SECTION 1

INTRODUCTION

1.1 Background:

1.1.1 Overview of Nepalese Financial System

Financial sectors refer to all the variables, retails, formal and informal institutions in an economy offering financial services to consumers, businesses, and other financial institutions. In its broadest definitions, it includes everything from banks, stock exchanges and insurers, to credit unions, microfinance institutions and money lenders (DFID, 2004). A modern financial system is important in the economy in order to pool and utilize financial resources, reduce cost and risk, expand and diversify opportunities, increase productivity and facilitate economic growth. Similarly growth of financial services sector is important for economic growth. Further Levine (1997) states that the level of financial development is a good predicator of future rate of economic growth. A deep and efficient financial system can robustly contribute to sustain economic growth and lower poverty (Beck, Levine and loyaza, 2000).Study made by Capiro and Honahon, (2001) also found that growth and effective functioning of a full service financial system is essential for economic development and prosperity.

Financial sector of Nepal can be divided into two parts – Banking system and Non-Banking system. The banking system comprises Nepal Rastra Bank and all commercial banks while Non-Banking system consists of the Development Banks, Finance Companies, Rural Micro Finance Development Banks, Saving and Credit Cooperatives with limited banking activities and Non-Government Organization with limited banking activities. Moreover Employees Provident Fund, Nepal Stock Exchange Limited, Insurance Companies, Deposit Insurance and Credit Guarantee Corporation, Credit Information Center Limited, Citizen Investment Trust and Postal Saving Offices are also categorized under the non bank financial system but do not come under the jurisdiction of central bank for their regulation and supervision (Karna :2008).

Evolution of organized financial system development in Nepal can be divided into three phases; 1937-1956, 1956-1985, post -1985.Establishment of Nepal bank ltd (NBL), the first commercial bank of Nepal, in 1937 is marked as the beginning of the development of the Nepalese financial system. Prior to the establishment of the NBL, Nepalese people have to keep their saving either in cash of in Indian banks. External transactions were affected through Indian banks. The central banking functions were shared between reserve bank of India and minting department of ministry of finance of Nepal (Acharya, Khatiwada and Aryal: 2003).

Nepal financial system underwent a major thrust after the establishment of NRB, the central bank in 1956.A number of financial institutions of diverse nature and varying institutions were established in the public sector. These includes Nepal Industrial Development Corporation(NIDC), Agriculture Development Bank(ADB/N), Employee Provident Fund(EPD), Rastriya Banijya Bank(RBB), Deposit and Credit guarantee corporation, Nepal Insurance Corporation and Securities, Marketing Centre.NRB was directly involved in setting most of these institutions with equity participation .Due to adoption of economic reform and liberalization of financial system, foreign banks are allowed to operate joint venture in Nepal was a kick-start in this regard. Nepal Arab Bank (Nabil) was established as the first joint venture commercial bank in 1984 with breaking the trend of knocking door of a bank by customer but start knocking door of customer. Two more joint ventures were established in the subsequent years Nepal Indosuez Bank (currently Nepal Investment Bank) was established in 1986 and Nepal grandlays Bank (currently standard chartered bank) in 1987. Himalayan Bank Ltd. was established with the joint venture with Habib Bank of Pakistan. Nepal SBI bank followed Himalayan Bank in 2051 B.S. The three new banks were opened in 2051 B.S., Nepal Bangladesh Bank Ltd., Everest Bank Ltd., and Bank of Kathmandu Ltd. Because of the induction of liberal policy not only a number of foreign bank with local participation were established but also a number of private sector banks came into operation. The basic objective to allow foreign bank to open a joint venture in Nepal was mainly to develop banking sector to create healthy competition and introduced new technological efficiency in banking sector. Entry of joint venture banks in the country opened the door to international standard banking services. Joint venture banks are providing personalized and customized service to their clients which are at par with foreign banks. They have introduced service packages like 24 hour banking, ATM and credit card.

As per Bank and Financial Institutions Act,2063(2006),Nepal Rastra Bank has classified the licensed institutions into “A”, “ B”, “C” and “D” classes on the basis of minimum paid up capital. Commercial Banks are A class institutions, whereas Development Banks are categorized as B, Finance Companies as C and Micro Finance Development Banks as D. These financial institutions are regulated and supervised by NRB. Some of the regulations imposed by the central bank are capital adequacy related regulation, loan classification, loan loss provisioning, single obligor limit, accounting and transparency, risk management, corporate governance, cash reserve ratio, deprived sector lending etc.These regulations have contributed to the soundness of Nepal’s financial system. By mid July 2009,there are 26 commercial banks, 63 development banks, 77 finance companies, 15 micro finance institutions, 16 cooperatives and 45 NGOs, 1 Citizen Investment Trust(CIT),1 Employee provident Fund,1 Deposit and Credit Guarantee Corporation(SCGC),1 Nepal Stock Exchange, 1 Security Board(SEBON) and several postal saving banks. Based on ownership structure as on mid July 2009, there are 3 Public Sector Banks and 23 Private Sector Banks. The Private Banks can be further re-grouped into the local private banks and Joint-Venture Banks. The banks with the local private investment are local private banks while the banks with the investment of foreign institutions along with the local investment are Joint-Venture Banks. As on mid July 2009, there were seven Joint venture private banks in Nepal.

