the above table, this ratio of KBL is: 1.53, 1.93, 2.19, 2.65 and 2.27 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 2.11 and S.D.0.37. But in case of EBL, the ratio is: 1.77, 2.55, 2.54, 2.92 and 2.72 respectively with the mean ratio of 2.5 and S.D. 0.39. This shows that the ratio of EBL is more than KBL.

G. Total income to Total Working Fund Ratio

The ratio measures the proportion of to total working fund. It measures the efficiency of total working fund in generating total income. The ratio is calculated by dividing the total income by total working fund.

In the above table, this ratio of KBL is: 0.07, 0.10, 0.11, 0.12 & 0.12 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.10 &

S.D. 0. But in case of EBL the ratio is: 0.07, 0.10, 0.10, 0.11 & 0.10 respectively with the mean ratio of 0.10 & S.D. 0.01. This shows that the ratio of KBL and EBL is consistent over the period.

H. Return on Loans & Advances Ratio

Return on loan and advances ratio measures the proportion of net income to loan and advances. It measures the efficiency of the loans and advances in generating the net income. It is calculated by dividend net profit of the bank by its loans and advances. Higher the ratio is the indication of higher performance of loans and advances in generating net profit and vice-versa.

In the above table, this ratio of KBL is: 0.02, 0.02, 0.02, 0.02 & 0.01 in the years stating from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.02 & S.D. 0. But in case of EBL the ratio is: 0.02, 0.02, 0.02, 0.02 & 0.03 respectively with the mean ratio of 0.02 & S.D.

I. Return on Total Working Fund Ratio (ROA)

This ratio measures the proportion of net profit of the bank to total working fund. It measures the efficiency of the working fund in generating its net profit. The ratio is calculated by dividing the net profit by working fund. Higher the ratio means the higher the efficiency of the bank in utilizing its working fund and vice-versa.

In the above table, this ratio of KBL is: 0.01, 0.01, 0.01, 0.01 & 0.01 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.01 & S.D. 0. But in case of EBL the ratio is: 0.01, 0.01, 0.01, 0.02 & 0.02 respectively with the mean ratio of 0.01 & S.D. 0.01.

J. Return on Equity (ROE)

Return on equity shows the proportion of net profit of the bank to its shareholders equity. It measures the efficiency of equity in generating the net profit of the bank. The ratio is calculated by dividing the net profit of the bank by its shareholders equity.

In the above table, this ratio of KBL is: 0.136, 0.120, 0.166, 0.128 & 0.161 in the years starting from FY 2061/62 till 2065/66 respectively with the mean ratio of 0.142 & S.D. 0.018. But in case of EBL the ratio is: 0.21, 0.25, 0.25, 0.24 & 0.29 respectively with the mean ratio of 0.25 & S.D. 0.03.

K. Earning Per Share (EPS)

EPS is calculated by dividing the total net earning of the by total number of shares. It shows the net profit per share. Higher the ratio indicates the higher the efficiency of the bank and vice-versa. It represents the overall efficiency of the bank.

In the above table, this ratio of KBL is: 17.58, 16.59, 22.75, 16.197 & 22.044 in the years starting from FY 2061/62 till 2065/66 respectively with the mean EPS is 19.32 & S.D. is 2.793. But in case of EBL the ratio is: 54.23, 62.78, 78.42, 93.32 & 99.96 respectively with the mean EPS of 77.74 & S.D. 17.40.

L. Net Interest Margin

Net interest margin measures the proportion of net interest (interest income – interest expenses) to loan and advances. It shows the efficiency of the bank to earn profit to meet the other various costs like office, staffing and etc. expenses and to provide the attractive return to shareholders. The ratio is calculated by dividing net interest by loans and advances. Higher the ratio indicates the higher bank's efficiency to meet other expenses and to provide return to shareholders. In the above table, this ratio of KBL is: 0.05, 0.04, 0.04 & 0.04 in the years starting from

FY 2061/62 till 2065/66 respectively with the mean ratio of 0.04 & S.D. 0. But in case of EBL the ratio is: 0.06, 0.05, 0.05, 0.05 & 0.05 respectively with the mean ratio of 0.05 & S.D 0. The ratio of EBL and KBL is slightly fluctuating over the period.

4.5 Growth Ratios

The study is based on the annual reports published by the banks for 5 years starting from FY 2061/62 to 2065/66. And the study is comparative. That is why; the findings of the study cannot be generalized. The growth ratio helps the researchers to determine the trend of the various parameters so that a conclusion about the various parameters of the bank can be outlined. The growth ratio can be calculated by dividing the last period figure by the preceding period figure. Here, the growth ratios related to investment policies are presented and analyzed.

