

# CHAPTER ONE

## INTRODUCTION

### 1. Background of Study:-

In the contest of rapid changing environment, Banking plays vital role in the economy of each country whether that may be big or small bank. A bank is a financial institute established for safe guarding the assets of different individuals and uses it to make loans and investments. It is a best advisor on all economics activities to the government. People deposit their savings rather than keeping with them selves to gain additional money or interest. The banker also provides a variety of financial services. The basis of banking business is borrowing from individuals firms and occasionally government i.e. receiving deposits from them with resources and also with the bank's own capital, the banker makes profit by borrowing at one rate interest and lending at a higher rate and by charging commission for services.

Due to bank's multi-disciplinary functions none can define exactly about. In spite some authors have tried to define as "A bank is one who is the ordinary course of his business, services money which he repays by honoring cheques of person from whom or on whose account he receives it."(Backford, 1990:29)

"A bank is a manufacturer of credit and machine for facility exchanges"  
(*white*, 1991:108)

“ Any institution offering deposits subject to withdraw on demand and making loans of Commercial or business nature is Bank.”(Federal U.S.A. Law)

"I believe in the fact the banks are not merely purveyors of money, but also in an important sense manufacturer of money."(*Sayers*, 1967:216)

“A Banker is a dealer in debt in his own and other peoples. The Bankers business is there to take the debt of other people to offer his own in exchange and there by to create money.”(Geoffrey, 1995:417)

Although there are various types of banks according to nature and function but only commercial banks are considered here for this study.

"A commercial bank means bank which deals in exchanging currency, accepting deposits, giving loans and doing commercial transaction."(Commercial Bank act 2031 B.S)

The origin of bank is linked to either Latin word "Bancus" Italian word "Banca" or French word "Banque". All three meaning bench or German word bank meaning joint stock company about the evolution of commercial bank, Bank of Venice setup in 1157 was the first commercial bank

In the context of Nepal, history tells us that in 1994 Nepal's first bank named "Nepal Bank Limited" was established. Similarly in 2013 "Nepal Rastra Bank " in 2024 "Agriculture Development Bank". Then in 2041 B.S. owing to the liberalization & privatization policy adopted by government in 2039 B.S., another landmark was achieved in the history of commercial banking in Nepal with the establishment of Nepal Arab Bank issthe first

joint venture bank and also the introduction of private investment in banking sector. It became a grand success and Banking sector experienced a boon in the history of joint venture banks.

Nepal Investment Bank (2043), Standard Charter Bank (Nepal Grindlays Bank 2043), Himalayan Bank limited (2043), Nepal SBI Bank (2050), Everest Bank Limited (2051), Nepal Bangladesh Bank (2051), Bank of Kathmandu (2051), Celon Bank of Nepal (2053) were some of the prominent banks established as joint venture undertaking.

Commercial banks are being run by bank and financial ordinance 2060, which has replaced the previous commercial bank act 2031. The ordinance has been amended once. According to the ordinance, bank and financial institutions are divided into four groups. Commercial banks are placed in group A. There are many commercial banks operating in Nepal, and many are about to establish. Since this thesis report is based on NABIL Bank Ltd., Kumari Bank Ltd, & Nepal SBI Bank Ltd., information about is necessary and given below:-

## **1.1An introduction about sample bank**

### **1.1.1NABIL Bank Limited:-**

NABIL Bank Limited (Previously Nepal Arab Bank Limited) is the first foreign joint venture bank of Nepal which started operations in July 1984 with technical service assistance with Dubai Bank Limited. NABIL was incorporated with the objective of extending international standard modern banking services to various sectors of the society looking for its objective. NABIL provides a full range of commercial banking services through 19

branches across the country and over 170 reputed correspondent banks all around the globe.

NABIL has emerged as a pioneer in introducing many innovative products and marketing concepts in the domestic sector as customer satisfaction its primary worth of doing business.

Highly qualified and experienced management team manages operation of the bank including day to day operation and risk management. Bank is fully equipped with modern technology, which includes ATMs, Credit Cards, State of art, world–renewed software from Infosys Technologies System, Bangalore, India, Internet banking system and Tele banking system.

Today NABIL Bank is a leader in the financial sector in Nepal with a network that has 19points of representation spread across the nation , complimented by a network of ATMs &now NABIL net &NABIL Tele the case of access of accounts and information for out customers has never been more convents. NABIL is a full service bank providing in local and foreign currency, visa and master card denominated in rupees and dollars, visa electron, debit cards, personal lending products for Auto, Home and personal loans, Trade financing products, Treasury service and corporate financing.

**Table no : 1.1**

**Capital structure of NABIL Bank Ltd. Based on annual report 2064\65**

<b>Particulars</b>	<b>amount in Rs (In '000)</b>	<b>%</b>
Equity capital	2437199	6.56
Total debt	34695560	93.44
Total liabilities	37132759	100

*(Source: Appendix no. 1)*

**Table no : 1.2**

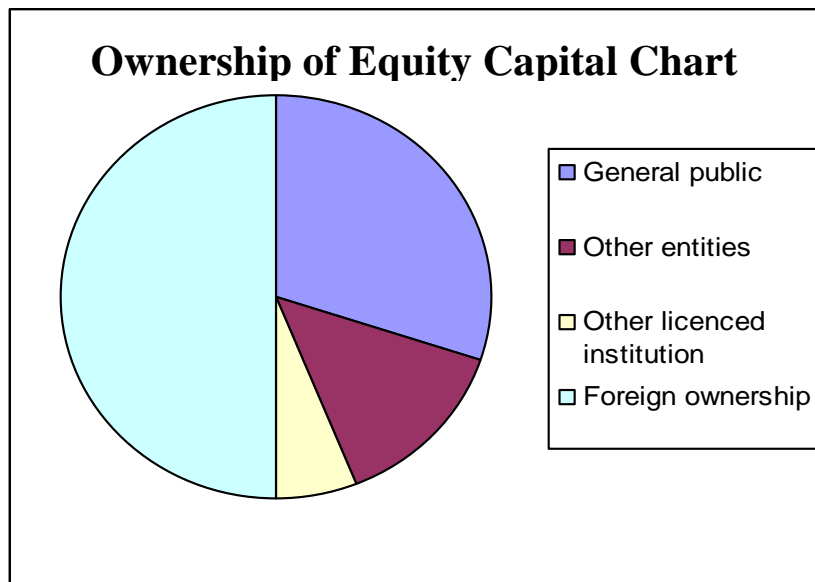
**Ownership of Equity capital of NABIL Bank Limited**

<b>Particulars</b>	<b>share capital in Rs (In '000)</b>	<b>owner's share in %</b>
<u>Domestic ownership</u>		
General public	206765	30%
Other entities	95479	13.86%
Other licensed institution	42365	6.15%
Total domestic ownership	344608	50%
Foreign ownership	344608	50%
Total equity	689216	100%

*(Sources: annual report of NABIL.)*

**Figure no: 1.1.1**

**Graphical Presentation of Ownership of Equity capital of NABIL**



### **1.1.2 KUMARI BANK LIMITED:**

Kumari Bank Ltd. Stepped in the private banking sector in the country as a new entrant since Chaitra 21, 2057 B.S. The Bank was promoted by some of the largest renewed business houses in the country.

KBL, the first national level Bank managed by Nepali management is also the bank with highest capital base. It took the initiative of establishing itself when the country was going through major economic and financial crisis. It stands with a vision to be a world class Nepalese Bank and to be a leading financial institution of the country. Its goal is to create its own niche in the market and get recognition as the most preferred organization among its customers, shareholders, regularity, authorities and all its stakeholders.

At present, The bank is running its operation from its head office situated at Putalisadak, Kathmandu and the branches are in Birgunj, Biratnagar, Pokhara, New road, Birtamode, Itahari etc. The bank was successful to register operating profit in the fast year of it operations which is indeed historical. KBL provides a full range of commercial banking service through its outlets spread across the nation and reputed correspondent banks across the global.

So, for it have been able to associate their customer with banking products like interest banking, mobile banking and auto sweep facilities which has helped them to meet their objectives of adapting modern technologies and coming up with innovative banking products the success of

the achievement relay on their organization values of good team work and high professionalism.

**Table no1.3**

**Capital structure of Kumari Bank Ltd. Based on annual report 2064\65**

Particulars	amount in Rs. (In ‘000)	%
Equity capital	1364885	9.08%
Total debt	13661714	90.92%
Total liabilities	15026599	100%

(Sources: Appendix II)

**Table no1.4**

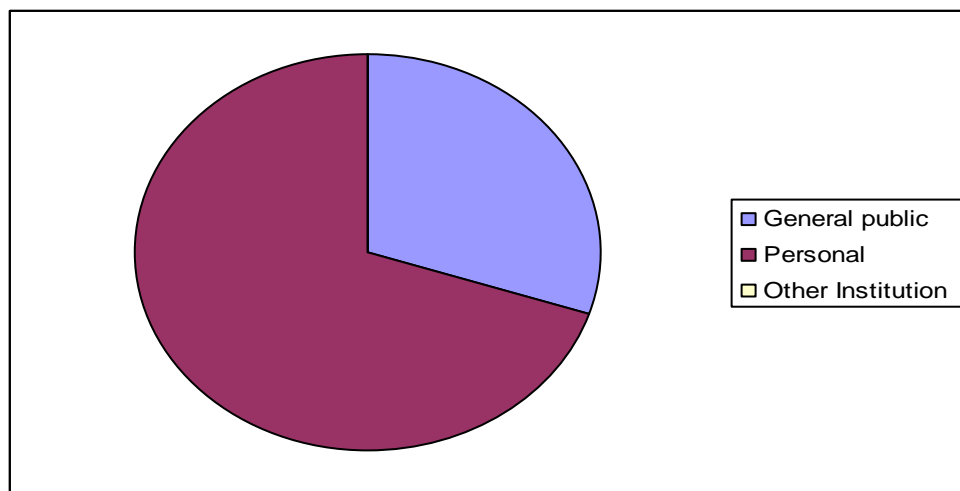
**Ownership of equity capital of Kumari Bank Limited**

Particulars	Share capital in Rs (in ‘000)	Owner’s share in %
<b><u>Domestic ownership</u></b>		
General public	321000	30
Personal	747716	69.88
Other Institution	1284	0.12
Total domestic ownership	1070000	100
Foreign ownership	-	-
<b>Total equity</b>	<b>1070000</b>	<b>100</b>

(Sources : annual report of KBL.)

**Figure no: 1.1.2**

**Graphical Presentation of Ownership Of Equity capital of KBL**



### **1.1.3 NEPAL SBI BANK LIMITED:-**

Nepal SBI Bank limited is one of the leading joint venture Bank. It was established in 2050 B.S. under the ‘Company Act 2021’ and ‘Banijya Bank Act 2031 B.S.’ as a joint undertaking with State Bank of India. The bank started its operation with an authorized capital of 24 crores and paid of capital of 12 crores. Out of which 50% was invested by state bank of India, 15% by employee provident fund (EPF), 5% capital is held by Agricultural Development Bank (ADB) and the rest 30% is from the general public of Nepal through issuing shares.

This bank has been able to secure an outstanding position among the commercial banks. It is able to draw the attraction of many people due to its customer friendly approach. Owing to its experience of international banking transaction round the globe, it has better reputation and goodwill among the commercial bank. Today this bank with 27 branch offices and a team of 249 enthusiastic, dedicated and efficient employees have been able to satisfy its customers with fast, easy and reliable banking services.

The principle activities of the bank during the year were personal & co-operate financial services, international network services, foreign currency exchange dealing etc. Apart from the traditional banking services, the bank has entered into the new era generation next banking by providing ATM services, credit card, safety deposit locker, remittance services letter of credit and many other such services.

The main pillars of support for Nepal SBI Bank Ltd are its customers, shareholders and its employees. It is Bank’s mission to deliver quality



banking and stakeholder satisfaction in the true meaning of the word. Bank fully grasp the ultimate importance of engaging more closely in customer relations at every level, ensuring satisfactory, sufficient profits and ploughing back the fruits of the business successes back to customers, the community, and shareholders.

Nepal SBI Bank's Code of Conduct encapsulates international best practices applicable to Nepali context. The level of commitment of the people to take SBI Bank to greater heights has been a huge catalyst. The team spirit within the organization is something the Bank is proud of.

**Table no1.5**

**Capital structure of Nepal SBI Bank Ltd. Based on annual report  
2064\65**

<b>Particulars</b>	<b>amount in Rs. (In '000)</b>	<b>%</b>
Equity capital	1414645	8.23
Total debt	15772801	91.77
Total liabilities	17187446	100

*(Sources: Appendix III )*

**Table no 1.6**

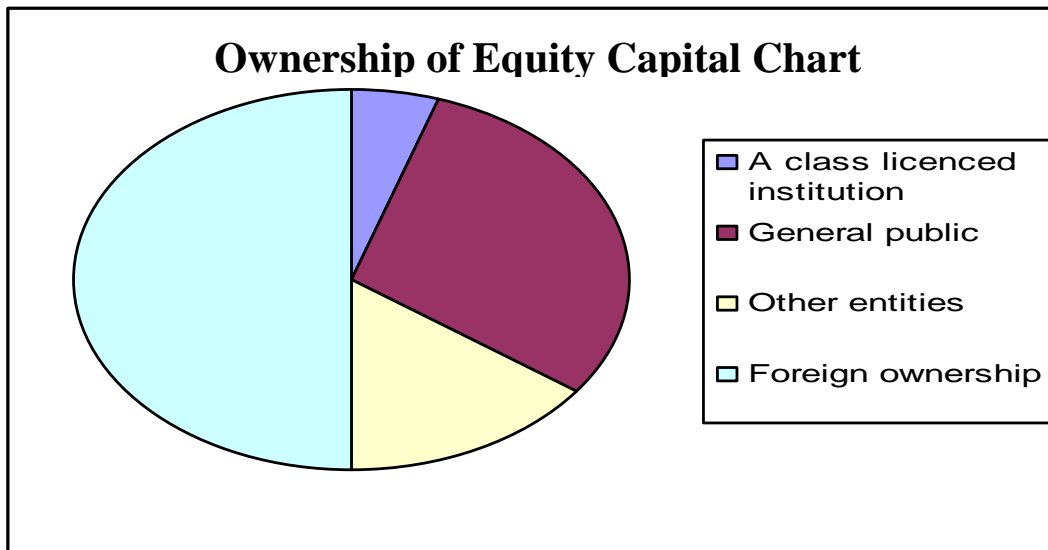
**Ownership of Equity Capital of Nepal SBI Bank Limited**

<b>Particulars</b>	<b>share capital in Rs (In '000)</b>	<b>owner's share in %</b>
<b><u>Domestic Ownership</u></b>		
A class licensed institution	43740	5
General public	262168	29.98
Other entities	131220	15
Total domestic ownership	437128	49.8
Foreign ownership	437400	50.02
<b>Total equity</b>	<b>874528</b>	<b>100</b>

*(Sources : annual report of NSBL.)*

**Figure no: 1.1.3**

**Graphical Presentation of Ownership of Equity capital of NSBL**



**1.2 Focus of the study:-**

Capital is the most crucial factor from beginning of the business organization. In the lack of capital, business organization cannot operate their daily activities properly. Therefore, to ensure the smooth operation of the firm, it must take into account its capital structure.

Capital structure concept holds a major place in the financial management including the banking institutions. Capital structure refers to the proportion of debt & equity capital. A perfect balance between debt and equity is required to ensure the trade-off between risk and return. Since capital structure is the liabilities part, therefore, it is highly riskier & sensitive. Debt equity ratio indicates the extent to which debt financing is used relative to equity financing. Dividing total debt by shareholder's equity, this ratio is calculated. Total debt consists of current liabilities & long-term debt whereas shareholder's equity consists of owner's fund, reserve & surplus retained earning etc.

The proper composition of debt & equity helps to generate high return to the business organization and helps in long-term solvency. Investors invest their funds in ownership securities or debt securities of the organization with the expectation of getting favorable return in the future. In the absence of proper utilization of the capital, it fails to meet their expectation & minimizes the credit worthiness of the organization and leads to fall the market value of the organization. On the other hand, optimum financial structure makes better use of society's fund and thus it increases the total wealth of the society.

### **1.3 Statement of Problem:-**

The two principal source of long-term financing are equity & debt capital. The composition of these two financing is known as financial structure or capital structure. One of the critical of all banking problem in recent years centers on raising & maintaining sufficient capital. A commercial bank has access to their sources of funds: capital, deposits and borrowing. Collection & maintenance of proportion of capital from different sources form the capital structure. Bank capital can't be treated as single & homogenous item. Choices of the form of capital structure & the way of raising it has important implication for bank's profitability because as the debt increases interest payable also increases and it will lesser the shareholder's profit.

#### **1.4 Significance of the Study:-**

The financial institutions holding lenders and owners are most concerned with the firm's long-term financial strengths. To judge the long-term financial position of the firm, capital structure & profitability of the firm are worthy to analyze. Capital structure and profitability would help to indicate and to follow the appropriate mix of debt & owner's equity in financing the firm's assets where profitability analysis would help to indicate the condition of earning from the various resources and to allow the appropriate profitability pattern. A firm having good return & efficient management is supposed to be better & bright in the future. Therefore, to this significance on account, this study on behalf of the firm's capital structure and profitability and its relationship is justified as a specific subject matter.

#### **1.5 Objective of the study:-**

Behind every study there are some objectives and the main objectives I have from this study is to provide brief information about the comparative analysis of capital structure and the overall performance of NABIL Bank Ltd. Kumari Bank Ltd. and Nepal SBI Bank Ltd.

This report has been prepared in order:

- To have precise insight about the capital structure of said bank.
- To find out factors affecting capital structure management decision.
- To analyze capital structure related variables.
- To calculate capital structure ratio.
- To examine long-term solvency of the said Bank.
- To evaluate debt servicing capacity of the above bank.
- To show the trend of composition & capital of the sample bank.
- To find the capital adequacy/sufficiency ratio of the said bank.