1.1.2 Banking sector:

It has been seen that the origin of banking was from the ancient time. Although at that time the banking activities were not in systematic way but banking activities used to hold from that time. It has been said that the lending and borrowing are as old as money itself. The word bank has been derived from the Italian word "banco". Macleod has defined the word banco as the accumulation of money or stock. Bank can be briefly defined as the financial intermediary between the depositor and credit seeker. The transaction can happen between the bank and depositor only when the depositors deposit certain amount in the bank and the bank has good relation with its customer. The Bank can make good relation with its customer only when it will be able to payback the amount deposited by the depositor at time. The intermediation takes place when bank accept deposit from general public, corporate bodies and private organization and invest those deposit for profitable purpose in form of loan and advances. The bank has started providing much more facility to its customer such as remittance of money, letter of credit, Bank guarantee and many more. The activities carried on by banks are called banking activity. Banking as an activity involves acceptance of deposits and lending or investment of money. It facilitates business activities by providing money and certain services that help in exchange of goods and services.According to Kinley, "Bank is an establishment which makes to individual such advances of money or other means of payment as may be required & safety made and to which individual entrust money or means of payment when not required by them for use.Commercial bank is defined as a bank or a division of a bank primarily dealing with deposits and loans from corporations or large businesses .This is what people normally call a "bank". The term "commercial" was used to distinguish it from an investment bank. Commercial banks were involved only in banking activities (accepting deposits and making loans, as well as other fee based services), whereas investment banks were limited to capital markets activities. It raises funds by collecting deposits from businesses and consumers through checkable deposits, savings deposits, and time deposits. It makes loans to businesses and consumers. It also buys corporate bonds and government bonds. Its primary liabilities are deposits and primary assets are loans. In fact, commercial banks take deposits from individual and institutional customers, which they then use to extend credit to other customers. They make money by earning more in interest from borrowers than they pay in interest to those whose deposits they accept. Liu (2004) Commercial banks are “institutions which use the funds entrusted to them by their customers to extend loans to consumers and business customers and distribute profits to the banks shareholders”. Bank and Financial Institutions Act

(BAFIA) 2064 has defined commercial bank as organization which exchange money, accept deposit, grant loan and perform commercial banking functions and which is not a bank meant for cooperative, agriculture, industries or for such specific purpose. In general, banking may be classified as retail and corporate banking. Retail banking, which is designed to meet the requirement of individual customers and encourage their savings, includes payment of utility bills, consumer loans, credit cards, checking account and Corporate banking, on the other hand, caters to the need of corporate customers like bills discounting, opening letters of credit, managing cash etc.

Banking is now an essential part of our economic system. Modern trade and commerce would almost be impossible without the availability of suitable banking services. Banking promotes investments. Banks easily invest the money they get in industry, agriculture and trade. They either invest it directly or advance loans to other investors. As per KFA Banking training manual, (2007) Banking sector is experiencing major changes as a result of economic reform initiated by government a decade ago .It has generated new and powerful customer and new private and joint venture banks. There are challenges for bankers to deliver their existing products and product in an innovative and cost effective way with the help of new emerging technology. Competition has poses challenges like market segmentation, product positioning and cross-selling. Bank has to reorganize branch network, reduce manpower, and attract talent executives. Banking sector is growing rapidly. Banks need to be efficient and competitive enough not only to the players of the banking industry but also to the non-banking financial institutions in order to attract depositors. The banks have to encourage prudent banking practices to strengthen and stabilize the financial system. Banks balance sheet position shows how effectively management has been able to manage the granting of loans to borrowers. Further KFA Banking training manual states that banking sectors has to face broadly two types of risk (i) Portfolio risk/ on –balance sheet risk are interest rate risk, liquidity risk and credit risk and other is capital risk and operational risk.(ii)Off- balance sheet risk arises due to off balance sheet activities like bank guarantee, LC or contingent claims and commitment to bank and counter guarantee.

<u>Problems in Banking sector in Nepal</u>

Basically banks in Nepal have been facing following problems in credit and investment sector. They provide loan against only fixed collateral but fails to focus on easy recovery part. Banking sector doesn’t have qualified credit staffs and credit appraisal /analysis regarding borrower and any business entity have not been done according to financial norms and internationally accepted standard. As the least developed country, everywhere we can see interference. So in the bank also the credit manger, credit analyst, credit officer are interfered in most of the cases by the member of the top management team and from the board of directors. There are few sources of getting the information about the clients like credit information bureau, bank itself and other market sources. Financial statements have also not given the real picture of the borrower’s financial status even though they are mostly audited by certified auditor.