a) Deposits Growth Rate

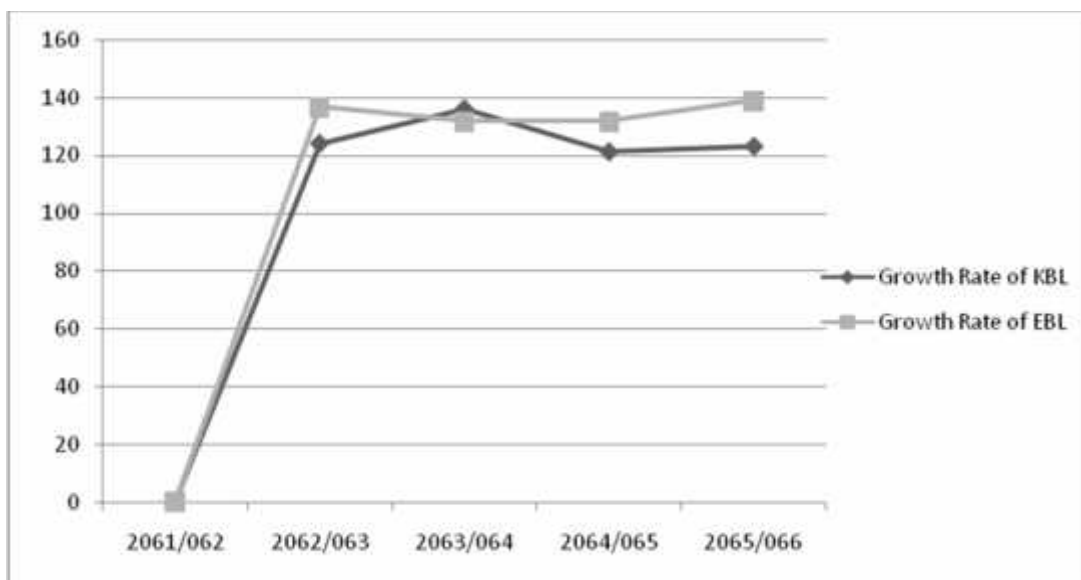
The growth ratio of total deposit shows the trend of the deposits of the bank. It shows the bank's efficiency in increasing its deposits.

Table 4.5
Deposit Growth Rate

FY	KBL		EBL	
	Total Deposit (Rs. in Million)	Growth Rate (in %)	Total Deposit (Rs. in Million)	Growth Rate (in %)
2061/062	6268.95	-	10097.69	-
2062/063	7768.96	123.93	13802.44	136.69
2063/064	1055.42	135.89	18186.25	131.76
2064/065	12780.15	121.05	23976.30	131.84
2065/066	15710.93	122.93	33322.95	138.98

(Source: Appendix V)

Figure 4.4
Deposit Growth Rate



In the above table, the growth rate of KBL is: --, 123.93%, 135.89%, 121.05% & 122.93% in the years starts from FY 2061/62 till 2065/66 respectively. But in case of EBL the growth rate is: --, 136.69%, 131.76%, 131.84% & 138.98% respectively. This shows that the growth rates of all the banks are fluctuating over the period.

b) Loans & Advances Growth Rate

The loan and advances growth rate shows the trend of the loan and advances of the bank.

Table 4.6
Loans and Advances Growth Rate

FY	KBL		EBL	
	Loan & Advances (Rs. in Million)	Growth Rate (in %)	Loan & Advance (Rs. in Million)	Growth Rate (in %)
2061/62	5590.93	-	7618.67	-
2062/63	6891.86	123.27	9801.31	128.65
2063/64	8929.01	129.56	13664.08	139.41
2064/65	11335.09	126.95	18339.09	134.21
2065/66	14593.35	128.74	23884.67	130.24

(Source: Appendix VII)

In the above table, the growth rate of KBL is: --, 123.27%, 129.56%, 126.95% & 128.74% in the years starts from FY 2061/62 till 265/66 respectively. But in case of EBL the growth rate is: --, 128.65%, 139.41%, 134.21% & 130.24% respectively.

c) Investment Growth Rate

The investment growth rate shows the trend of the investment of the bank over the study period. It shows the bank's efficiency to increase its investment.

Table 4.7

Investment Growth Rate

FY	KBL		EBL	
	Investment (Rs. in Million)	Growth Rate (in %)	Investment (Rs. in Million)	Growth Rate (in %)
2061/062	1190.27	-	2128.93	-
2062/063	1394.35	117.20	4200.52	197.31
2063/064	1678.95	120.36	4984.31	118.66
2064/065	2438.80	127.39	5059.56	101.51
2065/066	1510.83	70.64	5948.48	117.57

(Source: Appendix VI)

In the above table, the growth rate of KBL is: --, 117.20%, 120.36%, 127.39% & 70.64% in the years starts from FY 2061/62 till 2065/66 respectively. But in case of EBL the growth rate is: --, 197.31%, 118.66%, 101.51% & 117.57% respectively. This shows that the growth rate of the banks is highly fluctuating over the periods.

d) Net Profit Growth Rate

The net profit growth rate shows the trend of the net profit during the study period. It shows the efficiency of the bank in increasing its net profit.

Table 4.8
Net Profit Growth Rate

FY	KBL		EBL	
	Net Profit (Rs. in Million)	Growth Rate (in %)	Net Profit (Rs. in Million)	Growth Rate (in %)
2061/062	87.88	-	170.81	-
2062/063	103.67	117.97	237.29	138.92
2063/064	170.62	164.23	296.41	124.91
2064/065	174.93	102.53	458.22	154.59
2065/066	261.44	149.45	638.73	139.39

(Source: Appendix XXII)

In the above table, the growth rate of KBL is: --, 117.97%, 164.23%, 102.53% & 149.45% in the years starts from FY 2061/62 till 2065/66 respectively. But in case of EBL the growth rate is: --, 138.92%, 124.91%, 154.59% & 139.39% respectively. This shows that the growth rate of all the banks is fluctuating over the period.