## **1.6 Limitation of the Study:-**

This research paper is not total research. This research paper is made as the partial fulfillment of Master Degree of Business Studies. So researches suffering various problems like financial data are not available due to business secrecy, financial problem and time is limited. Therefore, researchers basically suffering from the following limitations:-

- The duration available for the study was very short. For a good research work the time available would not be enough even to collect data.
- This study just analyzes the capital. It excludes other components.
- Many seasonal factors have been ignored in this analysis.
- The study is based on the historical data. So the facts by the study may misguide for the future. It may be inappropriate for the study.
- The study is based on mostly secondary data. Therefore, conclusion drawn may not be fully true in real situation.
- The analysis is based on the limited year. Therefore, it is difficult to analyze the overall performance of the bank.

## **1.7 Organization of the Study:-**

The comparative analysis of capital structure between NABIL Bank Ltd. Kumari Bank Ltd. And Nepal SBI Bank Ltd. has been divided mainly into five chapters which are as follows:-

### **Chapter- i(Introduction)**

This chapter includes background, banks profile and objective of the study, statement of problem, significance of the study and limitation of the study where related subject matters have been included.

## **Chapter- ii (Review of Literature)**

In this chapter, related subject matter and findings have been reviewed, so far as possible. In this study, concept of capital structure etc has been reviewed.

## **Chapter- iii (Research Methodology)**

In this chapter research design and methodology has been discussed. Basically this chapter includes sources of data, data collection techniques, different data analysis tools that financial tools and various ratio analysis etc.,

## **Chapter- iv (Data Presentation And Analysis)**

This chapter deals with the data presentation and analysis on the basis of data received from the related banks. In this chapter various tools mentioned on the research methodology are used to analyze the capital structure of the sampled banks.

## **Chapter- v (Summary, Conclusion and Recommendation)**

The fifth chapter or the last chapter presents the summary of the study, conclusion drawn from the study and recommendation for the future package of plan of action. The exhibits and bibliography are incorporated at the end of the study.

## **CHAPTER - TWO**

### **REVIEW OF LITERATURE**

#### **2.1 Review of literature:-**

This chapter highlights upon the literature that is available in this particular topic. This chapter is divided into two parts: First part deals with the conceptual review & second chapter deals with relating some available literature including books, journals, articles & thesis etc.

The purpose of reviewing the literature is to develop some expertise in one's area to see what new contribution can be made and to receive some ideas for developing research design. Thus, the previous studies can't be ignored because they provide the foundation to the present study.

#### **2.1.1 Conceptual review:**

The term capital has a special meaning in the balance sheet of bank. Capital refers to those funds contributed by the bank's owner, consisting mainly of stocks; reserves & earning that are retained in the bank rather than paid out to the stockholders. Outsider's loan is instruments of in debtness. But these loans are used by bank as a permanent part of capital structure. Capital is a scare source and is much more essential to maintain smooth operation of any firm. The available capital & financial source should be utilized so efficiently that could generate maximum return.

Capital structure is very crucial part of the financial management as the various composition of debt and equity capital may impact differently on risk and rate of return to equity shareholders. The funds required to business

enterprises are raised either through the ownership securities (i.e. equity share & preference share) or creditors share (i.e. debenture or bonds). A business enterprise has to maintain proper mix of both the securities in a manner that the cost & the risk perception to the shareholders are minimized. The mix of different securities is portrayed by the firm's capital structure (Kamal Koirala 1990:105).

Capital structure refers to the mix of long-term sources of funds, such as debt, long-term debt, preference share capital & equity share capital including reserves & surplus (Pandey: 1999: 18). The optimum capital structure may be defined as that capital structure or combination of debt and equity that leads to the maximum value of the firm (Khan and Jain; 1990:487). Capital structure is the permanent financing of the firm, represented primarily by long-term debt, preferred stock and common equity, but excluding all short-term credit. Thus, a firm's capital structure is only a part of its financial structure.

Capital structure theories developed so far for the question of existence of optimal capital structure. Most of the theoretical & empirical debates so far are revolved around the maximization of the value of firm through the judicious composition of its debt & equity fund. At the time of expanding the branches of commercial bank, emphasis was given to the deposit mobilization & credit disbursement. However, the importance of quality credit could not be recognized & the banking sector failed to witness the expected developments. Subsequently, the banking sector faced the problem of bad debts, overdue loans, accrued interest, and accumulation of the non-banking assets and excess liquidity in the banking system. In



addition to these expected happenings new challenges were added to the Nepalese banking sector due to the adverse development in the domestic economy resulting from the deteriorating peace and security situation & continuous persistence of natural calamities inside the country on one hand & the global recession primarily caused by international terrorism on the other. To overcome such credit risk, market risk and operational risk, capital is a must. Viewing the need of capital for commercial banks Nepal Rastra Bank came with the 'Capital Adequacy Framework' to run commercial banks in a risk free environment.

The capital adequacy framework outlines the Nepal Rastra Bank's proposed guidelines of the revised international convergence of capital measurement and capital standard popularly known as Basel 2. Basel 2 is a new international capital standards set by the Basel Committee on Banking Supervision (BCBS). Basel Committee on Banking Supervision's (BCBS'S) recommendations on capital accord are important guiding framework for the regulatory capital requirement to the banking industry all over the world and Nepal is no exception. Now, the BCBS came out with Basel 2 framework which seeks to provide regulatory capital requirements that are more comprehensive and more sensitive to risk. Basel 2 is a major revision of the international standard on Bank's capital adequacy, which requires banks to implement risk management policies that align capital adequacy assessment with underlying credit risk, market risk and operational risk. Basel 2 establishes a more coherent relationship between how supervisors assesses regulatory capital and how they supervise banks, enabling examiners and better evaluate whether banks are holding prudent capital levels compared with their risk profiles. In short, the basic theme of capital adequacy framework based on Basel 2 is that for every kind of assets of bank there

must be some amount of capital back up so that all the credit risk, market risk & operational risk can be avoided.

The capital adequacy framework also emphasizes on capital and optimum capital structure.

### **Assumptions:-**

The following assumptions are made to grasp the elements of the capital structure and the value of the firm or the cost of capital controversy properly (Van Horne; 1985:243)

- firms use only two sources of capital i.e. debt capital and equity capital.
- the total assets of the firm are given. The degree of leverage can be changed by selling debt to repurchase shares or selling shares to retire debt
- the corporate and personal income taxes do not exist. This assumption is relaxed later on.
- the firm has a policy of paying 100% dividends.
- the operating earnings are not expected to grow.
- the business risk is assumed constant and independent of capital structure and financial risk.

In the analysis of capital structure theories, following notations are used:

$V_s$  = market value of ordinary shares \ market value of equity

$V_d$  = market value of debt

$V_f$  = total market value of the firm

$K_d$  = cost of debt

$K_e$  = cost of equity

$K_o$  = overall cost of capital

EBIT = earning before interest and taxes or NOI

### **2.1.2 Theories of capital structure:**

Several theories have been developed under the relevancy of capital structure to the value of firm and cost of capital. Net income approach and traditional approach argued capital structure as relevant matter and net operating approach and MM approach argued capital structure as irrelevant matter. They are:

- Net Income Approach (NIA)
- Net Operating Income (NOI) approach
- Traditional approach
- Modigliani-Miller approach(MM)

#### **❖ The Net Income Approach:-**

The net income approach is also known as relevant theory of capital structure, as the capital structure decision is relevant to the valuation of the firm suggested by David Durand. This approach contends that the value of a firm can be maximized by the proportion of debt minimize in the capital structure and minimize the overall cost of capital. The crucial assumptions of this approach are as below (Pandey, 1999: 26).

#### **Assumptions of NI approach:-**

(a) The debt capitalization rate is less than the equity-capitalization rate or cost of equity ( $K_d < K_e$ ).

(b) The use of debts doesn't change the risk perception of investors, as a result, the equity- capitalization rate ( $K_e$ ), and the debt-capitalization rate ( $K_d$ ), remains constant with changes in leverage.

(c) The corporate income taxes do not exist.

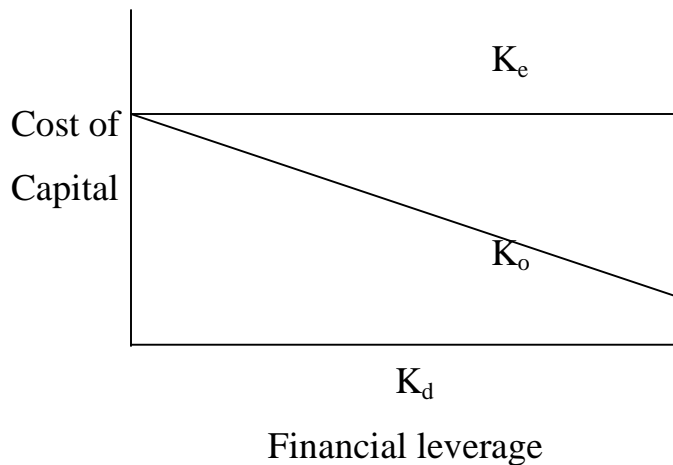
The overall cost of capital ( $K_o$ ) can be measured as:

$$K_o = \text{NOI} / V_f \quad \text{or, } K_o = \text{EBIT} / V_f$$

$$\text{Or, } K_o = K_e - (K_e - K_d) V_d / V_f$$

**Figure no : 2.1**

**The effects of leverage on the cost of capital under NI approach**



Under NI approach,  $K_e$  and  $K_d$  are assumed not to change with leverage. When the proportion of debt is increased in the capital structure, it causes overall cost of capital to decrease and approach the cost of debt. Thus, the firm will have the maximum value and the lowest cost of capital when it is all most debt-financed, under the NI approach.

❖ **The Net Operating Income Approach:-**

Net operating income approach is an irrelevant theory of capital structure. This approach is also known as modern theory or an independent hypothesis of capital structure which is also propounded by David Durand.

This theory assumes that the capital structure (proportion of debt and equity) is irrelevant to the value of firm and the overall cost of capital . Under this approach, net operating income is capitalized at an overall capitalization rate to obtain the total market value of the firm. The market value of debt ,then, is deducted from the total market value to obtain the market value of the stock.

The market value of the firm is determined as:

$$V_f = V_d + V_s$$

$$\text{Or, } V_f = \text{EBIT}/K_o$$

Where,  $K_o$  is the overall capitalization rate depends on the business risk of the firm. It is independent of financial mix. If NOI and  $K_o$  are independent of financial mix,  $V$  will be a constant and independent of capital structure changes. The critical assumptions of NOI approach are ( Pandey; 1999: 31)

Assumptions of NOI approach:

- The market capitalizes the value of the firm as a whole. Thus, the split between debt and equity is not important.
- The market uses an overall capitalization rate ( $K_o$ ) to capitalize the net operating income.  $K_o$  depends upon risk.
- If the business risk is assumed to remain unchanged,  $K_o$  is a constant.
- The use of less costly debt funds increases the risk of shareholders. This causes the equity-capitalization rate to increase. Thus, the advantage of debt is offset exactly by the increase in the equity capitalization rate ( $K_e$ ).

- $K_d$  is a constant.

The corporate income taxes do not exist.

The market value of equity can be determined as:

$$V_s = V_f - V_d$$

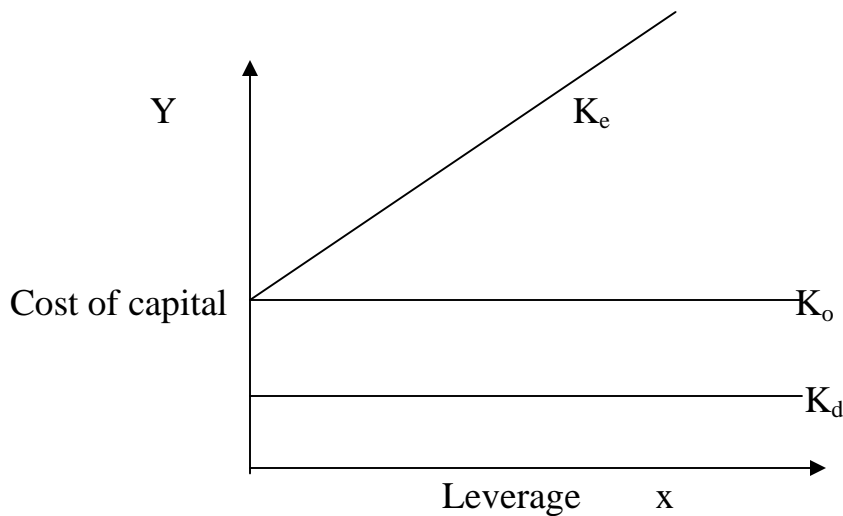
the cost of equity can be defined as follows:

$$K_e = K_o + (K_o + K_d) V_d / V_s$$

The equation indicates that  $K_e$  increases with leverage continuously, if  $K_o$  and  $K_d$  are constant

**Figure no: 2.2**

**The effects of leverage on the cost of capital under NOI approach**



As the average cost of capital,  $K_o$ , is constant this approach implies that there is not any unique optimum capital structure. It means, every capital structure is optimum, as the cost of capital is the same at all capital structure.

### ❖ Traditional Approach:-

This approach assumes the capital structure as relevant matter for the value and cost of capital of the firm. The traditional view (Solomon; 1969: 139), which is also known as an intermediate approach is a compromise approach between the net income approach and the net operating income approach. This approach contends that overall cost of capital of the firm can be minimized by judicious mix of debt and equity capital. This view clearly implicates that the cost of capital decreases within the reasonable limit of debt and the increase with leverage. Thus, an optimum capital structure exists and it occurs when the cost of capital is minimum or the value of the firm is maximum. This theory carries the simple implication that the cost of debt plus the cost of equity together on a weighted basis, will be less than the cost of equity, which existed on equity before debt financing.

According to the traditional position, the manner in which the overall cost of capital reacts to changes in capital structure can be divided into three stages (Solomon; 1969: 139).

#### **First Stage: Increasing Value**

The first stage begins with the initiation of debt in the total capital. In the beginning, the cost of equity ( $K_e$ ) remains constant or rises with debt and it does not increase fast enough to offset the advantage of low-cost debt. Here, the cost of debt,  $K_d$ , remains constant or rises negligibly. Thus, the value of the firm, ( $V_f$ ), increases and the overall cost of capital declines with increasing leverage.

Under the assumption that  $K_e$  remains constant within the acceptable limit of debt, the value of the firm will be:

$$V_f = V_s + V_d$$

Thus, as long as  $K_e$  and  $K_d$  are constant the value of the firm,  $V_f$ , increases at a constant rate.  $(K_e - K_d)/K_e$ , as the amount of debt increases.

$$K_o = X/V_f \cdot K_e - (K_e - K_d)V_d/V_f$$

This implies that with  $K_e > K_d$ , the average cost of capital will decline with leverage.

### **Second Stage: Optimum Value**

Once the firm has reached the certain degree of leverage, increase in leverage in have a negligible effect on the value or the cost of capital of the firm. This is so because the increase in the cost of equity due to the added financial risk exactly offsets the advantage of low cost debt. Thus, within that range or at the specific point, the value of the firm will be maximum or the cost of capital will be minimum.

### **Third Stage: Declining Value**

Beyond the acceptable limit of leverage, the value of the firm decreased with leverage or the cost of the capital increases with leverage. This occurs because investors perceive a high degree of financial risk and demand a higher equity-capitalization rate, which offers the advantage of low-cost debt.



The overall effect of above three stages is to imply that the cost of capital is a function of leverage. At first it declines with leverage and after entering a minimum level it starts rising. The relation between cost of capital and leverage is graphically shown in figure below, where the overall cost of capital curve,  $K_o$ , is saucer-shaped with a horizontal range. It indicates that there is a range of capital structures in which the cost of capital is minimized.  $K_e$  is assumed to increase slowly at first and then at a faster rate.

#### ❖ **Modigliani-Miller Approach (without tax) :-**

In 1958, two prominent financial researchers, Franco Modigliani and Morton Miller have been developed this theory. MM theory asserts that capital structure decision is irrelevant and there is no level of optimum capital structure. MM theory states that, in the absence of taxes the value and overall cost of capital is the expected net operating income divided by the total market value of the firm and it is equal to the capitalization rate of a pure equity stream of its risk class. In their 1958 article (Pandey:1999: 33), they provide analytical sound and logically consistent behavioural justification in favour of their hypothesis and reject any other capital structure theory as incorrect.

#### **Assumptions of MM approach:**

The MM approach can be best explained in terms of their propositions I and II. Their propositions based on certain assumptions, particularly related to the behavior of investors and capital market, the actions of the firm and the tax environment, can be described as (Pandey; 1999: 34)

- Firms can be grouped into homogenous risk classes. It is generally implied that firms within same industry constitute a homogenous class.
- Securities are traded in the perfect capital market situation. This specifically means that: (a) investors are free to buy and sell securities (b) no restriction as the firms do and (c) they behave rationally and transaction costs do not exist.
- No corporate income taxes exist.
- The risk of investors is defined in terms of the variability of the net operating income.
- Firms distribute all net earnings to the shareholders, i.e. 100% payout.

### **Proposition I**

With given assumptions, MM argue that for the firms in the same risk class, the total market value is independent of the debt-equity mix and is given by capitalizing the expected net operating income by the rate appropriate to that risk class (Pandey; 1999: 34).