1.1.3 Loan management

“Lending is a core function of a bank which contributes significantly to its profit. Banks lending activities are generally governed by certain principals. Since the lending activities involve the depositor’s money which is repayable on demand .Bank adheres to principal of safety and security, risk diversification, liquidity, profitability and loan purpose”

(IIBF, 2005).Loan management is simply management of loan and advances. Success of banking business depends on the efficient and effective management of loan. Poor loan management has proved to be one of the major causes of bank failure throughout the world. Thus loan management is always a challenging task in banking since it involves risk linked with credit operations. Loan management deals with minimizing those risks which are directly or indirectly involved in lending process. Lending is the principal business activity for most of the commercial banks as it provides highest return by the means of interest on loan and advances and fee on non-fund based credit activities. Banks also invest certain part of their loan in social development in the form of deprived sector lending. Effective management of loan portfolio and credit function is fundamental to bank's safety and soundness. Loan management is the process by which risk that is inherent in lending process are managed and controlled. In other words loan management is concerned with formulating and implementing lending policies. O.P Agrawal in his book "principal of banking", (Macmillan) has written that credit management is the management of credit portfolios of the bankers and financial institutions.

Loan management affects company's profitability and liquidity. The banks take care in analyzing creditworthiness of borrowing customer to ensure that the interest and principal amount on loan are timely recovered without any problem and liquidity. In short, loan mobilization and recovery are too important aspect of loan management but it also includes all the activities related with loan such as loan processing, marketing, monitoring, concentrating risk, hedging risk, and credit reporting.

1.1.6 Description of banks

Nepal SBI Bank ltd

It is the first Indo-Nepal joint venture in financial sector and an ‘A’ class licensed institution by NRB.Promoters of the bank are state bank of India (SBI),Employee provident fund(EPF),and Agriculture development bank .It was incorporated as a public limited company on April 20,1993 with authorized capital of Rs. 12 core and commence operation from July 7,1993. Under the Banks & Financial Institutions Act, 2063, Nepal Rastra Bank granted fresh license to NSBL classifying it as an "A" class licensed institution on April 26, 2006. SBI provides management support to the bank through its 3 expatriate officers including Managing Director who is also the CEO of the Bank. A core management team viz. Central Management Committee (CENMAC) consisting of the Managing Director, Chief Operating Officer, Chief Financial Officer and Assistant General Manager(Credit) oversees the overall banking operations in the Bank. ADBL divested its stake in the Bank by selling its entire 5% promoter shares to SBI on 14th June, 2009.Consequently; the Bank's corporate status has undergone change from its previous status as a Joint-venture Bank to a Foreign Subsidiary Bank of SBI(Source: website of bank).Its capital structure is as follows:

Authorized capital	2000 million
Issued capital	1661.6 million
Paid up capital	1653.6 million

Ownership structure

55% ownership was possessed by state bank of india

30 % ownership is held by general public

15% ownership is held by employee provident fund

Deposit scheme: Bank offers wide array of deposits like Current Account,Savings Account,Fixed Deposits, Swarnim Bachat,Ujjwal Bhavisya Bachat, Dhanvriddhi Bachat Yojana,Indreni Bachat ,Provident Fund Account , Swastha Bachat Khata,Varistha Nagarik Bachat,Vishesh Bachat

Loan scheme: It includes Education Loan Mortgage Loan, Mortgage plus Loan, Home Loan, Education Loan, Mortgage Loan, Mortgage plus Loan, Doctor Plus, Teacher Plus, SME Loan for Small and Medium Enterprises, Cash Credit, Project Term Loan.

Deposit collection and loan disbursement: Deposit collection of the bank up to July 2009 was Rs.27957 and Loan disbursement was Rs.15465.2 Million.

Key players:

CEO: Mr.VP Diana is the CEO of the bank.

Chairman: Mr. Bala Krishna Shrestha (B.K. Shrestha) is the Chairman of the Board of Directors of Nepal SBI Bank Limited. Mr.Shrestha has also served as a Director in various Commercial Banks and Corporate Entities, such as Premier Insurance Co. Ltd., Himal Cement Co. Ltd., Nepal Bank Ltd., Standard

Chartered Bank Ltd., etc. Mr. Shrestha is also the Chairman of Hama Group of Industries

Everest Bank ltd

EBL is a joint venture with Punjab national bank, a public sector bank of India. Bank has set up its representative offices at New Delhi (India) to support Nepalese citizen remitting money and advising banking related services. It is the first bank to bring out convertible preferences and to start banking in rural areas through agent. Everest Bank Limited (EBL) started its operations in 1994 as an ‘A’ class commercial bank with a view and objective of extending professionalized and efficient banking services to various segments of the society. The bank is providing customer-friendly services through its Branch Network. All the branches of the bank are connected through Anywhere Branch Banking System (ABBS), which enables customers for operational transactions from any branches. EBL has introduced Mobile Vehicle Banking system to serve the segment deprived of proper banking facilities through its Birtamod Branch, which is the first of its kind. EBL is first bank that has launched e-ticketing system in Nepal. EBL customer can buy yeti airlines ticket through internet. Its branches have increased to 32 till F/Y 2008-2009.Bank has been pursuing policy of not only to increase profit from year to year but consistency in its performance(Source : website of bank). Its capital structure is as follow.