4.6 Correlation Coefficient Analysis

Under this topic, Karl Person's co-efficient of correlation is used to find out the relationship between various independent and dependent variables such as deposits and loans and advances, deposits and investments, loans and advances and net profit, investments and net profit etc. The relationship may be positive and negative. It may be highly significant or insignificant. It helps the researchers to measure the nature and the degree of movement of the relationship between dependent and independent variables.

Table 4.9
Correlation Analysis

	KBL	EBL
Correlation between Deposit and loan and advances	0.9957	0.9970
Correlation between Deposit and Invest rent	0.5655	0.8715
Correlation between loan and advances and net profit	0.9754	0.9904
Correlation between investment and net profit	0.4148	0.4713

(Source: Appendix XXVII-XXX)

a) Correlation Co-efficient between Deposit and Loans and Advances

The correlation co-efficient between deposit and loan and advances measures the nature and degree of relationship between deposit and loans and advances. Here, deposit is independent variable and loan and advances is dependent variable.

In the above table, the correlation co-efficient between deposit and loan and advances of KBL is 0.9957 and of EBL is 0.9970 and SCBL is 0.9321. This means the loans & advances of KBL and EBL are perfectly positively correlated It means to provide the loans & advances to its customers the deposits are required. Higher the volume of deposits higher will be the volume of loans & advances.

b) Correlation Co-efficient between Total Deposits and Total Investment

The correlation co-efficient between total deposits and total investment describes the degree of relationship between these two items. How a unit increases in deposits impact in the volume of investment is measured by this correlation. Here, deposit is the independent variable and the investment is the dependent variable.

In the above table, the correlation co-efficient between deposits and investment of KBL is 0.5655, EBL is 0.8715. This means the deposits and investments are positively correlated but not perfectly.

c) Correlation between Loans & Advances and Total Net Profit

The correlation between total loans and advances and total net profit measures the degree of relationship between total loans and advances and total net profits. It measures whether the net profit is accompanied by increase in the volume of loans and advances. Here, the loans and advances is the independent variable where as the dependent variable.

In the above table, the correlation co-efficient between loans & advances and net profit of KBL is 0.9754, EBL is 0.9904. From this we can say that the amount of net profit heavily depends upon the amount and quality of loans & advances.

d) Correlation between Total Investment and Total Net Profit

The correlation co-efficient between total investment and total net profit measures the degree and the movement of the relationship between these two variables. Here, total investment is the independent variable and the net profit is the dependent variable.

In the above table, the correlation coefficient between investment and net profit of KBL is 0.4148, EBL is 0.4713. This means EBL and KBL have the positive correlation of investment with the net profit.

4.7 Trend Analysis and Projection for Next Five Years

The objective of this section is to present and analyze the trend of the deposits collection, its utilization and net profit of the bank during the study period. Here,

the researcher has presented and analyzed the trend of deposit, loan & advances, investment, and net profit of the bank during the study period.

a) Trend Analysis of Total Deposits

The trend value of deposit is presented in the table from 2061/62 to 2070/71. The trend value of deposit from 2066/67 to 2070/71 is expected values of the deposits in the respective years.

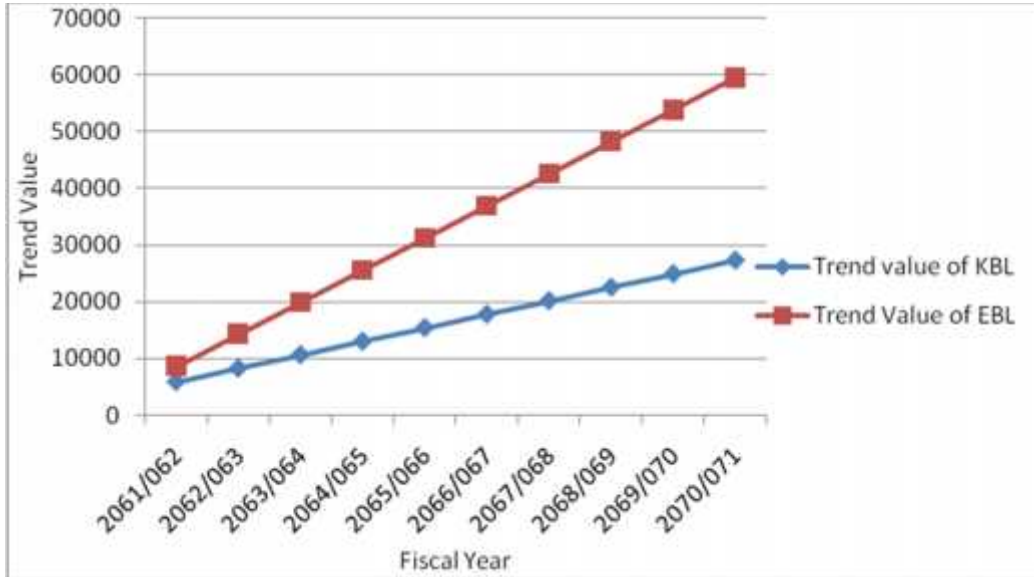
Table 4.10
Trend Analysis of Total Deposits

(Rs. in Million)