Proposition I can be defined as  $V_f = V_s + V_d = X/K_o = NOI/K_o$

Where,

$V_f$  = the market value of the firm

$V_s$  = the market value of the firm's ordinary equity

$V_d$  = the market value of debt

$X$  = the expected net operating income on the assets of the firm

$K_o$  = the capitalization rate appropriate to the risk class of the firm

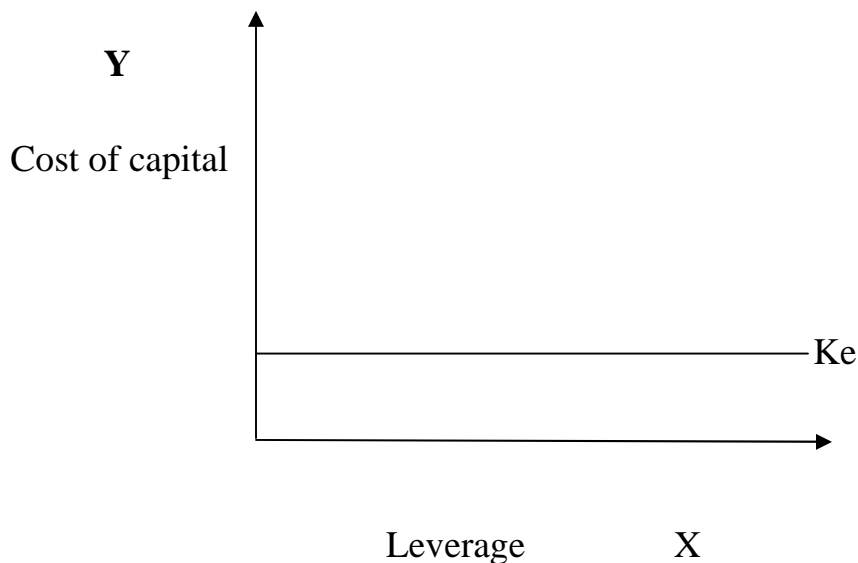
The case can be started in terms of the firm's average cost of capital.

If  $K_d$  and  $K_e$  are defined as the expected return on the firm's debt and equity respectively, then, expected net operating income is:

$$X = K_o V_f = k_e V_S + K_d V_d$$

Since MM conclude that the total market value of the firm is unaffected by the debt equity mix, it follows that the cost of capital is completely independent of its capital structure and is equal to the capitalization rate. The cost of capital function, as hypothesized by MM is presented in the figure.

**Figure no: 2.3**  
**The cost of capital under MM hypothesis proposition I**



Thus, two firms identical in all respects except to the capital structure have the same value and cost of capital. In this case, arbitrage will take place

to enable investors to engage in personal leverage as against the corporate leverage to restore equilibrium in the market (Pandey, 1999: 37)

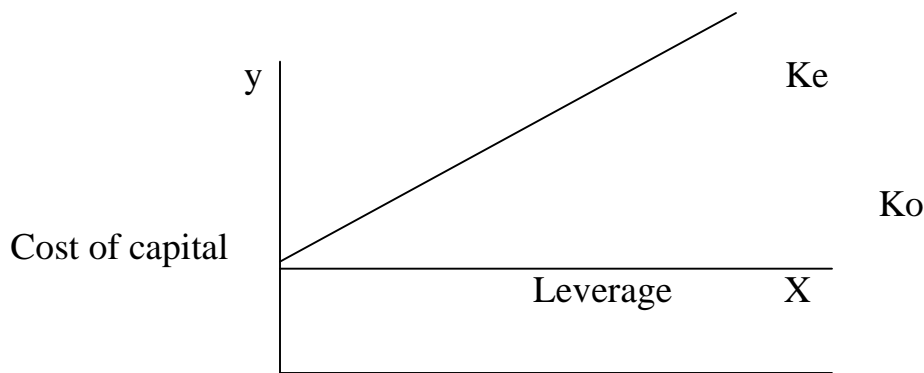
**Proposition II**

MM’s proposition II, which defines the cost of equity, follows the proposition I. The expected yield on equity can be defined as:

$$K_e = K_o + (K_o - K_d) V_d / V_s$$

The MM proposition could be valid, if  $K_d$  remains constant for any degree of leverage. But in practice  $K_d$  increases with leverage beyond the certain reasonable level of Debt. However, MM maintains that even if  $K_d$  is increasing,  $K_o$  will remain constant. They argue when  $K_d$  will increase at a decreasing rate may even turn down eventually. This is shown in figure

**Figure no: 2.4**  
**The cost of Equity under MM hypothesis proposition II**



**2.2 Review from journals and Articles:-**

Weston’s study (Weston; 1963:107), in “A test of cost of capital proposition,” made some important-improvement in the cost of capital

modes. He included firm size and growth as additional explanatory in his model.

He found that the regression co-efficient of leverage to be positive and significant, when dol. However, when the multiple regressions were run, he found that the correlation coefficient is significant and the regression co-efficient of leverage is negative and significant when the influence of growth is isolated leverage is found to be negative correlation with the cost of capital.

He concluded that the apparent lack of influence of leverage on the overall cost of capital observed by MM was due to the negative correlation of leverage with earning growth. Weston also listed MM preposition II.

Sharma and Rao (Sharma and Rao; 1969, 77) conducted the test of MM hypothesis on the influence of debt on the value of a firm to a non-regulated industry. They argued that estimate of cost of capital arrived at through this model will be accurate only when their hypothesis on debt and dividends are correct, this is an essential condition for the employment of this model. For the study purpose, they used samples of 30 engineering equation for three cross-section year: 1962, 1964 and 1965. Calculations of variables were done in exactly the same ways that done by MM with two exceptions. They experimented with total assets and sales for deflecting the variables and the results were meaningful when fixed of total assets were used as the deflector. They argued that when the growth rate of fixed assets was used as the growth variable, the results were somewhat inconsistent with the economic reasoning. They included that debt has non-tax advantage also. Thus, this paper support that the investors prefer corporate to personal

leverage and therefore, the value of a firm rises up to a leverage rate consider prudent.

Haim Bahadur Sharma (Sharma; 1968: 95) conducted a study “The capital structure and the cost of capital”. In this paper, the firm’s capital structure was examined in terms of two parameters: the expected rate of return on the firm’s capital structure and the efficient opportunity curve of yield versus risk was presented, and the range of efficient capital structure of the firm was derived.

The capital structure theorem was formulated; stating that the firm’s cost of capital is constant along the range of efficient capital structure and rises at the inefficient range. Since, the range of efficient capital structure of interest rates, it followed that the shape of the cost of capital curve is determined by the interest rate and if it is constant, any capital structure is efficient and that the cost of capital is also constant.

Wipper (Wipper; 1990:61) conducted a study to test the empirical relationship between cost of capital and leverage. He tried to eliminate the principle problem of study on the leverage and attempted to offer what are hoped to be more fruitful alternatives in determining the relationship between leverage and cost of capital. He argued that the leverage either the ratio of debt to equity at book values, both of these measures contains important conceptual basis. He therefore used different measures of leverage, viz,  $I/E=25$  where, I is the current level of fixed charges, E is the most recent year cash flow operating income determined from a logarithmic regression of income on time over ten years period, 25 is equal to two standard error around the regression line. He has assumed in the past

investigation that homogeneity of business risk could be achieved by comparing firm in the same industry classification.

Rao and Litznberges (Rao and Litznberges; 1970:82) conducted a study on effect of capital structure in the cost of capital in less developed and less efficient capital market (India) and in a highly developed and efficient capital market (United State). They used 28 Indian utilities and 77 American utilities. They conducted the study for five cross-section years; 1962-1966. They found that the results for the American utilities are constant to the MM proposition that except for the advantages of debt financing, the cost of capital is independent of capital structure and the result also supported that the MM hypothesis that investors are indifferent for the firm's dividend policy. In case of Indian utilities, the results are inconsistent to the MM approach and support the traditional belief, the judicious use of financial leverage will lower than the firm's cost of capital and investors have a preference for current dividends. In conclusions, they contended that the MM approach after allowing for the tax advantage of debt, the firm's cost of capital is independent of capital structure does not appear to be applicable in the case of a developing economy.

### **2.3 Thesis Review:-**

Keshar Jung Baral (1996) had submitted a thesis on the topic of "Capital structure and cost of capital in public sector enterprises of Nepal". The main objective of that study is to analyze the capital structure and cost of capital in public sector enterprises of Nepal. That study reached to the conclusion that performance of public enterprises are very poor and they are not adding the wealth of the society but diluting it, and hindering the

development of the country. Further, the huge amounts of adjusted losses of manufacturing and trading enterprises is quite below its cost of capital and overall cost of capital in almost fiscal years of the study period. Thus, it can be concluded that capital structure of enterprises in public sector in Nepal more or less is the outcome of the deliberate decision of Government but not a product of market and public enterprises structures.

Youba Nath Pant (1996) had submitted a thesis on the topic of “A study on capital structure and assets structure of NIDC”. The main objective of that study is to analyze capital structure and assets structure of NIDC finds that debt equity ratio and the total debt to equity ratio are very higher that leads the corporate risk. So, it should maintain the appropriate ratio of debt equity and total debt to equity by increasing share capital and decreasing the borrowing. Similarly, the total expenditure trend is higher than the total income trend. This is very dangerous trend to any business. So, the corporation should pay the attention to maintain the expenditure of the corporation by reducing bonus and other office expenses. He suggests the corporation maintains its liquidity ratio and investment, the total income will occur in increasing trend.

Ganesh Prasad Neupane (1997) had conducted a thesis on “A study on the assets and capital structure of Nepal Bank Limited”. The study was made with the objective to analyze the assets and capital structure of Nepal Bank Limited finds that the amount of other assets is more than 3.5 times than the amount of net worth. It indicates that not only all the amount of net worth is used in unproductive assets but also other liabilities are used in fixed assets as land, furniture, stationery at hand. So, the total income of the bank could not increase along with the increasing rate of total liabilities.



Ramesh Raj Aryal (2001) had submitted a thesis study on “An evaluation of capital structure of Bottlers Nepal Limited”. Objective of that study was to evaluate the capital structure of Bottlers Nepal Limited. Conclusion of that study was; all the calculations show the bad performance of the company due to the inefficient capital structure management. The company is regarded as highly geared up capital structured company. Thus, to design suitable pattern of capita structure for the company, the management must bring about a satisfactory compromising among these conflicting factors of cost, risk, control and timing. He recommended that the company to shift debt capital to equity capital when the company have high earning per share.

Deepak Khanal (2002) had presented his thesis on the topic of “Capital structure management of industrial public enterprises”. Main objective of that study was to analyze the capital structure of industrial public enterprises. It was found that capital investment and earning were not co-related and most of public enterprises in loss position. Debt equity ratio was not satisfactory, financial performance of these companies were not good, so he suggested that the management should reduced government subsidy and donation. They should improve their performance efficiency.

Rima Devi Shrestha (2003) had conducted a study on the topic of “Focus on capital structure (selected and listed companies)”. Her objective of that study was to analyze the capital structure of selected and listed companies. She used data from 19 companies and study had covered different sectors like manufacturing finance, utility service and other allied area. She had found that the most of these companies have debt capital relatively very higher than equity capital. Consequently, most of them are

operating at losses to the extent that payment of interest on loan has serious issues.

Most of these losses are after charging interest on loan. She has suggested that the government has to consider public enterprises is that of evaluating the relationship between use of debt and its impact on overall earning of public enterprises. So, government should be sure in knowing how using debt capital will minimize return. It should need to develop a suitable capital structure guideline to make public enterprises aware of the responsibility to repay the debt schedules. The other thing, which needs to be made publicity transparent that government money is not a lost less, found. Government has to analyze cost and risk return trade off. Thus, capital structure needs to be made more determinate by realistic analysis of cost.

R. L. Shrestha (2004) had conducted a thesis on the topic of “Capital adequacy of bank in Nepalese context”. His main objective is to study the capital adequacy of bank. It has suggested that bank should deal in highly risk transaction to maintain strong capital base.

However, the capital base should neither be too much leading to inefficient allocation of scarce resources not too weak as to expose to extreme risk. The study accepts that the operations of bank and the degree of risk associated with are subject to change country-wise, bank-wise and product-wise. Henceforth, the study suggests preparing standard capital adequacy ratios for each individual bank keeping in mind the various relevant factors.

Sarad Dungal (2007) had conducted a study on the topic of " Analysis of capital structure of Koshi Metal Crafts". His objective of the study was to examine the proportion of equity capital and debt capital for the balanced capital and debt capital for the balanced capital structure and to maximize the shareholder's wealth. And to analyze the relationship among the elements of the capital structure and characteristics.

Deepa Adhikari (2007) had presented her thesis on the topic of " A comparative study of capital structure management of Joint venture banks in Nepal". She presented this thesis with the main objective to provide the proper guidelines to the potential investors. And the other objective of this study are to evaluate the position of capital structure management and relationship between total debt and total equity of the three joint venture banks.

Guna Raj Dhakal(2008) had conducted a thesis on "comparative evaluation of capital structure between Dabur Nepal & Uniliver company". Main objective of this thesis is to anticipate the aspirations of the customers and consumers and to respond creatively and comparatively with balanced products and services which raise the quality products.

From the review of the studies conducted in different companies, it is transparent that the relationship between capital structure and cost of capital is almost non-existence. Thus, this study is conducted to analyze the capital structure of related banks (NABIL Bank, Kumari Bank and Nepal SBI Bank) with affecting that it will useful information for policy maker and the implementation of suggested findings.

# **CAPTER THREE**

## **RESEARCH METHODOLOGY**

### **3.1 Research Design:**

Research design is a plan structure & strategy of investigation conceived so as to obtain answers to questions and to control variance. The analysis of this study based on certain research design keeping in mind on the objectives of the study. Generally, research design means definite procedure and techniques which guides in studying profound ways of research viability. The main objective of the study is to analyze the capital structure of listed commercial bank in Nepal i.e. on a case study of NABIL Bank Ltd, Kumari Bank Ltd & Nepal SBI Bank Ltd. It emphasizes on descriptive and analytical study of the collected data from profit & loss account and balance sheet (i.e. financial statement) over a period of time as well as personal & telephone interviews. Analysis with different statistical & financial tools has been conducted to find out the necessary result also. Research design presents a series of guide posts to enable the researchers to progress in right direction in order to achieve the goals.

### **3.2 Population and sample:-**

The term "Population" used in statistics denotes the aggregate form which the sample is to be taken and the term "Sample" is that part of the population which we select for the purpose of investigation. Population refers not only to the people but, the totality of all observation that are selected for study. Population is also known as Universe. Sample refers to choose and part of population.

Here all the commercial banks are taken as Population and the number of sample are just three. This research report is based on comparative analysis of:-

a) NABIL Bank Limited

b) Kumari Bank Limited

c) Nepal SBI Bank Limited

### **3.3 Sources of data:**

The main sources of data are secondary extracted from the annual report published by banks & publication of NRB. Balance sheet and profit and loss account of last six years are taken for the secondary means. At times of necessity the primary sources of information are collected through discussion and enquiries made from concerned bank.

### **3.4 Methods of analysis and presentation of data:-**

For the collection of data several places have been visited. In this processes of data collection I have visited library of Post Graduate College, BRT, branch of Kumari Bank, NABIL Bank and SBI Bank.

The data collected for this analysis are mostly secondary data provided by the banks for different fiscal year's Income Statement, Balance Sheet, P/L A/c and Annual Reports are taken from secondary data.

### **3.5 Tools of Analysis:-**

Capital structure ratio and some other major ratio are used in this study. The capital structure ratio is defined as financial ratios which throw light on the long-term solvency of a firm as reflected in its ability to assure

the long-term creditors with regard to periodic payment of interest during the period of the loan and repayment of principal of maturity.

The major ratios used in this research are:

- a) Leverage
  - i. Degree of operating leverage
  - ii. Degree of financial leverage
  - iii. Degree of combined leverage
- b) Capital structure/ leverage/ solvency ratio
  - i. Debt equity ratio
  - ii. Debt to assets ratio
  - iii. Interest coverage/ time interest earned/ debt service ratio/ debt competency ratio
  - iv. Capital Sufficiency Ratio/ Capital Adequacy Ratio

# **CHAPTER-FOUR**

## **PRESENTATION AND ANALYSIS OF DATA**

### **4.1 INTRODUCTION:**

The major objectives of this study are to analyze the comparative case study of three commercial banks namely NABIL, Kumari and Nepal SBI Bank Limited respectively. This chapter has been prepared to present, analyze and interpret the results systematically. In the course of analysis, various financial and have been used. A single promoter can't judge the efficiency and effectiveness of the performance of the relevant banks so different parameters are used. To evaluate the capital structure of related banks various ratios, trend analysis are used.

The firm should maintain a sound capital structure to run its business operation in this competitive world. Both excessive as well as inadequate capital positions are unhealthy from the firm's point of view. So an enlightened management should therefore maintain right capital structure to meet its objective.

The data used for the analysis are Profit and Loss Account, Balance Sheet, ownership's equity, deposits, main index, etc. These data are based on annual report. Descriptive analysis is used to analyze the sources of capital. Other tools are used for analysis are the tools of leverage as DOL, DFL and DCL. Tools concerning ratio analysis are also calculated for checking long term solvency.

## 4.2 Descriptive analysis of Ratio:-

This section of the study explores the capital structure with respect to the capital, reserves, deposits, current liability and borrowing. The table below shows the paid-up capital, Reserves, Borrowing and deposits of above mentioned banks for the year 2064/65B.S.

**Table no: -4.1**  
**Paid up capital, Reserves, Borrowings & Deposits of NABIL, KBL & NSBIL for the year 2064/65**

(In 000)

<b>Banks</b>	<b>Paid up</b>	<b>Reserves</b>	<b>Borrowing</b>	<b>Deposits</b>
NABIL	689216	1747983	1360000	31915047
KBL	1070000	294885	100000	12774281
NSBIL	874528	540117	1627480	13715395

(Source:-Appendix no. I, II&III)

### 1. Share capital trend:-

Share capital is the fully paid up or issued capital of the concerned bank. The table that follows the deposits of the share capital trend of the commercial banks for six consecutive fiscal year.