Authorized capital	1000 Million

Issued capital	840.62 Million
Paid up capital	838.821 Million

Ownership structure

50% ownership was possessed by local Nepalese promoters

20% ownership is held by Punjab national bank-India

30% ownership is held by public

Deposit scheme: Bank offers wide array of deposit schemes in both local and foreign currencies. The schemes are: current account, saving account, saving premium account, fixed deposit, Cumulative deposit scheme, sunaulo bhavishya yojana, saral samridhi, bachat, unfixed deposit account, USD Account, EBL NRN Deposit, naari Bachat Khata Supreme Deposit.

Loan scheme: It includes Working capital loan, Term loan, Demand loan, Trust receipt loan,EBL home equity loan,EBL vehicle loan,EBL educational loan,EBL property plus loan, EBL professional loan scheme, Loan against share, Loan against Life Insurance Policy, Finance, Trade, Consortium.

Deposit collection and loan disbursement: Deposit collection of the bank till July 2009 was Rs.33322.9 Million whereas Loan disbursement was Rs. 24366.2 Million. Banks profit in 2008-2009 has increased to 638.7million from 451.2 million in same previous year.

Key players:

CEO: Mr. Ummat is the CEO of the bank.

Chairman: Mr. B.K Shrestha is the Chairman of Everest Bank Limited

1.2 Statement of problem

Basically banks in Nepal have been facing the problems in credit and investment sector and the present possibility for banks to diversify into wide range of services and products provides good opportunity for banking entrepreneurs and managers. But this diversification advantage is a once in a life time opportunity that should be utilized with some caution and sound management as this involves a great deal of risk. There is one saying that “the higher you go, the colder life becomes” .Banking industry is high-risk business but it is not necessary to be high profit industry. It is quite difficult to manage risk and return in banking industry. In Nepal most of the commercial banks are focusing on consumer loan, vehicle loan, real estate loan etc. However on the other part, growth of industrial loan has not been encouraging in recent years. Lack of sound knowledge and various risks associated with loan leads to unsecured loan and investment that might bring banks towards liquidity and bankruptacy.Due to transition phase, unstable government and deteriorating economic scenario Nepalese banks are reluctant to give loan to industrial and commercial sectors. So most of the banks are giving loan to profitable and unproductive sectors. More flow of loan towards unproductive sectors has become serious concern for the country. Lending policies are not systematic and co clear cut vision of policy is available on lending aspect. In Nepal it has been found that approval and lending decisions are made in favor of those persons who have personal network. So a new customer finds that loan providing process being very complicated and sometimes the documents submitted the loan sanctioning being fraudulent and for formally purpose only.

1.3 Rationale/objective of study

Banking is the activity of my interest. I have seen from the annual reports of various banks and find that most of their income is from the interest getting on the credit given .So I choose the topic loan mangement.This study attempts to evaluate loan management of EBL and NSBIL .Loan one of the most voluminous item among all the assets of the bank, the management need to be cautious while granting loan .Present scenario disclose an increasing trend of loan volumes and loan defaults for commercial banks. One of the best ways to prevent is to have proper loan management system. Keeping this in mind, I have selected the topic loan management for my research. The need for study has been justified by the following points:

- Increasing trend of loan and advances
- Rising non- performing loan of banks
- Increase in loan loss provision
- Liquidity and credit crunch problems

Main objective of research is to analyze loan management practices of commercial banks and come out with solid recommendation to enhance loan management.

However Specific objectives are given below:

1. To assess loan management process, system and practices.
2. To evaluate capability of loan management to reduce the impact of non-performing loan
3. To explore relationship between loan, deposit, invetment, income, borrowing and their impact on profit and performance of bank.
4. To analyze different benefits that the loan management might bring

1.4 Research questions

The study prepared several questions that might serve as the engine of the study. Through the use of the questions, the alignment of the study can be facilitated in aiming to achieve the presented objective. Research questions were developed to support in achieving research objectives:

1. How effectively these two banks have followed lending policies?
2. Whether trend of loan and advances and deposits are in satisfactory position or not?
3. How these banks measure liquidity and impact of loan and deposit on liquidity?
4. How bank measure lending performance and efficiency?

1.5 Hypothesis

One thesis is that research is usually begins in an uncertain and ambiguous manner. The researcher comes to know gradually what has to be done (Khaki, 2000).

1. Null Hypothesis: There is no significant relationship between loan and deposit

Alternative Hypothesis: There is significant relationship between loan and deposit

2. **Null Hypothesis: T**here is no significant relationship between loan and investment

Alternative Hypothesis: There is n significant relationship between loan and investment

3. Null hypothesis: There is no significant relationship between loan and total income

Alternative Hypothesis: There is significant relationship between loan and total income

4. Null Hypothesis: There is no significant relationship between loan and borrowing

Alternative Hypothesis: There is significant relationship between loan and borrowing

1.6 Significance of study

There are only few researches conducted on the topic loan management of commercial banks. Loan is a critical factor for the bank as it is a highest source of income for bank and affects profit and performance. Banks get highest return in the form of interest on loan. Growing competition and global financial crisis has had great impact in banking business. The loan risk has risen substantially. This has increased the importance of loan management and it is, therefore, a very current topic. Especially in the current economical situation, it is very important to have a clear and effective loan management function that can help in maximizing profits during these bad economical times. This study would be useful to all shareholders, investor and bankers. Further, this study would help other free researcher for conducting further research as it serves as a review of literature. Similarly finding of the study would be beneficial to other who is interested in knowing about this particular bank. This help to face challenges posed by other competitors and will help increase their reach by attracting new customers