FY	KBL		EBL	
	x	Trend value	x	Trend Value
2061/062	-2	5838.24	-2	8552.25
2062/063	-1	8227.76	-1	14214.69
2063/064	0	10617.28	0	19877.13
2064/065	1	13006.80	1	25539.57
2065/066	2	15396.32	2	31202.01
2066/067	3	17785.84	3	36864.45
2067/068	4	20175.36	4	42526.89
2068/069	5	22564.88	5	48189.33
2069/070	6	24954.40	6	53851.77
2070/071	7	27343.92	7	59514.21

(Source: Appendix XXXI)

Figure 4.5
Trend Analysis of Deposit



Here, the effort has been made to analyze the trend values of total deposit of KBL and EBL from 2061/62 to 2070/71, which includes the forecasting of five years. The above table shows the trend values deposits of different period from 2061/62 to 2070/71. The deposit forecasted for the FY 2066/67 of KBL is NPR. 17785.84 million and that for the FY 2070/71 is NPR. 27343.92 million. And of EBL is NPR 36864.45 million for the FY 2066/67 and NPR 59514.21 million for the FY 2070/71.

b) Trend Analysis of Loans and Advances

The trend values of loans & advances are presented in the table. The trend values of loans & advances from 2066/67 to 2070/71 are expected value of loans & advances in the respective years.

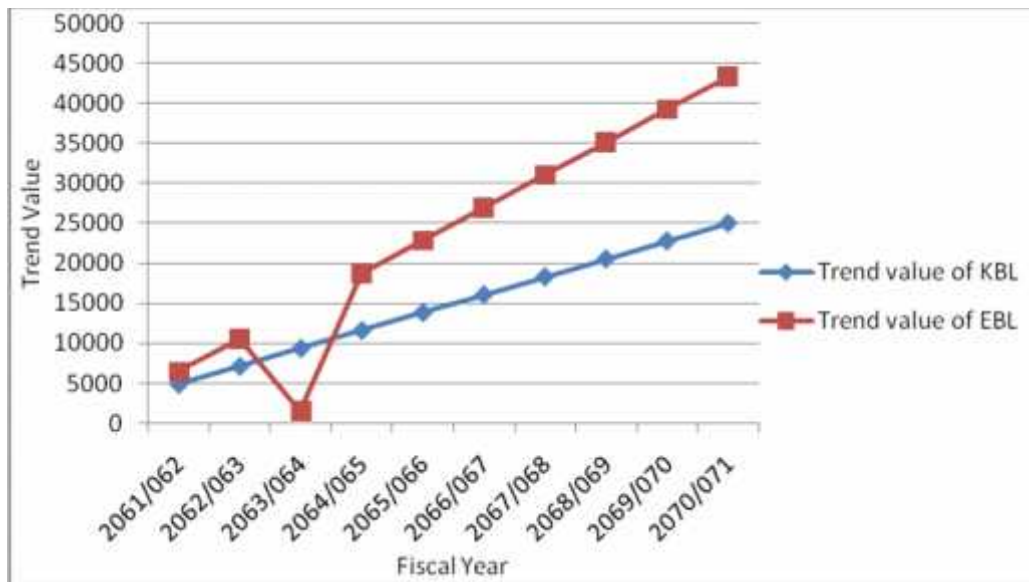
Table 4.11
Trend Analysis of Loans Advances

(Rs. in Million)

FY	KBL		EBL	
	x	Trend value	x	Trend value
2061/062	-2	4838.43	-2	6447.72
2062/063	-1	7083.24	-1	10554.64
2063/064	0	9328.05	0	1466.56
2064/065	1	11572.86	1	18768.48
2065/066	2	13817.66	2	22875.40
2066/067	3	16062.48	3	26982.32
2067/068	4	18307.29	4	31089.24
2068/069	5	20552.10	5	35196.16
2069/070	6	22796.91	6	39303.08
2070/071	7	25041.72	7	43410

(Source: Appendix XXXII)

Figure 4.6
Trend Analysis of Loans Advances



The above table shows that the loans & advances of all the bank is in increasing trend. The expected value of loans & advances of KBL in 2066/67 and 2070/71

are NPR 16062.48 million and 25041.72 million respectively. EBL in 2066/67 is 26982.32 and 43410 million in the year 2070/71.

c) Trend Analysis of Investment

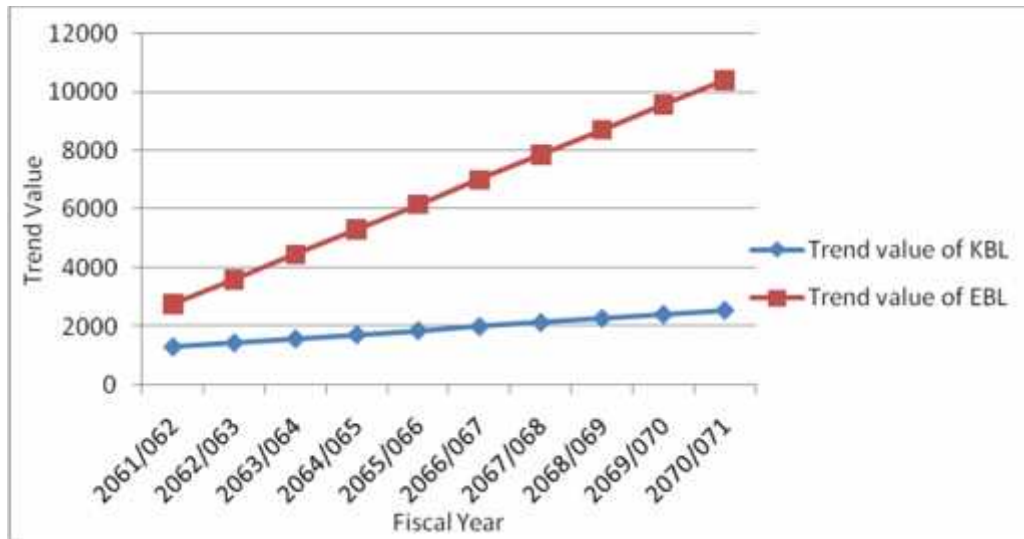
The trend values of investment are presented in the table. The trend values of investment from 2066/67 to 2070/71 are expected values of loans & advances in the respective years.