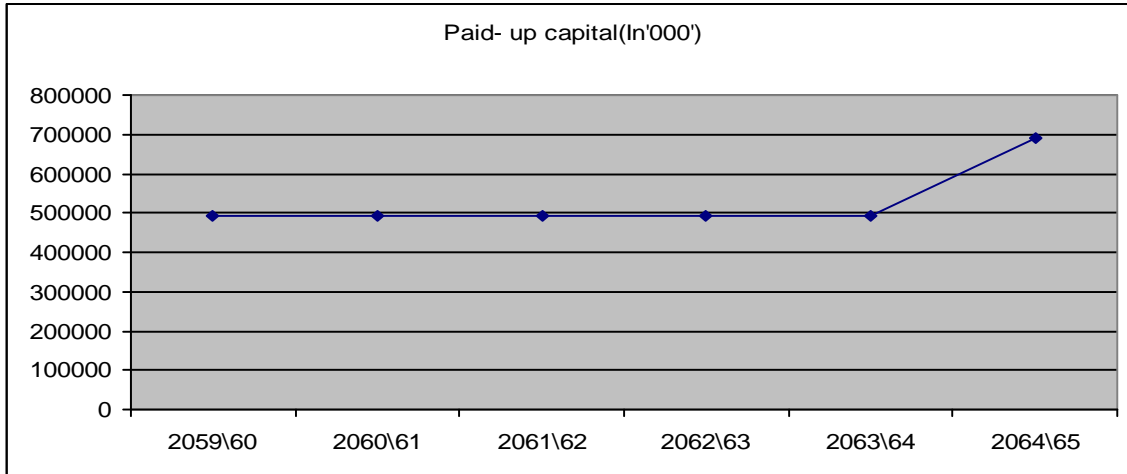
**Table 4.2**  
**Share capital trend of NABIL**

<b>Year</b>	<b>Paid- up capital(In'000')</b>	<b>Index trend</b>	<b>Yearly change</b>
2059\60	491654	100%	0
2060\61	491654	100%	0
2061\62	491654	100%	0
2062\63	491654	100%	0
2063\64	491654	100%	0
2064\65	689216	140.18%	40.18%

(Source:-Appendix no. I)



**Figure no 4.1**  
**Share capital trend of NABIL**

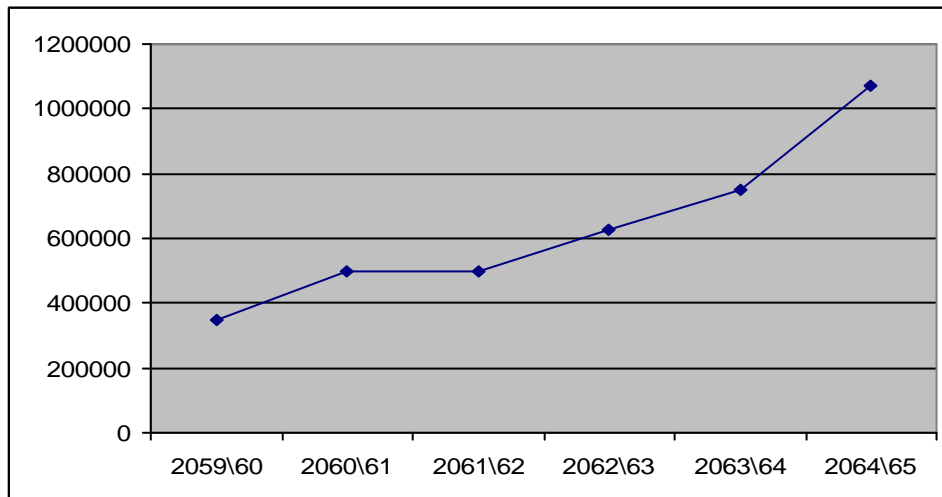


**Table no: 4.3**  
**Share capital trend of KBL**

Year	Paid- up capital(In'000')	Index trend	Yearly change
2059\60	350000	100%	0
2060\61	500000	142.86	42.86%
2061\62	500000	142.86%	0
2062\63	625000	178.57%	25%
2063\64	750000	214.29%	20%
2064\65	1070000	305.71%	42.66%

(Source:-Appendix no. II)

**Figure no: 4.2**  
**Share capital trend of KBL**



**Table no: 4.4**

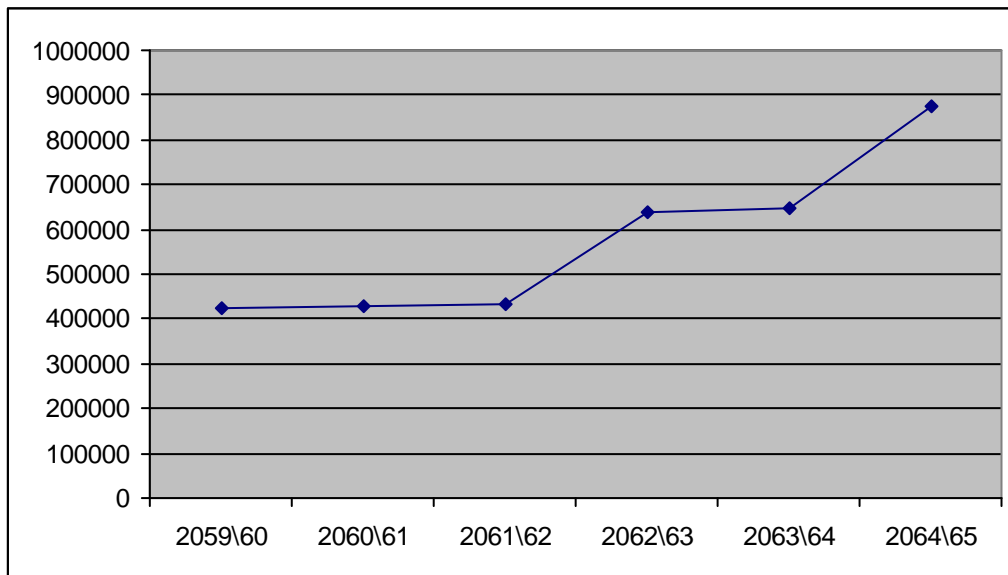
**Share capital trend of NSBL**

Year	Paid-up capital(In'000')	Index trend	Yearly change
2059\60	425157	100%	-
2060\61	426876	100.4%	0.4%
2061\62	431866	101.57%	1.13%
2062\63	640236	150.59%	48.25%
2063\64	647798	152.37%	1.18%
2064\65	874528	205.70%	35%

(Source: Appendix no. III)

**Figure no: 4.3**

**Share capital trend of NSBL**



**2. Reserves and surplus trend:-**

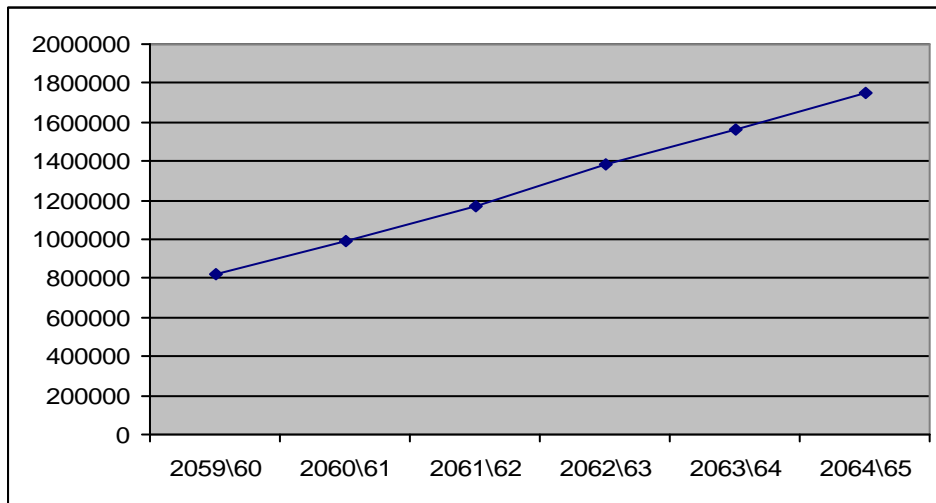
It refers to the total capital of the concerned bank and includes general reserve, share premium and other reserves. The following table shows the reserve and surplus of the mentioned bank for 6 consecutive years.

**Table no: 4.5**  
**R/S Trend of NABIL**

Year	R\S(In'000')	Index trend	Yearly change
2059\60	822533	100%	-
2060\61	990028	120.36%	20.36%
2061\62	1165984	141.76%	17.78%
2062\63	1383340	168.18%	18.64%
2063\64	1565395	190.31.29%	13.16%
2064\65	1747983	212.51%	11.67%

(Source: Appendix no. I)

**Figure no: 4.4**  
**R/S Trend of NABIL**

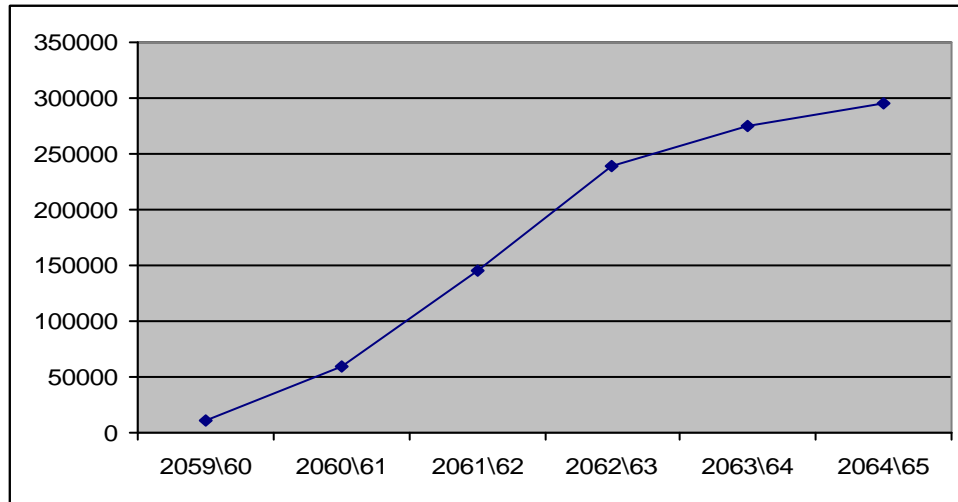


**Table no: 4.6**  
**R/S Trend of KBL**

Year	R\S(In'000')	Index trend	Yearly change
2059\60	11033	100%	441.28%
2060\61	59719	541.28%	441.28%
2061\62	145442	1318.25%	143.54%
2062\63	238851	2164.88%	64.22%
2063\64	275630	2498.23%	15.40%
2064\65	294885	2672.76%	6.99%

(Source: Appendix no. II)

**Figure no: 4.5**  
**R/S Trend of KBL**

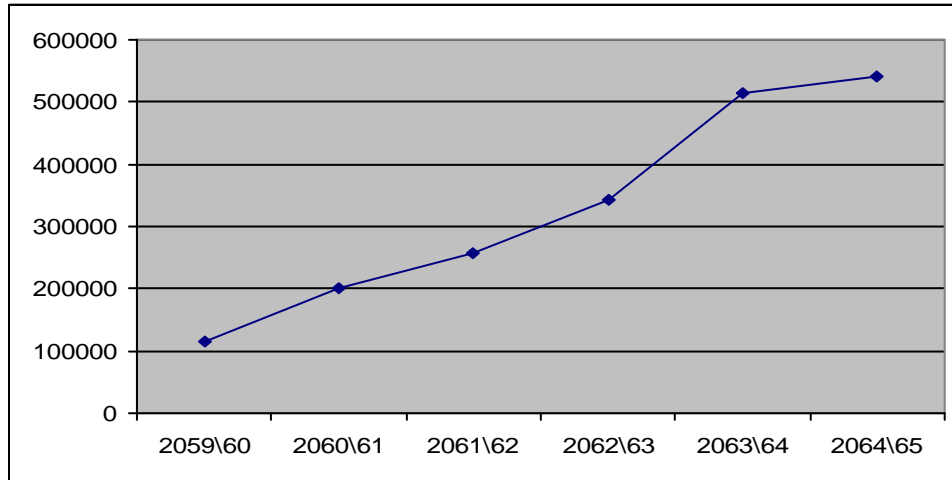


**Table no: 4.7**  
**R/S Trend of NSBL**

Year	R\S(In'000')	Index trend	Yearly change
2059\60	114695	100%	-
2060\61	199761	138.06%	38.06%
2061\62	257147	177.72%	28.73%
2062\63	342138	236.45%	33.05%
2063\64	515492	356.26%	50.66%
2064\65	540117	470.92%	32.18%

(Source: Appendix no .III)

**Figure no: 4.6**  
**R/S Trend of NSBL**



### 3. Borrowing Trend:-

It is an amount taken by the commercial bank from different lenders. It includes both the local and foreign borrowing. Borrowing trend of the commercial bank is shown in the table placed below:

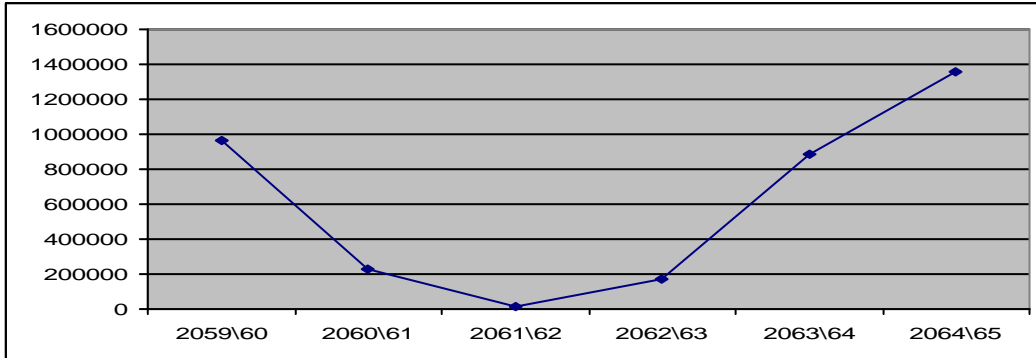
**Table no: 4.8**

#### **Borrowing Trend of NABIL**

Year	Borrowing(In'000')	Index trend	Yearly change
2059\60	961461	100%	-
2060\61	229660	23.89%	-76.11%
2061\62	17063	101.7%	-92.59%
2062\63	173202	18.01%	9.18%
2063\64	882573	91.79%	4.10%
2064\65	1360000	141.45%	54.10%

(Source: Appendix no. I)

**Figure no: 4.7**  
**Borrowing Trend of NABIL**

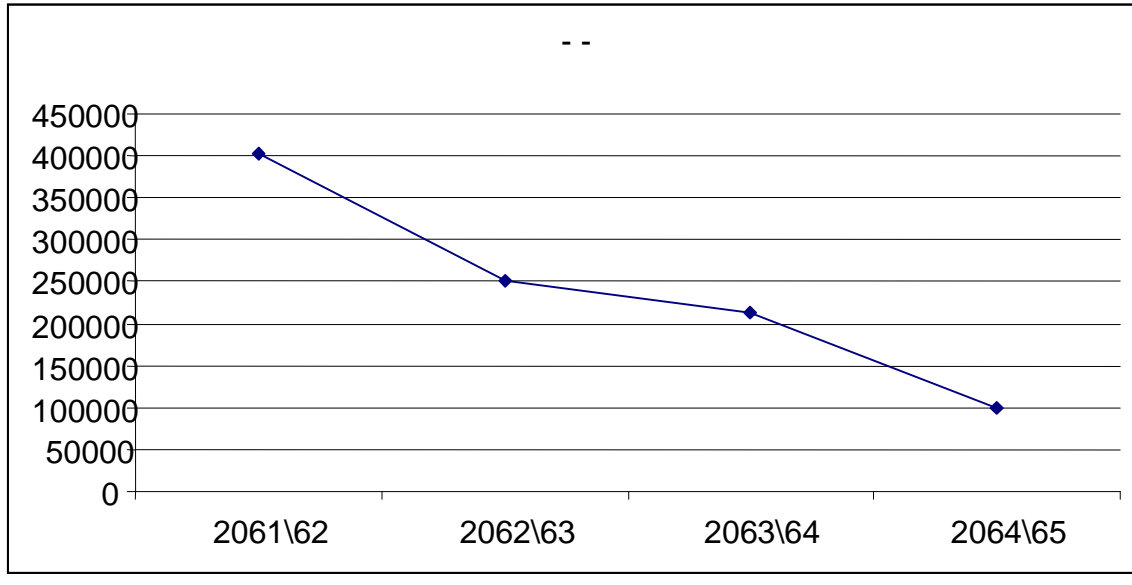


**Table no: 4.9**  
**Borrowing Trend of KBL**

Year	Borrowing(In'000')	Index trend	Yearly change
2059\60	-	-	-
2060\61	-	-	-
2061\62	401761	100%	-
2062\63	251400	62.58%	-37.42%
2063\64	212970	53.01%	-15.29%%
2064\65	100000	24.89%	-53.05

(Source: Appendix no. II)

**Figure no: 4.8**  
**Borrowing Trend of KBL**

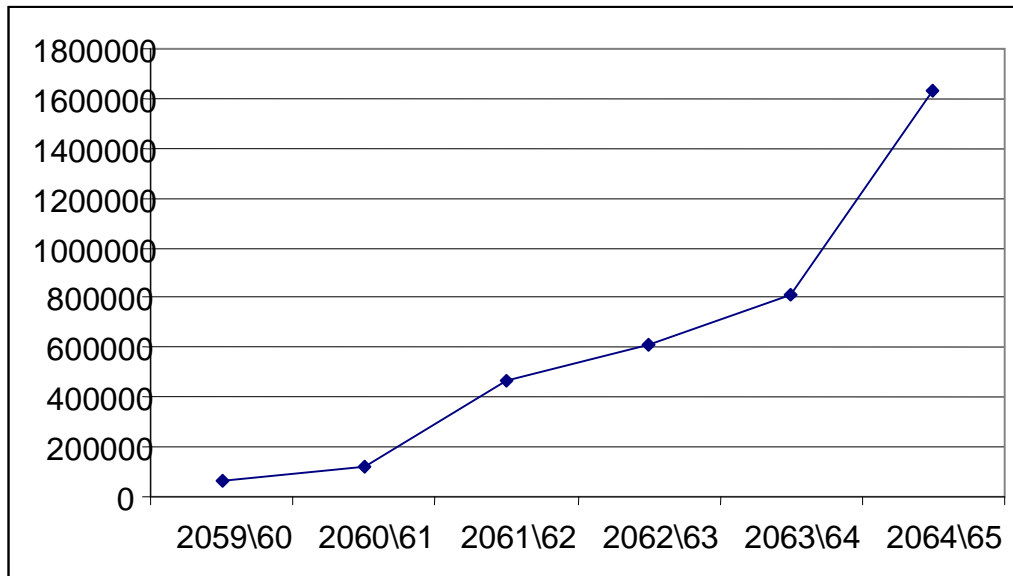


**Table no: 4.10**  
**Borrowing Trend of NSBL**

Year	Borrowing(In'000')	Index trend	Yearly change
2059\60	65826	100%	=
2060\61	117178	178.01%	78.01%
2061\62	469629	713.44%	300.78%
2062\63	612429	930.38%	30.41%
2063\64	815365	1238.67%	33.14%
2064\65	1627480	2472.40%	99.60%

(Source: Appendix no. III)

**Figure no: 4.9**  
**Borrowing Trend of NSBL**



#### **4. Deposit Trend:-**

Deposit refers to the money collected in the bank having an account as current, saving and fixed deposits of the commercial banks.