1.7 Limitation of study

Since the study is focusing to partial fulfillment for the requirement course of MBS of T.U. Reliability of various statistical tools and lack of research experiences will be major limitation. Study has to be conducted irrespective of limited time and resources .Some major limitations are given below:

- ❖ Focus only on lending part i.e. loan and advances
- ❖ Due to limited time and resources, only two banks are selected for study

- The balance sheet dates of all companies are not homogeneous. In the study an effort has been made to make the data uniform by taking mid July as the fiscal year. This study will cover time period of F/Y 2002/2003- 2008/2009
- Data published from various sources differ. Figure published by NRB and other bank may not tally. So in this study NRB is taken as an authentic source of data.
- Questionnaire was distributed only to some selected branch mangers of branches located within Kathmandu valley.

1.8 Layout of study:

It is the overall structure of entire research work. This study has been categorized into five chapters

Section- I: Introduction

The first chapter deals with the introduction, background of the study, statement of the Problem, objective of the study, significance of the study, limitation of the study and layout of the study

Section-II: Review of literature:

The second chapter is mainly focused with literature review that includes a discussion on the conceptual framework on loan management and review of major studies relating with lending decisions

Section- III: Research and methodology

The third chapter describes the research methodolology used to conduct the present research. It deals with research design, sources of data, data processing, sample units, period of study, method of study and financial tools.

Section- IV: Data processing and analysis

The fourth chapter is concerned with analytical framework. It includes the analysis of financial indicators i.e. ratio analysis. Thus study use statistical tools like mean, correlation coefficient, regression and trend analysis for analyzing data.

Section- V: Summary, conclusion and recommendation

The fifth chapter includes the summary, conclusion and recommendation. The bibliography and annexes are also incorporated at the end of study.

SECTION 2

REVIEW OF LITERATURE

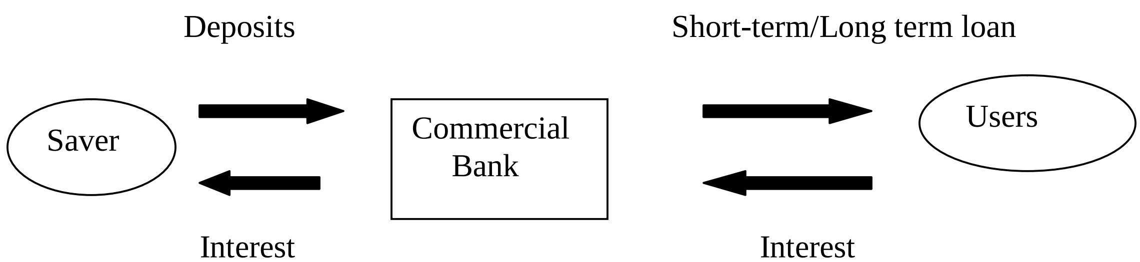
Pant (2005) has defined review of literature as a way to discover what other research in the area of our problem has uncovered. The main purpose of literature review is to find out what research studies have been conducted in one's chosen filled of study and what remains to be done (Wolf and Pant, 2003).Generally, in my thesis I am trying to describe the loan management system, practices and risk management in Nepal SBIL and EBL. I have made every possible effort to review the literature from the available sources like library, internet, books, journal, research papers and dissertations. It has been categorized into two groups:

- Conceptual framework

- Review of empirical study

2.1 Conceptual framework

Generally, in my thesis I am trying to describe the loan management system, practices and risk management in the selected sample bank. Rapid changes in banking services, high level of competition and increasing loan of commercial banks make it important to understand loan management practices in bank. The principal function of bank is to collect deposit from public and lend money to various users against specific rate of interest.



A loan is a kind of advance made with or without security at agreed rate of interest.It is the most profitable asset of the bank. So bank management always tries to increase loan portfolio in order to get more profit. The borrower initially receives an amount of money from the lender, which he pays back, in regular installments, to the lender. Borrower has to pay interest on the loan. So loan is typically the major primary source of income to banks. Though lending is the primary activity of the bank, they are very cautious in granting the loans to their clients because their funds are collected from the general public in the form of deposits that can be withdrawn at a short notice at any time. For this, the provided loan and investment should be secured for easy recovery not only backed by fixed collateral securities. This shows importance of managing lending activities for success and profit. Lending activities are guided by certain principals like principal of safety and security, principal of liquidity, principal of risk diversification, principal of profitability and principal of purpose of loan. Moreover, Bank balance sheet position shows how effectively management has been able to manage the granting of loans to borrowers. In order for the bank to secure the risks with lending, research suggests that lending decisions are based on figures in the balance sheet and income statements (Berry & Robertson, 2006; Deakin & Hussain, 1994). Such reliance on accounting data requires (i) a set of company documents compiled according to quality standards and (ii) that the information available should allow an assessment of present and future financial standing of the company (Berger and Udell, 2006). Every act of lending by a bank automatically creates the deposits that will balance it. Lending is one of the core functions of commercial bank.