Table 4.12
Trend Analysis of Investment

FY	KBL		EBL	
	x	Trend value	x	Trend value
2061/062	-2	1305.76	-2	2757.54
2062/063	-1	1444.26	-1	3607.35
2063/064	0	1582.76	0	4457.16
2064/065	1	1721.26	1	5306.97
2065/066	2	1859.76	2	6156.78
2066/067	3	1998.26	3	7006.59
2067/068	4	2136.76	4	7856.4
2068/069	5	2275.26	5	8706.21
2069/070	6	2413.76	6	9556.02
2070/071	7	2552.26	7	10405.83

(Source: Appendix XXXIII)

Figure 4.7
Trend Analysis of Investment



The above table shows that the investment of the entire bank is in increasing trend. The expected value of investment of KBL in the year 2066/67 is 1998.26 million and in the year 2070/71 is 2552.26 million. EBL in the year 2066/67 is 7006.59 million and 10405.83 million in the year 2070/71.

d) Trend Analysis of Net Profit

The trend values of net profit are presented in the table. The trend values of net profit from 2066/67 to 2070/71 are expected value of net profit in the respective years.

Table 4.13
Trend Analysis of Net Profit

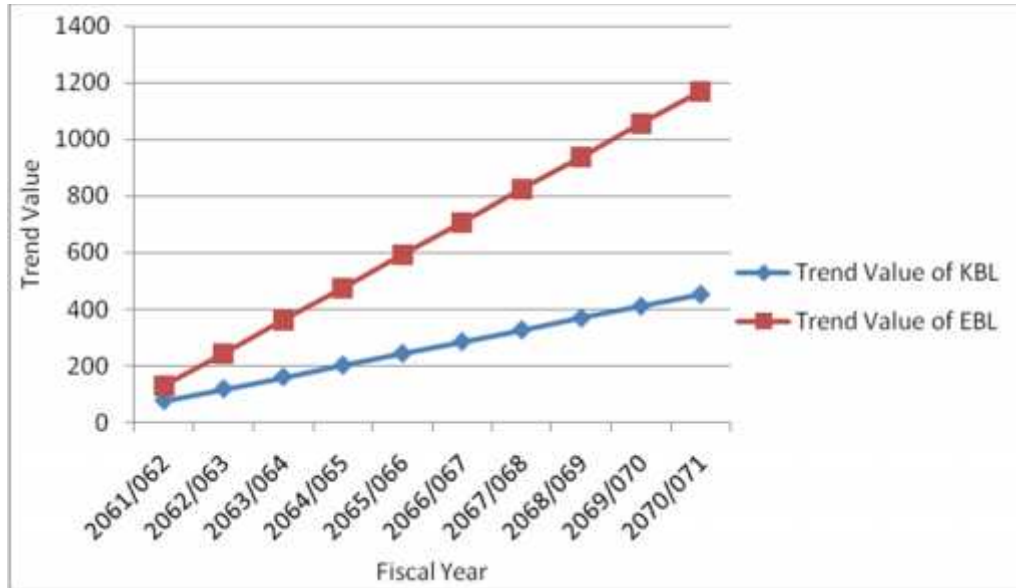
FY	KBL		EBL	
	x	Trend Value	x	Trend Value
2061/062	-2	76.03	-2	128.94
2062/063	-1	117.87	-1	244.62
2063/064	0	159.71	0	360.30
2064/065	1	201.55	1	475.98
2065/066	2	243.39	2	591.66
2066/067	3	285.23	3	707.25
2067/068	4	327.07	4	823.02

2068/069	5	368.91	5	938.7
2069/070	6	410.75	6	1054.38
2070/071	7	452.59	7	1170.06

(Source: Appendix XXXIV)

Figure 4.8

Trend Value of Net Profit



The above table shows that the net profit of the entire bank is in increasing form. The expected value of net profit of KBL in 2066/67 and 2070/71 are 285.23 million and 452.59 million respectively. EBL is 707.25 million in the year 2066/67 and 1170.06 million in the year 2070/71.