The table below shows the deposit trend of the sample banks.



**Table no: 4.11**

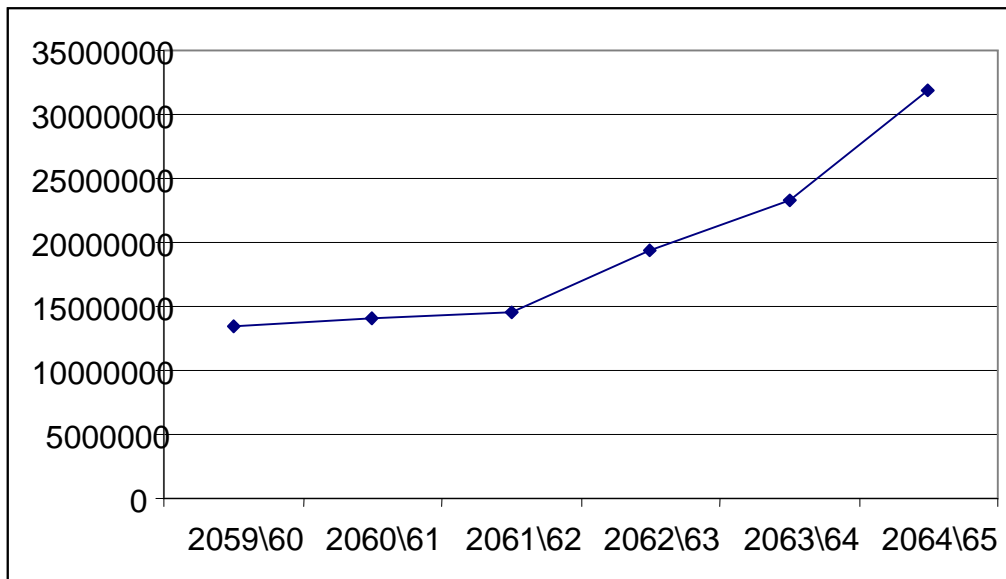
**Deposit Trend of NABIL**

Year	Deposit(In'000')	Index trend	Yearly change
2059\60	13447661	100%	-
2060\61	14119032	105%	5%
2061\62	14586609	108.47%	3.3%
2062\63	19347399	143.87%	32.64%
2063\64	23342285	173.58%	20.65%
2064\65	31915047	237.33%	36.73%

(Source: Appendix no. I)

**Figure no: 4.10**

**Deposit Trend of NABIL**



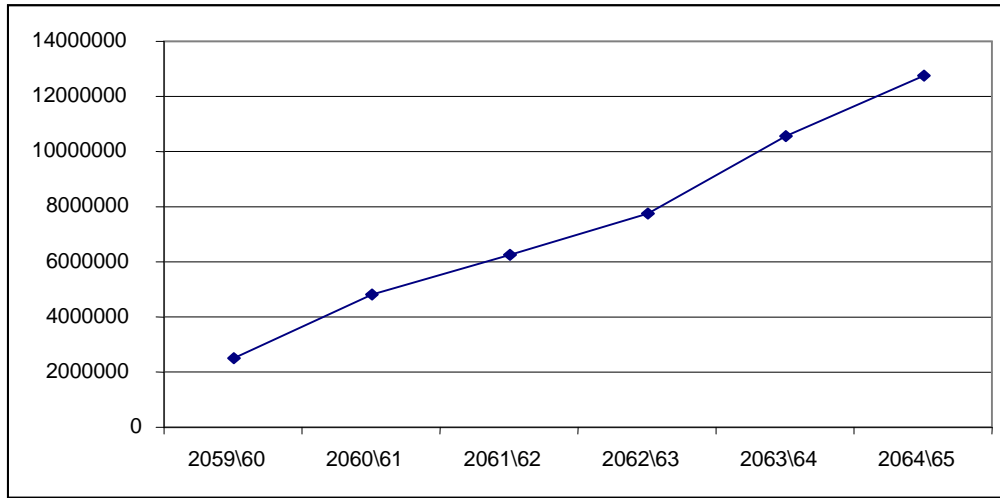
**Table no: 4.12**

**Deposit Trend of KBL**

Year	Deposit(In'000')	Index trend	Yearly change
2059\60	2513144	100%	-
2060\61	4807937	191.31%	91.31%
2061\62	6268954	249.45%	30.39%
2062\63	7768957	309.13%	23.92%
2063\64	10557091	420.08%	35.89%
2064\65	12774281	508.30%	21%

(Source: Appendix no. II)

**Figure no: 4.11  
Deposit Trend of KBL**

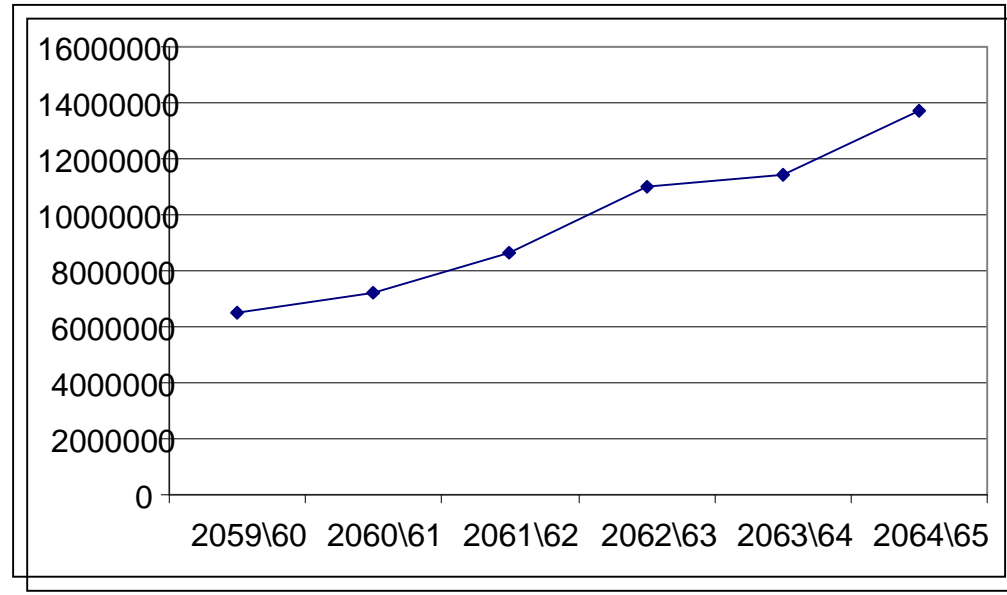


**Table no: 4.13  
Deposit Trend of NSBL**

Year	Deposit(In'000')	Index trend	Yearly change
2059\60	6522817	100%	-
2060\61	7198327	110.36%	10.36%
2061\62	8654774	132.68%	20.23%
2062\63	11002041	168.67%	27.12%
2063\64	11445286	175.47%	4.03%
2064\65	13715395	210.27%	19.83%

(Source: Appendix no. III)

**Figure no: 4.12**  
**Deposit Trend of NSBL**



### 5. Total Liabilities Trend:-

It is the total capital of commercial banks. It includes share capital (paid-up), R/S, Deposits, current liabilities of the sample bank. Total liabilities trend of the commercial bank has been shown below in the table for six consecutive fiscal year.

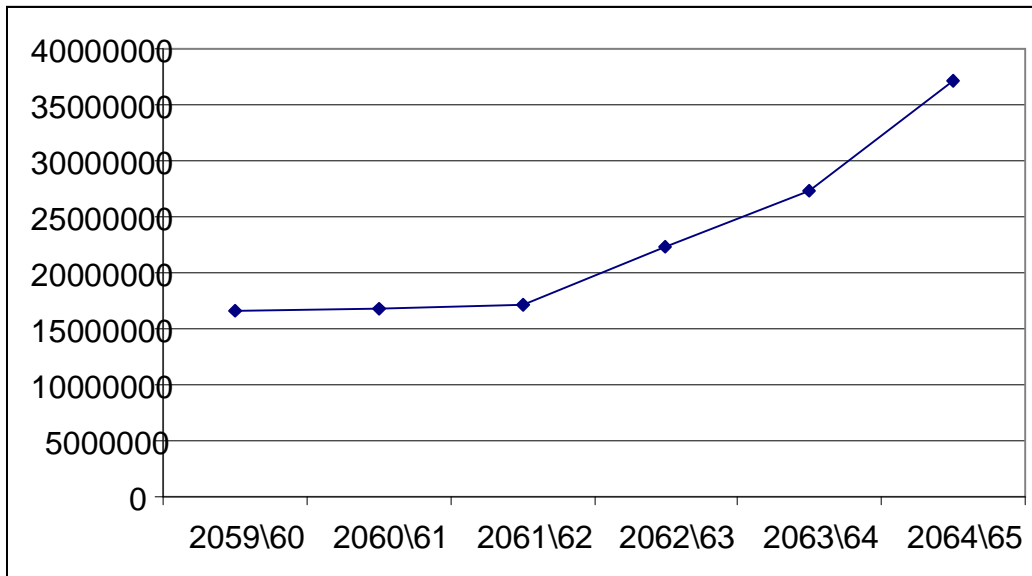
**Table no: 4.14**  
**Total liabilities trend of NABIL**

Year	Total liabilities(In'000')	Index trend	Yearly change
2059\60	16562625	100%	-
2060\61	16745487	101.10%	1.10%
2061\62	17064082	103.03%	1.91%
2062\63	22329971	134.82%	30.86%
2063\64	27253393	164.55%	22.05%
2064\65	37132759	224.20%	36.25%

(Source: Appendix no. I)

**Figure no: 4.13**

**Total liabilities trend of NABIL**



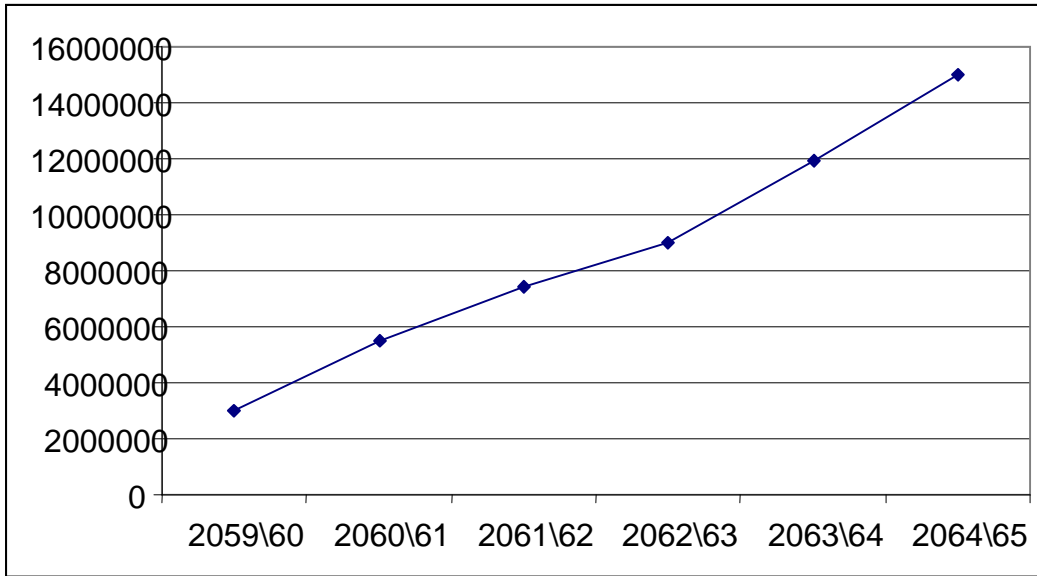
**Table no: 4.15**

**Total liabilities trend of KBL**

Year	Total liabilities(In'000')	Index trend	Yearly change
2059\60	2986175	100%	-
2060\61	5494177	183.99%	83.99%
2061\62	7437882	249.08%	35.38%
2062\63	9010276	301.73%	21.14%
2063\64	11918311	399.12%	32.28%
2064\65	15026599	503.21%	26.08%

(Source: Appendix no. II)

**Figure no: 4.14**  
**Total liabilities trend of KBL**

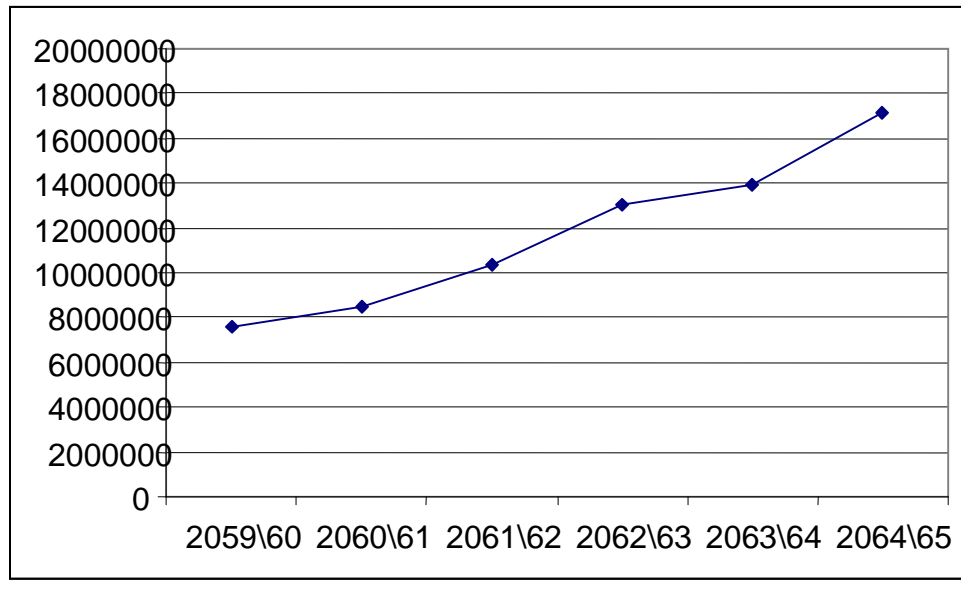


**Table no: 4.16**  
**Total liabilities trend of NSBL**

Year	Total liabilities(In'000')	Index trend	Yearly change
2059\60	7566327	100%	-
2060\61	8440406	111.55%	11.55%
2061\62	10345373	136.73%	22.57%
2062\63	13035839	172.29%	26.01%
2063\64	13901201	183.72%	6.64%
2064\65	17187446	227.16%	23.77%

(Source: Appendix no. III)

**Figure no: 4.15**  
**Total liabilities trend of NSBL**



## **6. Leverage:-**

Leverage tools prove to be best acquired and managed study of leverage helps to maintain good capital structure. Leverage helps to analyze the effect of capital collection form certain sources to decide the composition of capital structure. It guides to the optimum use of debt capital with as low interest rate as possible thereby increasing the profit of shareholders.

James and Waller “Leverage may be defined as percentage return on equity to percentage return on total capitalization.”

Lawrence J. Gitman- “The term leverage is quite commonly used to describe the firm’s ability to use fixed cost assets or funds to magnify the return on its owners.”

From above we may conclude that a practice of using debt capital at low interest rate thereby increasing equity holder’s rate of return is leverage. It helps for choosing best alternative for capital collection.

Leverage can be classified into three categories.