Loan management is the process by which risk that is inherent in lending process are managed and controlled. It is concerned with formulating and implementing lending policies. Income and profit depends on lending and investment procedure. A sound procedure provides high return and profit. So higher the loan, higher will be profit but loan should be increased such that it is manageable. Moreover lending and investment are important not only for bank but also to the overall economic development of the country. Loan management affects company's profitability and liquidity. The banks take care in analyzing creditworthiness of borrowing customer to ensure that the interest and principal amount on loan are timely recovered without any problem and liquidity. In short, loan mobilization and recovery are too important aspect of loan management but it also includes all the activities related with loan such as loan processing, marketing, monitoring concentrating risk, hedging risk, and credit reporting. Sound loan policy can attract more customer and increase volume of deposits, investment. Every bank has its own lending policies. Lending policies provides guidelines for loan officers for granting loans. Diana Mc Haughton in her research paper" Banking institution in developing market states that loan policy should incorporate several elements such as regulatory environment, the availability of fund, the selection of risk, loan portfolio balances and term structure of liabilities. Loan management is guided by loan policy adopted by bank and help to minimize risk inherent in loan. A considered view is that banks' lending policy could have crucial influence on nonperforming loans (Reddy, 2004) .The purpose of loan management is to manage the costs and risks associated with credit .Finding the optimal level of risk and reward where the company's

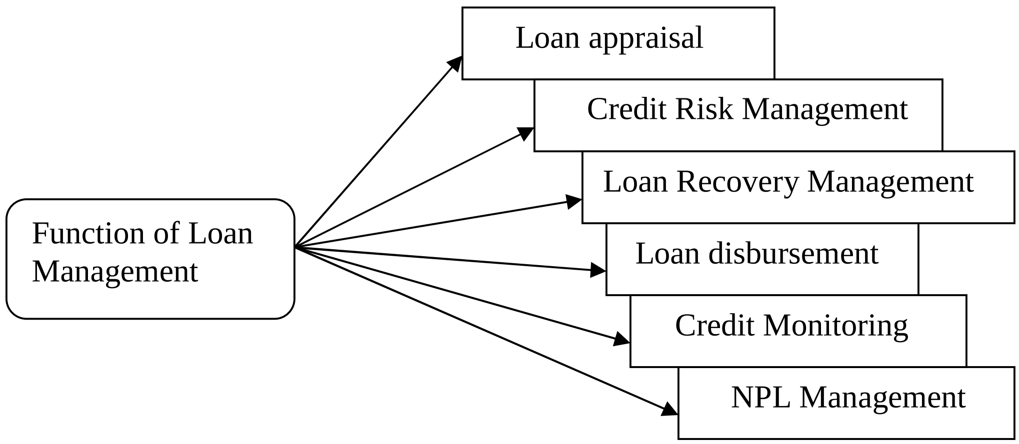
profitability and earnings are highest is the main goal of loan management. Loan management has gained more importance because credit/loan risk increases rapidly in recent days as commercial banks are increasing their loan and investment. In order to protect themselves from risks and maximize returns, commercial banks develop different tools such as loan management policies and procedures (e.g. loan appraisal policies), customer assessment systems, monitoring systems, and so on. In short, before approving loans, commercial banks assess potential risks in connection to clients ("screen" clients), and later on monitor loans.

The following statement sums up the importance of loan management. "Optimizing cash flow and avoiding bad debts are two key objectives of any successful business. Setting up a good credit control system is the starting point for both" (Directors Briefing 2006). Loan management's main objective is to try and balance the risk and reward relationship.

Loan management can contribute to the financial performance of the company. Loan officer has to assess the credit worthiness of the customer and it is based on financial information of the buyer like profitability, liquidity and financial solvency.

Loral Narayananan in her study “Effective Credit Management - 5 Keys to Help Companies Survive in the Current Economy” states two important strategies for bank to survive in market one is effective credit management for consistency in your credit and collection processes. This consistency can be achieved through well designed and actively implemented credit and collection policy. Even if you already have a credit and collection policy, it's important to review it on a regular basis to assess its effectiveness and to make sure you are following it. Second is with current customers, don't assume they're okay now because they were okay last year. Review the creditworthiness of all of your important customers. Companies that appeared secure six months ago may now be on the verge of collapse. Set up regular reviews to monitor each customer's creditworthiness to keep a step ahead of bad debt write-offs. Loan management covers the various aspects like credit appraisal, NPA management, recovery management and all the areas right form the beginning like inquiry till the loan has been paid up.

Fig.2.1.1 Functions of loan management



2.1.1Types of credit/loan

Thapa and Rawal (2010) have mentioned in their book that Credit is a kind of product which can be developed on the basis of terms and conditions demanded by the credit agreement between bank and the borrower. It can be classified as:

1. Funded

2. Non-funded

3. Working capital

4. Consumer or corporate

1. Funded loan:

It refers to the loan which is disbursed in the form of cash or any other payment. Whenever bank gives loan and cash goes out of the bank immediately, then it is called as funded loan. Some of the examples of funded loans are overdraft, trust receipt loan, importer/exporter loan, demand loan, home/hire purchase/auto loan etc.