4.8 Major Findings of the Study

In the preceding part, the researcher has presented and analyzed the various aspects of the study with the help of the financial and statistical tools. In this part, the researcher has enlisted the major findings in a summarized manner so that a complete picture of the data presentation and analysis can be presented. The major findings of the study, based on the financial and statistical tools can be presented as follows:

A. Liquidity Ratio

1. Current ratio of KBL is ranging from 1.03 to 1.07 over the study period. Current ratio of EBL is ranging from 0.08 to 1.05.
2. Cash and bank balance to total deposit ratio of KBL is ranging from 0.05 TO 0.11 over the study periods however the ratio of EBL is ranging from 0.10 to 0.18 in the same period. Cash and bank balance is the Cash Reserve Ratio (CRR) which is to be managed by the banks in duly manner (not too high and not too low). The minimum CRR to be maintained by the banks is 5% of the total deposit. The so; both banks have maintained the CRR all over the periods.
3. Cash and bank balance to current assets ratio of KBL is ranging from 0.04 to 0.06 during the study period and the ratio of EBL is ranging from 0.09 to 0.19.
4. Investment on government securities to total current assets ratio of KBL is ranging from 0.03 to 0.15 during the study period and the ratio of EBL is ranging from 0.16 to 0.23 of the same period.

B. Assets Management Ratio

1. Loans & advances to total deposit ratio of KBL is ranging from 0.85 to 0.93, it is higher than 90% level & where as the ratio of EBL is ranging from 0.71 to 0.76.
2. Total investment to total deposit ratio of KBL is ranging from 0.09 to 0.19 whereas the ratio of EBL is 0.18 to 0.30. This shows that the ratio of EBL is higher than that of KBL during the study period.
3. Loans & advances to total working fund ratio of KBL is ranging in between 0.75 & 0.79 whereas the ratio of EBL is ranging from 0.61 to 0.68 over the periods. This shows that the ratio of EBL is inconsistent in comparison to KBL.

4. Investment on government securities to total working fund ratio of KBL is ranging from 0.06 to 0.15 whereas the ratio of EBL is 0.14 to 0.22 over the periods.
5. Total outside assets to total deposits ratio of KBL is ranging from 0.90 to 1.08 whereas the ratio of EBL is 0.97 to 1.03 over the periods. This shows that the ratio of KBL is more than that of EBL in most of the years.
6. Loans & advances to total outside assets ratio of KBL is ranging from 0.82 to 0.99 where as the ratio of EBL are 0.70 to 0.80 over the periods. This shows that the ratio of KBL is higher than that of EBL. Since it invests the large amount in the risky area than that of EBL
7. Investment on government securities to total outside assets ratio of KBL is ranging from 0.07 o 0.17 whereas the ratio of EBL is 0.17 to 0.25 over the periods
8. Total outside assets to total assets ratio of KBL is ranging in between 0.77 & 0.92 whereas the ratio of EBL is in between 0.81 & 0.88 over the periods. The ratio of KBL is higher than that of EBL.

C. Activity Ratio

1. Loan loss provision to total loans & advances ratio of KBL is ranging from 0.01 to 0.02 where as the ratio of EBL is 0.03 to 0.04. KBL has less loan loss provision to total loans & advances than that of EBL.
2. Non-performing loans to total loans & advances ratio of KBL is 0.01 & EBL is ranging in between 0.01 & 0.02.

D. Profitability Ratio

1. Interest income to total income ratio of KBL is ranging in between 0.60 and 0.92 whereas the ratio of EBL is ranging in between 0.58 & 0.84. Ratio of all banks is fluctuating over the periods.

2. Total interest earned to total outside assets ratio of KBL is ranging from 0.07 to 0.09 throughout which is consistent where as the ratio of EBL is ranging in between 0.06 & 0.07 over the periods.
3. Interest expenses to total expenses ratio of KBL is ranging in between 0.61 to 0.82. The ratio of KBL constantly increasing over the periods but in case of EBL the ratio is in decreasing in 2064/65.
4. Total interest income to total working fund ratio of KBL is in between 0.06 and 0.07 where as the ratio of EBL is in between 0.05 & 0.06. This shows that the ratio of all the banks is consistent over the periods.
5. Total interest expenses to total working fund ratio of KBL is in between 0.03 and 0.04 whereas the ratio of EBL is in between 0.02 and 0.03. The ratio of KBL is higher than that of EBL in the last four years.
6. Total income to total expenses ratio of KBL is in between 1.53 and 2.27 whereas the ration of EBL is in between 1.77 and 2.92. The ratio of KBL is in increasing trend throughout the periods but in case of EBL the ratio is fluctuating over the periods.
7. Total income to total working fund ratio of KBL is in between 0.07 and 0.12 and of EBL is in between 0.07 and 0.11. The ratio of KBL is increasing all over the periods. But in case EBL, ratio is ups and downs. The ratio is increasing all over the periods.
8. Return on loans & advances ratio of KBL is in between 0.01 and 0.02 but in case of EBL the ratio is consistent i.e. 0.02 all over the periods except 0.03 in 2065/66. The ratio of KBL also seems consistent in the first four years.
9. Return on total working fund ratio (ROA) of KBL in all the years is 0.01 which is very consistent. EBL has 0.01 in first three years and 0.02 in last two years.
10. Return on equity (ROE) of KBL is in between 0.120 & 0.161, where as the ROE of EBL is in between 0.21 and 0.29. The ROE of KBL is higher than EBL in all the years of study period.

11. Earning per share (EPS) of KBL is in between 16.197 & 22.044; whereas the EPS of EBL is in between 54.23 & 99.96. Here, the EPS of EBL is greater than KBL in all the years.
12. Net interest margin of KBL is in between 0.04 and 0.05 whereas the NIM of EBL is in between 0.05 and 0.06. In case of KBL and EBL, NIM is decreased in last four years.