### **6.1 Degree of operating leverage (DOL):-**

The relationship between the rate of change that takes place in sales and the resulting rate of change in net operating income is known as operating leverage. A firm has high degree of operating leverage if it is using higher percentage of fixed cost out of the total cost.

$$\text{DOL} = \frac{\% \text{ change in EBIT}}{\% \text{ change in sales or income}}$$

Or

$$\text{DOL} = \frac{\text{CM}}{\text{EBIT}}$$

### **6.2 Degree of financial leverage (DFL):-**

Financial leverage refers to use of fixed financial costs to show the effects of changes in earnings before interest and taxes on the firm's earnings per share. The degree of financial leverage is the ratio of the percentage change in EPS to percentage change in EBIT.

$$\text{DFL} = \frac{\% \text{ change in EPS}}{\% \text{ change in EBIT}}$$

OR

$$\text{DFL} = \frac{\text{EBIT}}{\text{EBIT} - \text{I} - \text{Pd} / 1 - t}$$

Hence, there is no pref. dividend (Pd)

$$\text{Therefore DFL} = \frac{\text{EBIT}}{\text{EBT}}$$

### **6.3 Degree of combined Leverage:-**

The combination between operating and financial leverage is known as combined leverage which shows the potential use of fixed cost, both operating and financial magnify the effect of changes in sales on the firm's earnings per share. Thus, it shows the total impact of fixed cost in the firm's operating and financial structure.

$$\text{DCL} = \frac{\% \text{ change in EPS}}{\% \text{ change in sales}}$$

OR,

$$\text{DCL} = \text{DOL} * \text{DFL}$$



**Table no: 4.17**

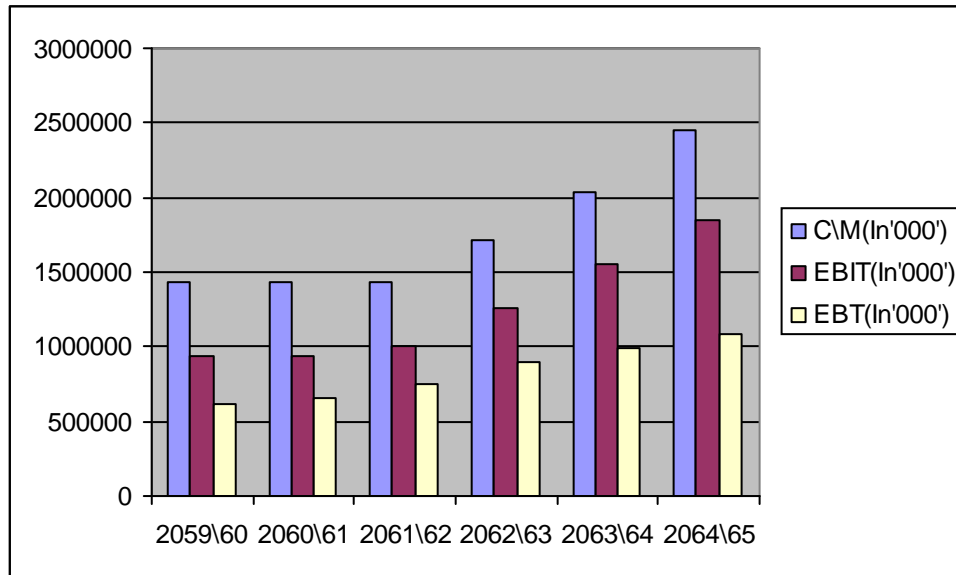
**Calculation of DOL, DFL and DCL of NABIL**

Year	C\M(In'000')	EBIT(In'000')	EBT(In'000')	DOL	DFL	DCL
2059\60	1427450	932766	615418	1.53	1.52	2.32
2060\61	1426435	940074	657126	1.52	1.43	2.17
2061\62	1438444	999910	756365	1.44	1.32	1.90
2062\63	1717410	1255228	898067	1.37	1.40	1.92
2063\64	2041150	1550818	995108	1.32	1.56	2.06
2064\65	2452948	1847431	1088995	1.33	1.70	2.26

(Source:-Appendix no IV)

**Figure no: 4.16**

**Graphical presentation of C\M, EBIT & EBT of NABIL**



**Table no: 4.18**

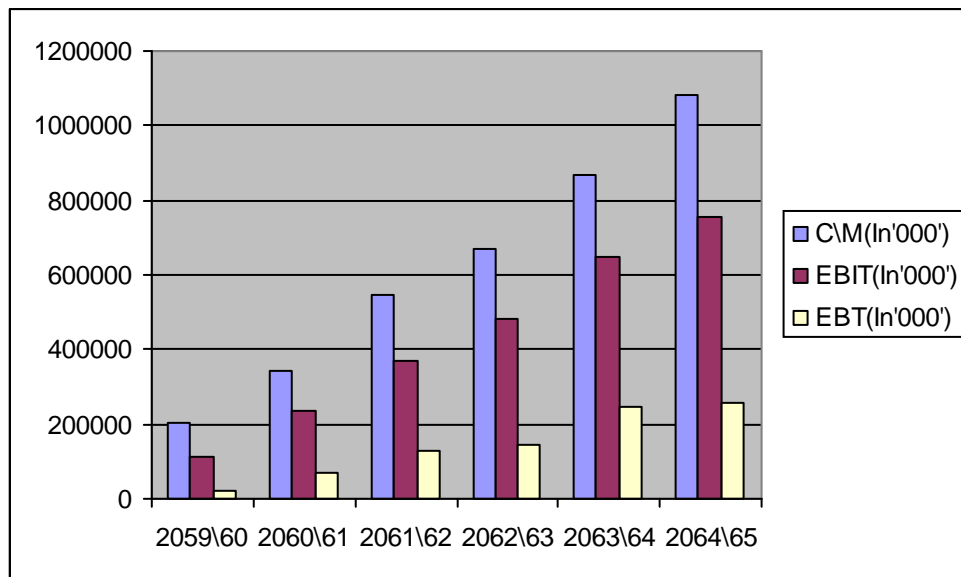
**Calculation of DOL, DFL and DCL of KBL**

Year	C\M(In'000') <sub>2</sub>	EBIT(In'000') <sub>2</sub>	EBT(In'000') <sub>2</sub>	DOL	DFL	DCL
2059\60	205880	113234	20289	1.82	5.58	10.16
2060\61	342849	233040	69137	1.47	3.37	4.95
2061\62	546040	370790	130660	1.47	2.84	4.18
2062\63	668185	484198	147142	1.38	3.29	4.54
2063\64	868293	645599	248546	1.35	2.60	3.51
2064\65	1080942	756185	257451	1.43	2.94	4.20

(Source:-Appendix no. V)

**Figure no: 4.17**

**Graphical presentation of C\M, EBIT & EBT of KBL**

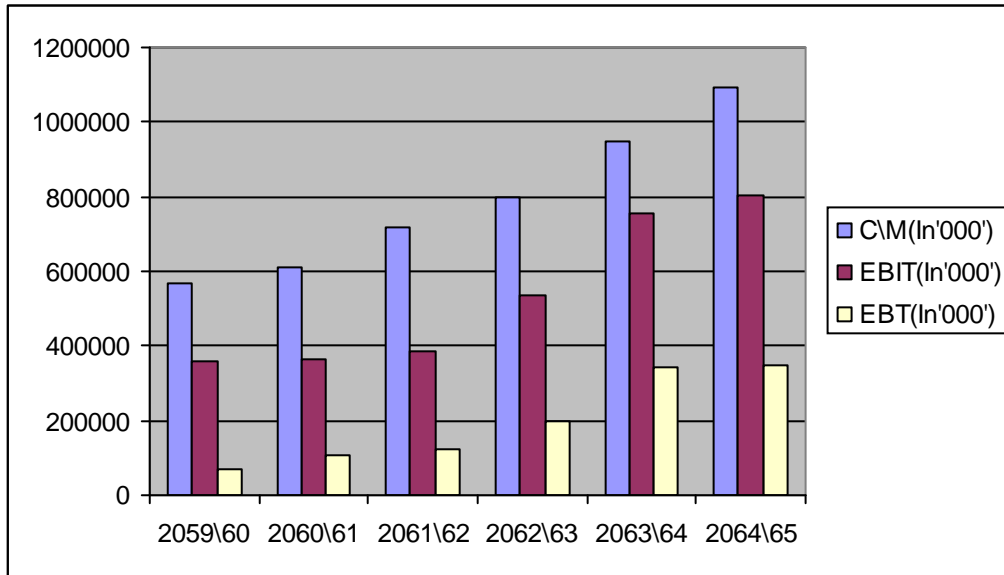


**Table no: 4.19**  
**Calculation of DOL, DFL and DCL of NSBL**

Year	C\M(In'000')	EBIT(In'000')	EBT(In'000')	DOL	DFL	DCL
2059\60	565908	360874	69054	1.57	5.23	8.20
2060\61	611606	365451	109532	1.67	3.34	5.60
2061\62	718988	383624	125194	1.87	3.06	5.74
2062\63	799670	534535	199765	1.50	2.68	4
2063\64	945774	756852	344590	1.25	2.19	2.74
2064\65	1092977	802927	348009	1.36	2.31	3.14

(Source:-Appendix no. VI)

**Figure no: 4.18**  
**Graphical presentation of C\M, EBIT & EBT of NSBL**



DOL, DFL and DCL must be above 1. The result below 1 show that the capital structure is not suitable and cannot earn as the firm should have.

According to DOL the result is positive because DOL of above bank of each year is above 1. However the trend is fluctuating.

According to DFL also the result is above 1. It suggests the use of debt capital is maximum. If the result is equal to 1, it means the firm has not used debt capital. The trend of DFL in the five consecutive years is decreasing.

According to DCL, the result seems satisfying. It shows the change is EPS with 1 % change in sales or income. However the result is decreasing.

### **7. Capital structure/Leverage/Solvency Ratio:-**

Leverage ratio analysis is the long term solvency of the firm. Solvency is the Bank's ability to pay its debt when they become due. This ratio also shows the manner by which the capital structure is formed. That is why it is called capital structure ratio.

#### Leverage Ratio includes:

- ❖ Debt equity ratio
- ❖ Debt to total assets ratio
- ❖ Interest coverage ratio/time interest Earned/Debt competence ratio
- ❖ Capital sufficiency/ capital adequacy ratio

### **7.1 Debt Equity Ratio:-**

Debt equity ratio indicates the extent to which debt financing is used relative to equity financing. Debt equity ratio is a vital tool used to analyze the long term solvency of a firm. Here the debt can be defined as total debt or as long term debt. Long term creditors generally prefer to see a modest debt equity ratio since it means greater protection and a greater stake in company's future for equity holders. Total debt includes current accounts saving accounts, calls and short deposits, overdrafts, fixed deposits, loan and advance borrowing from other banks. Shareholders equity or net worth includes paid-up capital reserve and surplus. It is computed as:

$$\text{Debt Equity ratio:} \quad \frac{\text{Total Debt}}{\text{Shareholder's equity}}$$

### **7.2 Debt to Assets ratio:-**

Debt to Assets Ratio shows what portions of the capital assets are financed by outside funds. When successfully employed this ratio benefits the shareholders by raising their expected return earning per share. A high ratio shows Bank's success in exploiting debt to be more profitable as well as it also indicates that it is a riskier capital structure and vice-versa. It is computed as:

$$\text{Debt of Assets Ratio} = \frac{\text{Total Debt}}{\text{Total Assets}} * 100\%$$

**Table no: 4.20**

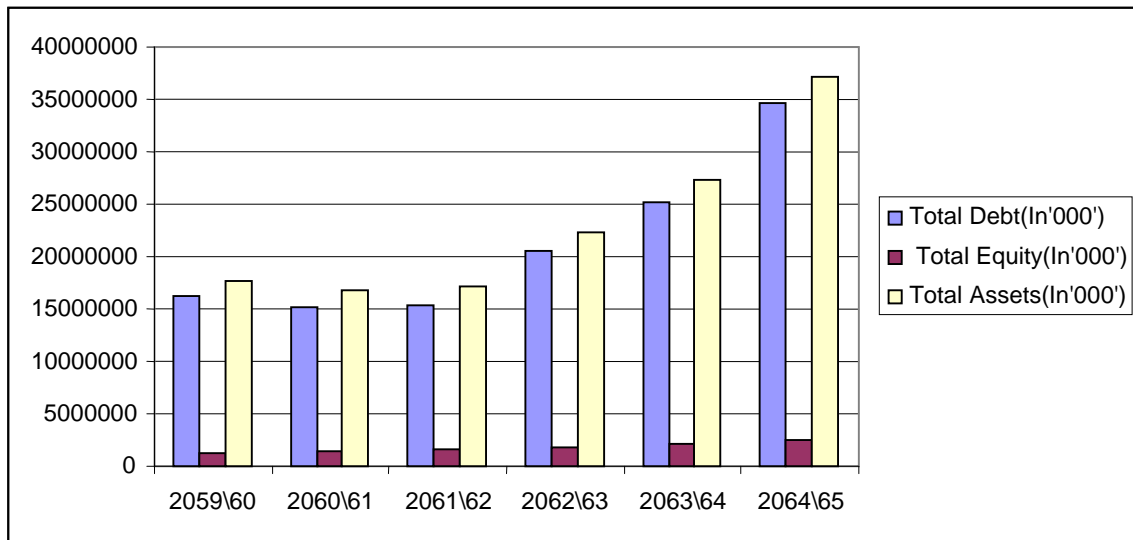
**Calculation of Debt/Equity Ratio and Debt Assets ratio of NABIL**

Year	Total Debt(In'000')	Total Equity(In'000')	Total Assets(In'000')	Debt/Equity Ratio	Debt assets Ratio
2059\60	16315065	1314187	17629252	12.42	92.55%
2060\61	15263805	1481682	16745487	10.30	91.15%
2061\62	15406444	1657638	17064082	9.30	90.29%
2062\63	20454977	1874994	22329971	10.91	91.60%
2063\64	25196343	2057050	27253393	12.25	92.45%
2064\65	34695560	2437199	37132759	14.24	93.44%

(Source:-Appendix no. I)

**Figure no: 4.19**

**Graphical presentation of Total debt, Equity & assets of NABIL**

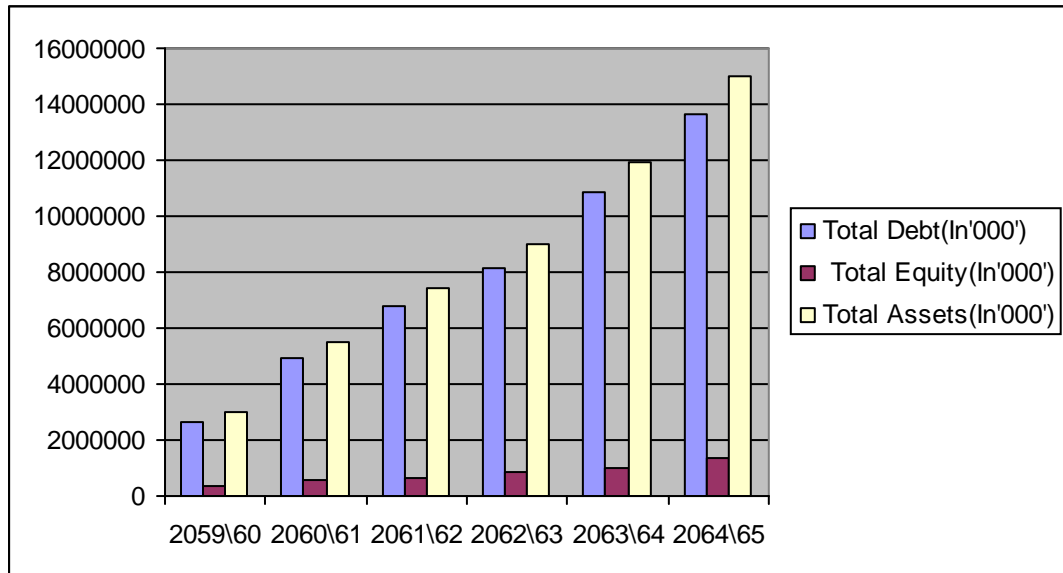


**Table no: 4.21**  
**Calculation of Debt/Equity Ratio and Debt Assets ratio of KBL**

Year	Total Debt(In'000')	Total Equity(In'000')	Total Assets(In'000')	Debt/Equity Ratio	Debt assets Ratio
2059\60	2625142	361033	2986175	7.27	87.91%
2060\61	4934458	559719	5494177	8.82	89.81%
2061\62	6792440	645442	7437882	10.52	91.32%
2062\63	8146425	863851	9010276	9.43	90.41%
2063\64	10892681	1025630	11918311	10.62	91.39%
2064\65	13661714	1364885	15026599	10.00	90.92%

(Source:-Appendix no. II)

**Figure no: 4.20**  
**Graphical presentation of Total debt, equity & assets of KBL**



**Table no: 4.22**

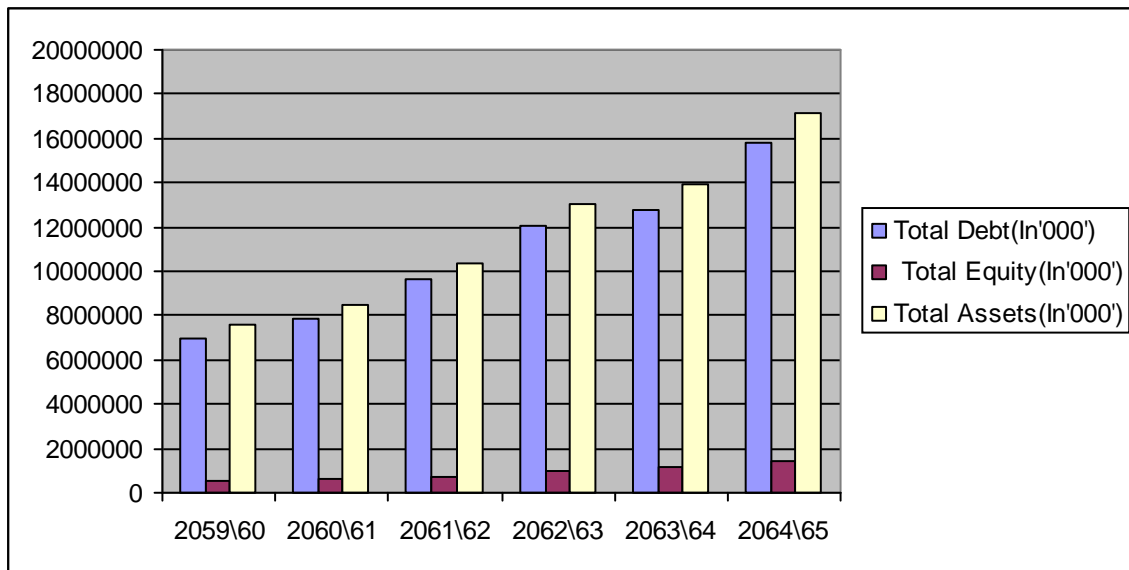
**Calculation of Debt/Equity Ratio and Debt Assets ratio of NSBL**

Year	Total Debt(In'000')	Total Equity(In'000')	Total Assets(In'000')	Debt/Equity Ratio	Debt assets Ratio
2059\60	6996475	569852	7566327	12.28	92.50%
2060\61	7813769	626637	8440406	12.47	92.60%
2061\62	9656360	689013	10345373	14.01	93.34%
2062\63	12053465	982374	13035839	12.27	92.41%
2063\64	12737911	1163290	13901201	10.95	91.65%
2064\65	15772801	1414645	17187446	11.15	91.77%

(Source:-Appendix no. III)

**Figure no: 4.21**

**Graphical presentation of Total debt, Equity & assets of NSBL**





### 7.3 Interest coverage/Time interest Earned/Debt competence Ratio:-

The interest coverage ratio also named as the time interest earned ratio is designed to relate the financial changes of a firm to its ability to service to cover them. Interest coverage ratio reflects the firm's ability to pay interest out of earnings. This ratio is simply the ratio of earnings before interest and tax (EBIT) for a particular reporting period to the amount of interest charges for the period. Too high or too low ratio is unfavorable to the banks. Too high ratio implies unused debt capacity at a firm's conservativeness in using debt to its best advantage. Whereas low ratio imply a danger signal that the firm is using excessive debt and does not have the ability to offer assured payment of interest to the creditors.

$$\text{Interest coverage Ratio} = \frac{\text{EBIT}}{\text{Interest Expenses}}$$