2. Non funded loan

In non funded loan bank do not have to pay cash but need to commit a conditional payment. Some examples of non funded loan are letter of credit, guarantee, and acceptance

3. Working capital

The loan which are given for the purchase of long term assets for more than one year and repaid in fixed installment are called working capital loan. Some examples of working capital loan are project loan, home loan, hire purchase loan etc

4. Consumer or corporate loan

These loans are the loans which are granted for the consumption purpose and these loans are based on security and future cash flow .some examples are vehicle loan, personal loan.However corporate loan are the loan which are granted for big business houses. (Thapa and Rawal: 2010).

2.1.2 Credit limit

Credit limit is the maximum amount of credit a company allows its customers to owe it at any one time. (Credit Guru, 2010).Advantages of setting credit limit are:

- It frees up time for the credit managers to focus on other tasks
- It speeds up the credit process
- It reduces the risk and improves the credit collection activities
- It serves as a account monitoring tool

Credit risk is not only a way to manage credit but also to control it. If a bank decides to give credit above the limit, then loan officer should see credit worthiness of the customer. The procedure for setting a credit limit and changing a credit are defined in loan policy.

Output

Total loan

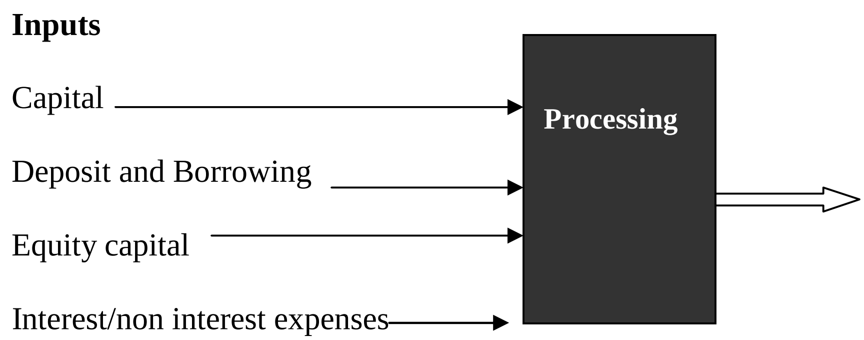


Fig 2.1.2.1 Loan management system of a commercial bank

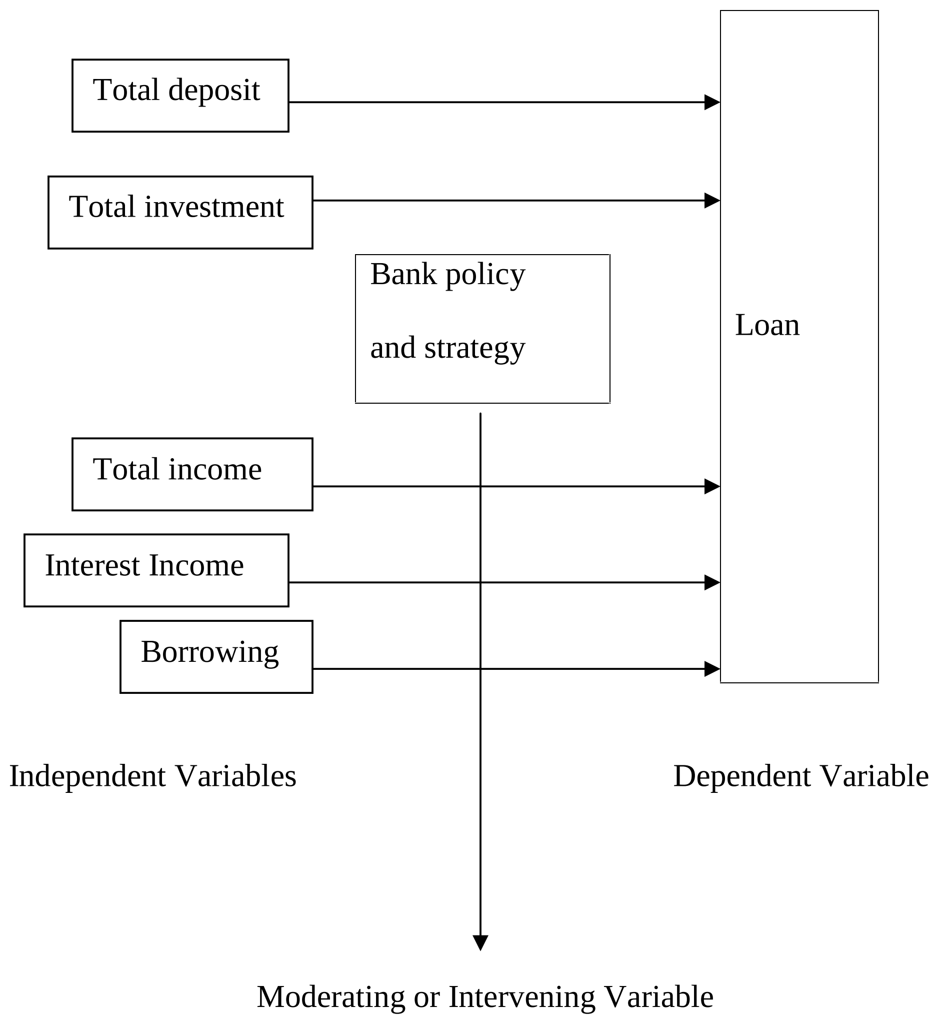
A bank's balance sheet is different from that of a typical company. You will not find inventory, accounts receivable, or accounts payable. But on assets side, you'll see mostly loans and investments, and on the liabilities side, you'll see deposits and borrowings. Loans represent the majority of a bank's assets (Saunders and Cornett, 2005). A bank can typically earn a higher interest rate on loans than on securities. Loans, however, come with risk. If the bank makes bad loans to consumers or businesses, the bank will take a hit when those loans aren't repaid. Because loans are a bank's bread and butter, it's critical to understand a bank's book of loans. Other assets, including property and equipment, represent only a small fraction of assets. A bank can generate large revenues with very few hard assets. Compare this to some other companies, where plant, property, and equipment (PP&E) is a major asset. Surprisingly, cash represents only about 2% of assets. That's because the bank wants to put its money somewhere to earn something. If the bank simply keeps its cash in its locker and forgets about it, it will not be able to earn profit. Thus, a bank keeps most of its money tied up in loans and investments, which are called "earning assets" in banking language because they earn interest. Banks don't like putting their assets into fixed-income securities, because return in these securities is not as high as compare to income from loan.