CHAPTER - V

SUMMARY, CONCLUSION AND RECOMMENDATION

There are two aspects included in this chapter. The first aspect focuses on the summary and the conclusion of the study while the second aspect focuses on the suggestions and recommendations that are useful to improve the performance of Commercial Bank references of KBL and EBL.

5.1 Summary

Economic development is essential for the development of the country. For this, it is required to transform savings into actual investment. Economic development is supported by the financial infrastructure of the country. The financial institutions transfer funds from surplus spending units to deficit units.

The basic task of financial institutions is to mobilize the saving of the community and ensure efficient allocation of the savings to high yielding investment projects to offer attractive and secured returns to different sectors of the economy according to the planned priorities of the country. On the other hand, this process of financial institutions gives rise to the money and other financial assets which therefore have a central place in the development process of the economy. Banking sector plays an important role in the economic development of the country. It provides an effective payment and credit system, which facilitates the channeling of funds from the surplus (savers) units to the deficit units (investors) in the economy.

Investment operation of commercial banks is a very risky one. For this, commercial banks have to pay due consideration while formulating investment

policy. A healthy development of any commercial bank depends upon its investment policy. A good investment policy attracts all the borrowers and the lenders, which helps to increase the volume of quality deposits and investment.

In the most years, banks are the leading buyers of bonds and notes issued by the government to finance public facilities, ranging from hospitals and football stadium to airport and highways. Moreover, bank reserves the principal channel for government economic policy to stabilize the economy. And banks are also the most important sources of short-term working capital needed for the businesses. They have increasingly become active in recent years in making long-terms business loans for new plant and equipments. When businesses and consumers must make payments for the purchase of goods and services, more often they use bank provided cheques, credit or debit cards, or electronic accounts connected to a computer network. It is the bankers, to whom they turn most frequently for advice and counsel when they need financial information and financial planning.

A bank always puts in effort to maximize its profitability. The profit is excess of income over expenses. The major source of income of a bank is interest income from loans, investments and fee based income. As loan and advances dominate the asset side of the balance sheet of any bank; similarly, earnings from such loan and advances occupy a major space in income statement of the bank. However, it is very important to be reminded that most of the bank failures in the world are due to the shrinkage in the value of loan and advances. Hence, loan is known as risky asset and investment operation of commercial banks, is a very risky one. Risk of non-performing loans erodes even existing capital. Considering the importance of lending to the individual banks and also to the society it serves, it is imperative that the bank meticulously plans its credit operations.

The major problem in almost all underdeveloped countries and Nepal as no exception is that of capital formation and proper utilization. In such countries, the commercial banks have to shoulder more responsibilities and acts as development banks, due to the lack of other specialized institutions.

Commercial banks in the developing countries like Nepal have the greatest responsibility towards the economic development of the country. In modern times, since credit or bank money constitutes bulk is of the economy's aggregate money supply it mostly changes the volume of the bank money or credit rather than changes in the total supply of the high-powered money issued by the reserves held by the bank against their deposit liabilities that account for the changes in the aggregated money supply. The main goal of the bank as a commercial organization is to maximize the surplus by the efficient use of its funds and resources. In spite of being a commercial institution, it has a responsibility (obligation) to provide social service oriented contribution for the social economic enlistment of the country by providing specially considered loans and advances towards less privileged sectors.

A bank's marketing starts with a proper relationship with customers either to attract savings or for the loan disbursement. Both the depositors and the creditors are customers of the bank. Bank's offer various products for deposit mobilization and disburse the credit products as per the portfolio management. Customers as per their need purchase different types of product offered in the market. Deposit products offered to the customers are categorized into general products and special products, and credit products can be bifurcated into fund based products and non-fund based products. The fund based products in practice are developed from the credit products generally known as overdraft, working capital loan, Term loan, bills purchase or negotiation, export and import bills, import/trust receipt loan, export credit, loan against fixed deposit receipt, loan against shares, loan against

securities, and loan against bank guarantee and deprived sector loan. The term loan used in practice generally addresses short term loan medium term loan and long term loan to be advanced in various forms such as housing loan, hire purchase loan and bridge financing. The non-fund based product is composed of letter of credit (LC) and bank guarantees with different forms (bid bonds, performance bonds, etc.)

Among the different banking products available in the market, the product with high demand are consumer credit, export and import credit, term loan, Project loan and syndicate loan. All banks and financial institution on the basis of their capital base and liquidity position offer these credits products but none of them so far have been found to have expertise in any one of them for marketing. Relying on any one of the product by portfolio seems more risky. Banks in foreign countries are known to bring out numerous products. As an example, the bank of America has a vast range of banking business serving individuals and small firms and a big share of the loan syndicate market. It means markets are there for some products and it is created for others. Banks in Nepal are weak in locating the existing market and in crating new markets too.

Loan disbursement is a trade of win-win game lenders and borrowers both get benefited out of it. Customers are the ultimate source of income not products. For the analysis of customers several questions need to be answered. This includes questions such as which customer buys the product and how do they use it? Where do customers buy the product, when do customer buy, how do customers choose, why do they preferred that product, how do they respond, and will they buy again. All these data available in the respective files of the customer make the marketing activities quite easier and effective.