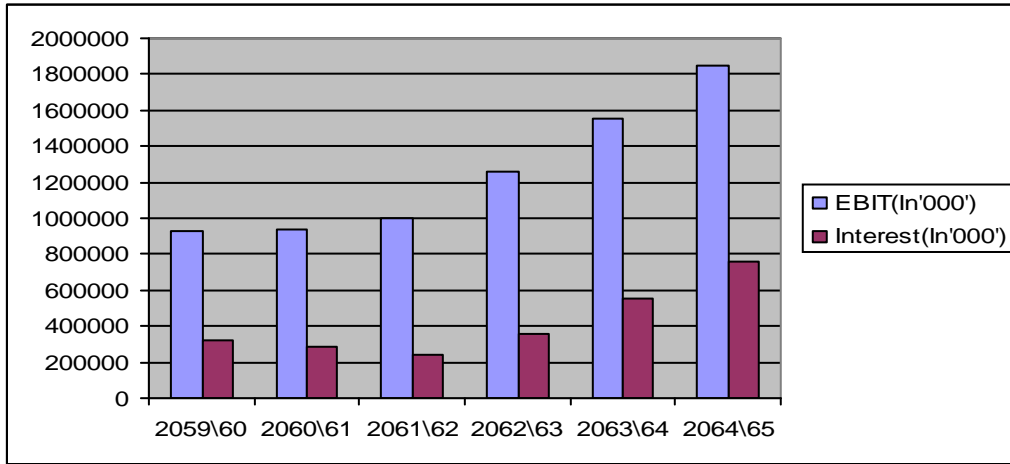
**Table no: 4.23**

#### **Computation of interest coverage Ratio of NABIL**

Year	EBIT(In'000')	Interest(In'000')	T\E Ratio
2059\60	932766	317348	2.94
2060\61	940074	282948	3.32
2061\62	999910	243545	4.11
2062\63	1255228	357161	3.52
2063\64	1550818	555710	2.79
2064\65	1847431	758436	2.44

(Source:-Appendix no. IV)

**Figure no: 4.22**  
**Graphical presentation of EBIT & Interest of NABIL**

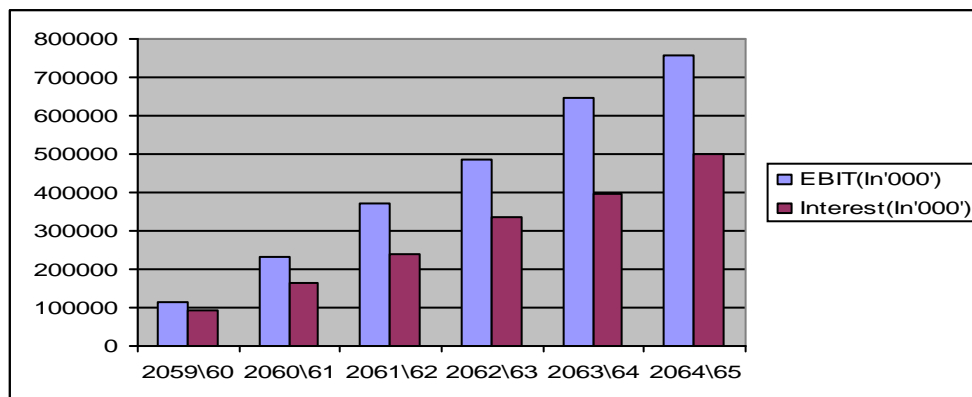


**Table no: 4.24**  
**Computation of interest coverage Ratio of KBL**

Year	EBIT(In'000')	Interest(In'000')	T\E Ratio
2059\60	113234	92945	1.22
2060\61	233040	163903	1.42
2061\62	370790	240130	1.54
2062\63	484198	337056	1.44
2063\64	645599	397053	1.63
2064\65	756185	498734	1.52

(Source:-Appendix no. V)

**Figure no: 4.23**  
**Graphical presentation of EBIT & Interest of KBL**



**Table no: 4.25**

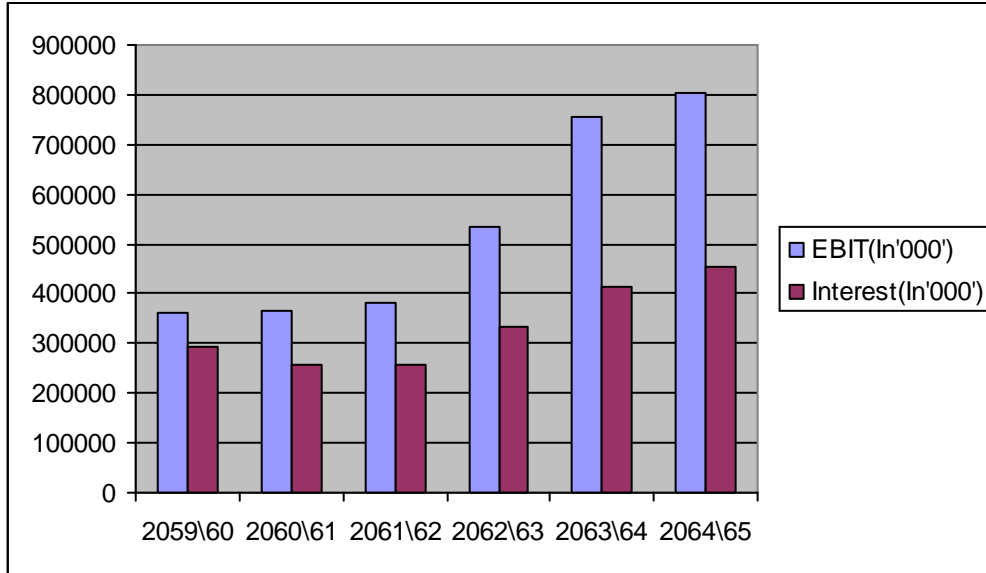
**Computation of interest coverage Ratio of NSBL**

Year	EBIT(In'000')	Interest(In'000')	T\E Ratio
2059\60	360874	291820	1.24
2060\61	365451	255919	1.43
2061\62	383624	258430	1.48
2062\63	534535	334770	1.60
2063\64	756852	412262	1.84
2064\65	802927	454918	1.77

(Source:-Appendix no. VI)

**Figure no: 4.24**

**Graphical presentation of EBIT & Interest of NSBL**



**7.4 Capital sufficiency/ Capital adequacy ratio:-**

Capital sufficiency or capital adequacy is a recent term in financial structure. Capital sufficiency ratio is based on the capital adequacy framework of Nepal Rastra Bank which itself is the proposed guidelines of the revised international coverage of capital measurement and capital standard or popularity known as Basel 2. It is used in case of bank to assess the strength of the capital, the sufficiency of the capital. Appropriate capital

sufficiency ratio has always been a controversial issue for the commercial bank. However very high or lower capital sufficiency ratio is considered to be unfavorable in terms of lowered return or lowered solvency respectively .The capital sufficiency ratio emphasis that for every kind of assets there must be some amount of capital back-ups.

Capital sufficiency Ratio is calculated as under:

Capital Sufficiency/Adequacy Ratio (CSR): -

$$= \frac{\text{Total capital fund}}{\text{Total risk weighted assets}}$$

Under capital adequacy framework, for the purpose of calculation of capital fund. Commercial banks are required to classify their capital into two parts as follows:

A. Core capital (Tier 1 capital):-

In order to rank as Tier 1, capital must be fully paid up, have no fixed servicing or dividend costs attached to it, and be freely available to absorb losses ahead of general creditors. Capital also needed to have a very high degree of permanence if it is to be treated as tiers 1.

Tier 1 capital consists of

- a. Paid up capital
- b. Share premium
- c. Non- redeemable preference share

- d. General reserve fund
- e. Cumulative profit/loss( up to previous FV)
- f. Capital Adjustment fund
- g. Current year's profit and loss (as per balance sheet)
- h. Retained earning
- i. Dividend equalization reserve
- j. Other reserve

B. Supplementary Capital ( Tier 2 capital) consists of

- a. Loan loss provision
- b. Exchange equalization reserve
- c. Assets revaluation reserve
- d. Hybrid revaluation reserve
- e. Unsecured subordinate term debt
- f. Interest rate fluctuation fund
- g. Investments adjustment reserve

The capital adequacy ratio is calculated by dividing eligible regulatory capital by total risk weighted exposure. In order to calculate capital adequate ratio banks are required to calculate their risk weighted exposure in respect to credit risk, market risk and operational risk. The methodology to calculate risk weighted exposure (RWE) for each of these risk categories is various. However Nepal Rastra Bank has the flexibility of choosing any of the approach and according to NRB the following approaches are decided to adopt initially.

1. Simplified standardized approach for credit risk

2. Basic indicator Approach for operational risk
3. Net open position approach for market risk

In the below tables we have calculated the capital Sufficiency/adequacy ratio of the sample commercial bank for the five consecutive year.

**Table no: 4.26**

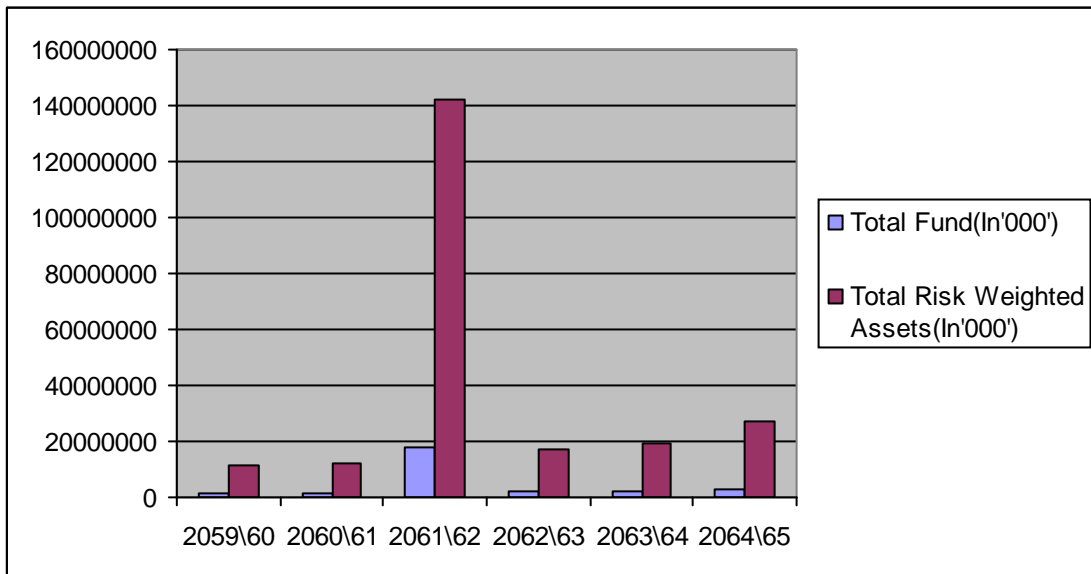
**Capital sufficiency Ratio of NABIL**

Year	Total Fund(In'000')	Total Risk Weighted Assets(In'000')	CSR
2059\60	1455096	11153131	13.05
2060\61	1609416	11872009	13.56
2061\62	17766073	141930072	12.52
2062\63	2089324	16976369	12.31
2063\64	2307632	19166766	12.04
2064\65	2998730	27010564	11.10

( Source: Appendix no. VII & X)

**Figure no: 4.25**

**Graphical presentation of Total fund & Total Risk weighted Assets of NABIL**

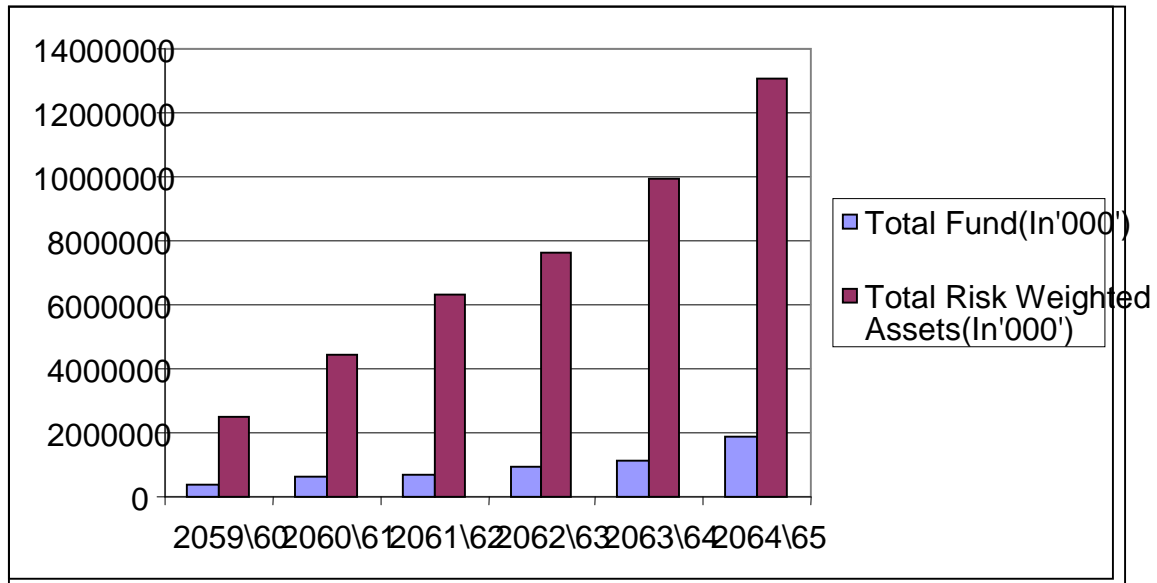


**Table no: 4.27**  
**Capital sufficiency Ratio of KBL**

Year	Total Fund(In'000')	Total Risk Weighted Assets(In'000')	CSR
2059\60	390913	2528768	15.46%
2060\61	596463	4449407	13.41%
2061\62	705529	6291844	11.21%
2062\63	940979	7625050	12.34%
2063\64	1115207	9959911	11.20%
2064\65	1882926	13070379	14.41%

( Source: Appendix no. VIII & XI)

**Figure no: 4.26**  
**Graphical presentation of Total fund & Total Risk weighted Assets of KBL**



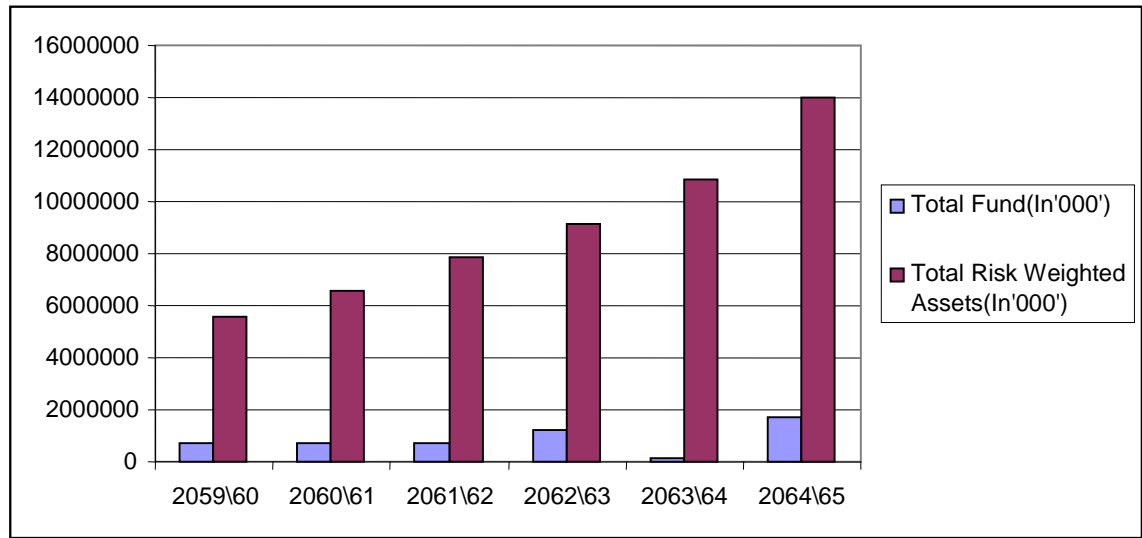
**Table no: 4.28**  
**Capital sufficiency Ratio of NSBL**

Year	Total Fund(In'000')	Total Risk Weighted Assets(In'000')	CSR
2059\60	686277	5559624	12.34%
2060\61	717204	6551967	10.95%
2061\62	744876	7869616	9.47%
2062\63	1242570	9159271	13.57%
2063\64	144800	10873279	13.29%
2064\65	1722187	13975708	12.32%

( Source: Appendix no. IX & XII)

**Figure no: 4.27**

**Graphical presentation of Total fund & Total Risk weighted assets of NSBL**





## **CHAPTER -FIVE**

### **SUMMARY, CONCLUSIONS AND RECOMMENDATIONS**

#### **5.1 Summary:-**

This study deals with the capital structure of NABIL Bank ltd, Kumari Bank ltd and Nepal SBI Bank ltd. So the basic objective of the study is to analyze the composition of component part of capital structure of the above mentioned banks. The study has been divided into five chapters.

The first chapter consists of framework of the study as well as profile of selected commercial banks. This chapter also speaks out about the focus of the study. The study is based on some assumption and it has its own limitations.

Similarly, second chapter is good review of the issues related with abstracts of capital structure.

Third chapter includes design methods and procedures of the thesis report. Sources of data and method of data collection are also mentioned. It also explains the tools and techniques used for the analysis of required data.

Fourth chapter deals with presentation and analysis of data. In this chapter some of the financial tools such as leverage, capital structure ratio, index of the components of capital structure as well as graph have been used to analyze the facts. This chapter is considered as the most important part revealing the performance of the selected Banks.

Finally the fifth chapter is about summary conclusions and recommendations. Facts and findings from the study are recalled in this chapter. This chapter also recommends some suggestions for the financial betterment of the commercial banks.

## **5.2 Conclusions:-**

The share capital of NABIL remains at Rs. 491654 in five consecutive years .In the fiscal year 2064\65 it increased to Rs.689216.The share capital of KBL in the fiscal year 2059\60 is Rs.350000 and it has increase to Rs. 500000 and it remains same in the fiscal year 2061\62 also. After the fiscal year 2062\63 the share capital of KBL is increasing each year. However, the trend of increasing of KBL is unexpectedly high in the fiscal year 2064\65.And the share capital of NSBL in fiscal year 2059\60 is Rs.425157.In the fiscal year 2060\61 it increased to Rs.426876.But, in the fiscal year 2061\62 it decreased to Rs.431866.After the fiscal year 2062\63 the share capital of NSBL is increasing each year.

The reserve and surplus of NABIL, KBL and NSBL in the increasing trend. The increasing trend of reserve and surplus is very high in each fiscal year .Increasing reserve and surplus will reduce the shareholder's profit.

NABIL and NSBL had borrowed from the local and foreign institutions. The trend of total borrowing of NABIL is very fluctuating. However, the trend of total borrowing of NSBL is increasing each year. KBL had not borrowed from outside in the fiscal year 2059\60 and 2060\61. Thereafter, the borrowing trend of KBL is decreasing in each year.

The deposit trend of NABIL, KBL and NSBL also seem to be increasing over the last six years. In the capital structure of any financial institutions deposit play the vital role because it is very essential for any financial organizations.

The total liabilities of NABIL, KBL and NSBL also seem to be increasing over the last six years.

From the study of DOL, we seem that percentage of change in profit of shareholders is greater than the income. It is good for firm to have such result. The trend of DOL of NABIL is in the decreasing trend. However, the trend of DOL of NSBL and KBL is quite fluctuating.

According to study of DFL, we can see that KBL and NSBL have higher degree of financial leverage in the fiscal year 2059\60. DFL of both banks have been decreasing trend. But, the DFL of NABIL is quite fluctuating in each year. If, the DFL is increasing trend , it implies that the firms have used greater amount of debt capital in their financial structure. This directly affects the EPS and reduce the EPS. So, the maximum use of debt is not suitable. But, if the trend of DFL is decreasing, it implies that the firm is trying to reduce the debt amount. If the result comes to 1, it means the firm has not used debt capital.

DCL shows the ratio between EPS and income. It shows the effect of change in income due to the change in EPS. It is the combination of DOL and DFL and that is why it is called degree of combined leverage. DCL

trend of NABIL, KBL and NSBL is quite fluctuating. This result shows that the positions of banks are not bad and not satisfactory.

EPS is one of the most widely used majors of the bank's performance. It is important index of the bank's performance and the investor really heavily on it for their investment decision. The EPS of NABIL ranges between RS.84.66, Rs.92.61, Rs.105.49, Rs.129.21, Rs.137.08 and Rs.108.31 respectively in the fiscal year 2059\60, 2060\61, 2061\62, 2062\63, 2063\64 and 2064\65. Similarly, the EPS of KBL ranges between Rs.3.26, Rs.9.74, Rs.17.58, Rs.16.59, Rs.22.70 and Rs.16.35 respectively in the fiscal year 2059\60, 2060\61, 2061\62, 2062\63, 2063\64 and 2064\65. The EPS of NSBL ranges between Rs.11.47, Rs.14.25, Rs.13.29, Rs.18.28, Rs.39.35 and Rs.28.33 respectively over six consecutive year.

Capital structure (Leverage) ratio has been used to analyze the long-term solvency of the mentioned Banks. This ratio also shows the manner by which capital structure is formed.

Debt-equity ratio is the relationship between borrowed funds and owner's capital. The debt equity ratio of NABIL is 12.042 times, 10.30 times, 9.30 times, 10.91 times, 12.25 times and 14.24 times respectively in the fiscal year 2059\60, 2060\61, 2061\62, 2062\63, 2063\64 and 2064\65. Similarly, D\E Ratio of KBL is 7.27 times, 8.82 times, 10.52 times, 9.43 times, 10.62 times and 10 times respectively for six consecutive year. The D\E Ratio of NSBL is 12.28 times, 12.47 times, 14.01 times, 12.27 times, 10.95 times and 11.15 times respectively in the fiscal year 2059\60, 2060\61, 2061\62, 2062\63, 2063\64 and 2064\65.

Hence, the result shows that the total debt of each bank is increasing in each year as compared to shareholder's fund. It is quite not good for financial institutions.

Combination of debt assets ratio is in terms of total debt to total assets reveals that the commercial banks are highly leveraged on six years time horizon. It means the assets of selected banks have been financed more funds collected from creditors.

The trend of debt assets ratio of NABIL, KBL and NSBL is fluctuating over the study period of six years.

Debt ratio of concerned bank shows the value of assets is a bit greater than total debt. And its increasing trend refers to increasing financial risk and decreasing trend refers to decreasing financial risk.

Interest coverage ratio is the firm's ability to cover the interest coverage ratio of NABIL and KBL is fluctuating over the study period. The trend of interest coverage ratio of NSBL is increasing over the period of 2063\64 but it is decreased in year 2064\65.

The computed interest coverage ratio of all three banks in above tables shows how many times the interest changes are covered by profits. Through the coverage ratio of bank is positive these banks should make effort to improve the prevailing situation by improving its operating efficiency to reduce the amount of debt capital through refunding debt simultaneously.

Capital sufficiency ratio shows the excess of capital over its risk weighted assets. Appropriate capital sufficiency ratio has always been an issue for commercial banks. Because very high Capital sufficiency ratio is unfavorable in terms of lowered return whereas very low ratio is unfavorable in terms of lowered solvency. However, according to Basel 2 framework the standard capital sufficiency ratio is 11%.

The Capital sufficiency ratio of NABIL for six consecutive years is 13.05%, 13.56%, 12.52%, 12.31%, 12.04% and 11.10% respectively it implies that the Capital sufficiency ratio of all six years are above the standard.

The Capital sufficiency ratio of KBL for six consecutive years is 15.46%, 13.41%, 11.21%, 12.34%, 11.20% and 14.41% respectively it also implies the Capital sufficiency ratio exceeds the standard. Similarly, the Capital sufficiency ratio of NSBL for six consecutive years is 12.34%, 10.95%, 9.47%, 13.57%, 13.29% and 12.32% respectively. Which it implies that in the year 2060\61 and 2061\62 it is under the standard and in the year 2059\60, 2062\63, 2063\64 and 2064\65 it exceeds the standards.

Among the three Banks, the Capital sufficiency ratio of NABIL seems quite good as it is near the standard level all the six years period. The ratio is 13.05% in year 2059\60, 13.56% in 2060\61, 12.52% in 2061\62, 12.31% in 2062\63, 12.04% in 2063\64 and 11.10% in 2064\65.

### 5.3 Recommendations

) A clear financial picture can be viewed from all above presentation. Now some valuable and timely suggestions and recommendation are put forwarded on the basics of finding and conciliation or literally their financial pictures in order to revitalize and improve financial position of NABIL, KBL and NSBL.

) The capital structure of selected bank is highly leveraged. The proportion of debt and equity capital should be decided keeping in mind the efforts of tax advantage and financial distress. The bank when in difficult to pay interest and principal, ultimately lead to liquidation or bankruptcy. For such the bank should reduce the high use of debt capital.

) Debt Assets ratio also suggests to reduce the outsider's fund as for as possible because there is low difference between debt and total assets.

) DFL and DCL refer that EPS of the sample Bank is greatly affected by interest expenses. So interest paid out should be reduced to increase EPS and to reduce interest expenses bank loan as a whole should be reduced.

) The fluctuating trend of capital sufficiency ratio suggests that Bank's are not meeting the standard ratios. Sometimes they have very highly reserve of capital and sometimes are suffered by under capitalization.

) Additionally banks are required and recommended to expand assets and branches which ultimately affect the banks capital structure and expected to increase the profitability more than the present.

) Similarly, commercial banks are not basically concentrated to mobilize their deposits funds in productive areas. So they are proposed to come forward to match government obligation by financing the priority sector development sectors.

) The profitability position of the firm is not much satisfactory. Deposits of the increasing trend of EAT each year; banks are not able to make enough money. Having geared up capital structure position and insufficient return indicates the resources to be put into more profitable sector and be mote concerned to get better return and be careful about their financial condition so that their returns would not be depressed any more.



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# APPENDIX

**APPENDIX NO.I**  
**Comparative Balance Sheet of NABIL**  
**As at 31st Ashad, 2059/60 to 2064/65 (In '000')**

<b>Capital &amp; Liabilities</b>	<b>2059/60</b>	<b>2060/61</b>	<b>2061/62</b>	<b>2062/63</b>	<b>2063/64</b>	<b>2064/65</b>
Share Capital	491654	491654	491654	491654	491654	689216
Reserve & Surplus	822533	990028	1165984	1383340	1565395	1747983
Debentures & Bonds	--	--	--	--	--	240000
Borrowings	961461	229660	17063	173202	882573	1360000
Deposits	13447661	14119032	14586609	19347399	23342285	31915048
Bills Payable	108944	173499	85420	112607	83515	238422
Proposed & Undistributed Dividend	--	--	361221	435084	509418	437373
Income Tax Liabilities	--	--	15345	34605	--	38777
Other	730372	741613	340787	352080	378553	465941

Liabilities						
Total	16562625	16745487	17064082	22329971	27253393	37132759

Assets	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Cash Balance	187777	286886	146353	237819	270407	511427
Balance with NRB	966990	683600	389705	318359	1113415	1829471
Balance with Bank/Financial Institutions	--	--	23323	74061	16003	330244
Money at Call & Short Notice	670204	928733	868428	1734902	563533	1952361
Investment	6031176	5835948	4275528	6178533	8945311	9939771
Loans, Advance & Bills Payable	7755952	8189993	10586170	12922543	15545779	21365053
Fixed Assets	251915	338126	361235	319086	286895	598039
Non-banking Assets	--	--	--	--	--	--
Other Assets	708611	492199	413340	544668	512050	606394
Total	16562625	16745487	17064082	22329971	27253393	37132759

Source:- Annual Report of NABIL from F/Y 2059/60 to 2064/65

## APPENDIX NO.II

### Comparative Balance Sheet of KBL As at 31st Ashad, 2059/60 to 2064/65 (In '000')

Capital & Liabilities	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Share Capital	350000	500000	500000	625000	750000	1070000
Reserve & Surplus	11033	59719	145422	238851	275630	294885
Debentures & Bonds	--	--	--	--	--	400000
Borrowings	--	--	401761	251400	212970	100000
Deposits	2513144	4807937	6286954	7768957	10557091	1277428
Bills Payable	4129	14637	7339	11919	16554	65297
Proposed & Undistributed Dividend	--	--	--	6378	--	--
Income Tax Liabilities	--	--	--	296	11007	(9650)
Other	107868	111883	114386	107275	95059	331786

Liabilities						
Total	2986175	5393477	7437882	9010276	11918311	1502659

Assets	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Cash Balance	40800	68472	111249	135795	190748	565641
Balance with NRB	250905	617007	332122	210553	384845	244576
Balance with Bank/Financial Institutions	--	--	--	43282	96520	123624
Money at Call & Short Notice	--	--	90000	145000	372215	55360
Investment	423155	983504	1190271	1394948	1678418	2138798
Loans, Advance & Bills Payable	2105736	369009	5590926	6891855	8929013	1133508
Fixed Assets	40425	57152	82984	91933	189324	222001
Non-banking Assets	--	--	--	3592	2394	3141
Other Assets	125154	119033	40330	93318	74834	338370
Total	2986175	5393477	7437882	9010276	11918311	1502659

Source:- Annual Report of KBL from F/Y 2059/60 to 2064/65

### APPENDIX NO.III

## Comparative Balance Sheet of NSBL As at 31st Ashad, 2059/60 to 2064/65 (In '000')

Capital & Liabilities	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Share Capital	425157	426876	431866	640236	647798	874528
Reserve & Surplus	144695	19761	257147	342138	515492	540117
Debentures & Bonds	--	--	--	200000	200000	200000
Borrowings	65826	117178	469629	612429	815365	1627480
Deposits	6522817	7198327	8654774	11002041	11445286	13715395
Bills Payable	--	--	31123	46239	48856	75115
Proposed & Undistributed Dividend	--	--	--	35470	91024	12229
Income Tax	--	--	--	--	--	--

Liabilities						
Other Liabilities	407832	498264	500834	157288	137378	142582
Total	7566327	8440406	10345373	13035839	13901201	17187446

Assets	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Cash Balance	269659	161222	143750	244188	287531	308102
Balance with NRB	1063875	703204	579995	626123	556678	403810
Balance with Bank/Financial Institutions	--	--	--	247848	278481	631049
Money at Call & Short Notice	--	--	123113	363200	350000	304013
Investment	1207275	1907521	2607680	3610775	2659453	3088887
Loans, Advance & Bills Payable	4468720	5143662	6213879	7626736	9460451	12113698
Fixed Assets	71033	62350	66452	66712	97219	120222
Non-banking Assets	--	--	--	24556	3847	--
Other Assets	485764	432446	610505	225701	207541	217665
Total	7566327	8440406	10345373	13035839	13901201	17187446

Source:- Annual Report of NSBL from F/Y 2059/60 to 2064/65

## APPENDIX NO.IV

### Comparative Income Statement of NABIL From F\Y 2059/60 to 2064/65 (In'000')

Particulars	F\Y 2059\60	F\Y 2060\61	F\Y 2061\62	F\Y 2062\63	F\Y 2063\64	F\Y 2064\65
<b>Income:-</b>						
Interest Income	1017872	1001617	1068747	1309999	1587759	1978697
Commission & Discount	144406	135 958	128377	138294	150609	156235
Income from Currency exchange	144075	157324	184879	185484	209926	196487
Income from Other Sources	34151	38755	56441	82898	87575	97445
Non- operating Income	86946	92781	--	735	5281	24084

A)Total Income	1427450	1426435	1438444	1717410	2041150	2452948
<b>Expenses:-</b>						
Staff Expenses	210583	180840	199516	219781	240161	262908
Office Expenses	166200	150759	190299	182696	188183	220751
Non-operating Expenses	51537	82822	(35479)	(30095)	(37517)	12959
Bonus for Staff	66364	71940	84198	89800	99505	108899
B)Total Expenses	494684	486361	438534	462182	490332	605517
EBIT	932766	940074	999910	1255228	1550818	1847431
less:- Interest Expenses	317348	282948	243545	357161	555710	758436
EBT	615418	657126	756365	898067	995108	1088995
Less:-tax	199147	201763	237671	262741	321086	342522
EAT	416273	455363	518694	635326	674022	746473
Less:-Preferred Dividend	0	0	0	0	0	0
EAS	416273	455363	518694	635326	674022	746473
No. of Share(N)	4917	4917	4917	4917	4917	6892
EPS(EAS\N)	84.66	92.61	105.49	129.21	137.08	108.31

Source:- Annual Report of NABIL from F/Y 2059/60 to 2064/65

## APPENDIX NO.V

### Comparative Income Statement of KBL From F\Y 2059/60 to 2064/65 (In'000')

Particulars	F\Y 2059\60	F\Y 2060\61	F\Y 2061\62	F\Y 2062\63	F\Y 2063\64	F\Y 2064\65
<b>Income:-</b>						
Interest Income	185090	310216	499918	605527	791284	957246
Commission & Discount	9413	16446	23083	26281	40764	48495
Income from Currency exchange	7144	14414	14989	26374	20294	41808
Non- operating Income	3650	--	5442	--	670	15588

Income from Other Sources	583	1773	2608	10003	15281	17805
A)Total Income	205880	342849	546040	668185	868293	1080941
<u>Expenses:-</u>						
Staff Expenses	23254	28576	42395	59820	74244	89570
Office Expenses	45504	56441	71812	88683	104079	148143
Non-operating Expenses	21515	17112	46527	20772	19515	61300
Bonus for Staff	2373	7680	14516	14712	24856	25744
B)Total Expenses	92646	109809	175250	183987	222694	324757
EBIT(A-B)	113234	233040	370790	484198	645599	756185
less:- Interest Expenses	92945	163903	240130	337056	397053	498734
EBT	20289	69137	130660	147142	248546	257451
Less:-tax	8879	20437	42760	43454	78296	82506
EAT	11410	48700	87900	103688	170250	174945
Less:-Preferred Dividend	0	0	0	0	0	0
EAS	11410	48700	87900	103688	170250	174945
No. of Share(N)	3500	5000	5000	6250	7500	10700
EPS(EAS\N)	3026	9.74	17.58	16.59	22.70	16.35

Source:- Annual Report of KBL from F/Y 2059/60 to 2064/65

## APPENDIX NO.VI

### Comparative Income Statement of NSBL From F\Y 2059/60 to 2064/65 (In'000')

Particulars	F\Y 2059\60	F\Y 2060\61	F\Y 2061\62	F\Y 2062\63	F\Y 2063\64	F\Y 2064\65
<u>Income:-</u>						
Interest Income	469740	493598	578372	708719	831117	970513
Commission & Discount	29960	30667	42568	40754	52592	50918
Income from Currency exchange	18510	30616	32357	43060	49464	51989



Income from Other Sources	47696	56725	64248	7137	12601	19557
Non- operating Income	--	--	1443	--	--	--
A)Total Income	565908	611606	718988	799670	945774	1092977
<u>Expenses:-</u>						
Staff Expenses	33731	32510	37582	50540	53232	74890
Office Expenses	77364	82180	90629	99214	120112	152380
Non-operating Expenses	86266	119295	193243	95405	(18881)	27977
Bonus for Staff	7673	12170	13910	19976	34459	34803
B)Total Expenses	205034	246155	335364	265135	188922	290050
EBIT(A-B)	360874	365451	383624	534535	756852	802927
less:- Interest Expenses	291820	255919	258430	334770	412262	454918
EBT	69054	109532	125194	199765	344590	348009
Less:-tax	20305	48680	67807	82762	89681	100263
EAT	48749	60852	57387	117003	254909	247746
Less:-Preferred Dividend	0	0	0	0	0	0
EAS	48749	60852	57387	117003	254909	247746
No. of Share(N)	4251	4269	4319	6402	6478	8745
EPS(EAS\N)	11.47	14.25	13.29	18.28	39.35	28.33

Source:- Annual Report of NSBL from F/Y 2059/60 to 2064/65