Portfolio is the holding of a collection of investment. For some individuals and institutions, it is the entire holdings consisting of both assets and liabilities. An investment held as a part of the portfolio is less risky than the same investment held individually. So, every individuals and institutions should manage the portfolio by which the individuals and institutions get maximum return. The concept of the portfolio comes from "not putting all the eggs in one basket". Portfolio theory evaluates the reduction of non-systematic or diversifiable risks through the selection of securities or other instruments in to a composite holding or efficient portfolio. This efficiency means that a portfolio would offer lower risks or more stable returns lower non-systematic risks. Also, instruments that are inversely related on a return basis reduce the diversifiable risks. The basic theory assumes that returns are independent, investors expectations are homogeneous, and that the normalized probability distributions are stable.

Investment positions are undertaken with the goal of earning some expected rate of return. Investors seek to minimize inefficient deviations from the expected rate of return. Diversification is essential to the creation of an efficient investment because it can reduce the variability of returns around the expected return.

5.2 Conclusions

1. The mean of current ratio of KBL is 1.05, EBL is 1.04 during the study period. Since the ratio is more than one, the banks are able to meet its current obligations. The current ratio is decreasing in the most recent years in all the banks. The mean of cash and bank balance to total deposit ratio of KBL is 0.07, EBL is 0.. The cash and bank balance to total deposit ratio of EBL & KBL is fluctuated in FY 2065/66. The mean of cash and bank balance to current ratio of KBL is 0.05 whereas of EBL is 0.12. Likewise the mean of investment of government securities to current assets ratio of KBL is 0.10, EBL is 0.20. In conclusion, it can be said that the liquidity position of three

banks are satisfactory since the current ratio of both the banks are more than one over the period. The liquidity position of KBL is decreasing. It suggests that the banks are maintaining low liquidity. It will help to increase the overall profit of the bank.

2. The cash and bank balance to total deposit ratio as stated earlier should be more than 5% of total deposit, which is set by NRB. It means the banks could maintain CRR as set by NRB.
3. The mean of investment to total deposit ratio of KBL is 0.16 whereas of EBL is 0.23. The ratio EBL is fluctuating over the periods than that of KBL. The loans and advances to total working fund ratio of KBL is more than EBL. It shows that the KBL has more productive investment. However, it increases the liquidity risk of the bank.
4. The mean of investment on government securities to total working fund ratio of KBL is 0.12 whereas of EBL is 0.19. It shows that the EBL is maintaining its liquidity by increasing its investment in government securities.
5. The mean of total outside assets to total deposits ratio of KBL is 1 & of EBL is 0.98. The ratio of KBL is fluctuating over the periods of than that of EBL. Mean of loans and advances to total outside assets ratio of KBL is 0.89, EBL is 0.76. In this also, the ratios are fluctuating over the periods.
6. The mean of loan loss provision to total loans and advance ratio of KBL is 0.01, EBL is 0.03. It shows EBL has high ratio than that of KBL in all the years. It means KBL have the more quality loans than that of EBL. The means of non-performing loans to total loans and advances ratio of KBL is 0.01, EBL is 0.01.
7. The mean of interest income to total income to total income ratio of KBL is 0.67, EBL is 0.63. It shows that the interest income has the greater portion of total income is KBL than that of EBL. The mean of interest earned to total outside assets ratio of EBL & KBL is 0.07.

8. The mean of interest expenses to total expenses ratio of KBL is 0.72, EBL is 0.67. However, the ratio is increasing in KBL throughout the period whereas in EBL the ratio is decreased in 2064/65.. The mean of total income to total expenses ratio of KBL is 2.11 and of EBL is 2.5 1. The EBL has more ratio than that of KBL
9. The mean of ROA of both the bank is 0.01. It shows that the ratio is consistent over the periods. The mean of ROE of KBL is 0.142 and of EBL is 0.25.. The mean of EPS of KBL is 19.032, EBL is 77.74.
10. The growth rate of deposit for the period of EBL is more than that of KBL in different years. The growth rate of KBL of loans & advances is less than that of EBL in every year. The EBL is increasing the volume of loans & advances. The growth rate of investment and net profit of all banks are highly fluctuating over the periods.
11. Correlations of three banks with the different variables are positive. It means all the variables are positively correlated with the variables used in the research. Trend analyses of all the variables are in increasing throughout the periods.

5.3 Recommendations

Based on the analysis and finding of the study, the following recommendations can be made as suggestions to make the portfolio management practices of KBL, EBL effective and efficient.

1. As the current ratios of all the banks are more than 1:1, it is good as it can meet the short-term obligations. The cash and bank balance to total deposit ratio 5% set by NRB. So, all banks are conscious to maintain its CRR. Investment on government securities to total current assets ratio of KBL is higher than EBL. So the EBL have to increase the volume of investment in the government securities.

2. The loan loss provision to total loans and advances of KBL is less than that of EBL. So, EBL have to maximize in the quality lending. Hence, the loan loss provision will be minimized. NPL of KBL is also lower than the EBL. So, EBL should minimize its NPL since it doesn't indicate well.
3. Both banks have to increase their investment in risk free securities. Similarly, they have to increase their ROA in coming years.

Keeping all these in consideration, KBL & EBL should include their weaknesses by adopting the innovative approach to marketing. In the light of growing competition in the banking sector, the business of the bank should be customer oriented. It should strengthen and activate its marketing function as it is an effective tool to attract and retain the customers. For the purpose, these banks 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. These banks 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.

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