In this study functional relationship between dependent variables and independent variable has been established. So study is based on the relationship between loan of commercial banks i.e. dependent variable and independent variables are deposits, investment, income, borrowing and income. However loan is also affected by various factors like country economic situation, preferences of customer, directives of central bank and so on.

Conceptual model of the study is:

Loan = f (Total deposit, Total investment, Total income, Total Borrowing)

Fig 2.1.2.2 Conceptual framework of the study



Above figure shows that deposit, investment income, borrowing, interest incomes are independent variables whereas loan and advances is dependent variable. However bank policy and strategy has been taken as a moderating variable. Moreover, some more relationship has been established for the study such as relationship between deposit and loan, total investment, borrowing and total income. These functional relationships are analyzed through statistical tools like correlation coefficient and regression.

Primary or principal functions of a commercial bank are three types

A. Acceptance of Deposit B. Lending C. Investment

A) Acceptance of Deposit: An important function of commercial banks is to attract deposit from the public. Those people who have cash account and want their safety; they deposit that amount of banks. Commercial banks accept deposits from individual, company or business firm and take responsibility to repay the deposit in the same currency whenever they are demanded by depositors.

B) Lending: Another function of commercial banks is to make loans and advance out of the deposit receive in various forms. Bank use the accumulated public deposits to productive uses by way of loans and advances, overdraft and cash credits against approved collateral and securities. Bank's least expensive means of funding loan growth is through deposit accounts. When this is not available, banks must rely on more expensive funding sources such as borrowing funds.

C) Investment: Commercial banks are also involved in Investment. Generally investment means long term and medium term investments. It includes investment in government securities, share, and debenture of other financial institutions.

2.1.3 The Loan Policy:

The goal of every credit manager is to achieve the highest level of profitable loan, over the shortest period of time, with the minimum bad debts. In this highly competitive market for its market share it is not possible to lend loan only to solvent customer. Trading with customers that have high credit risk, needs to be profitable. For this bank should have sound policy. Loan policy is a standard and guidelines for lending decisions and activities. Loan Policies are made by Board of Directors and should communicate within the organization. So loan mobilization and recovery are two important part of loan policy. “A credit policy is the blueprint used by a loan officer in making its decision to provide loan to the customers. In order to implement credit policy to work it is essential that everybody is committed to it and everyone has to know what they are doing, why they are doing it and what are the consequences if it is not done. However loan policy should be flexible. Lending policies are based on profit maximizing of institutions and economic development of the country and it may differs from bank to bank. Some banks approach credit very conservatively, lending only to financially strong, well-established borrowers. Growth-oriented banks may approach lending more aggressively, lending to borrowers who pose a higher repayment risk. It provides a framework for achieving asset quality and earnings objectives; sets risk tolerance levels, and guides the bank’s lending activities as per bank’s strategic direction. The policy should provide a realistic description of where the bank wants to position itself. Policies should be periodically reviewed and revised to response changes in the bank’s strategic direction, risk tolerance level and market situation. NRB has sent various directives, guidelines and a circular regarding credit and this is necessary so as to use fund received as per direction set by policies .NRB time to time gives directives and guidelines on credit for safe, sound and profitable lending. So bank has to set the direction of use of fund received from stakeholders, depositors and others. The policies provide uniformity in lending activities.

2.1.4 Loan process:

The objective of loan management is to control loan approval process and achieve loan quality. However, every loan approval process should introduce adequate controls mechanism to achieve quality in credit at the time of origin. The process should be in line with bank's credit guidelines, its risk profile, and the capabilities of its lenders. The loan approval decisions are made by credit committee of a bank. Johnson and Johnson (1985), Hempel and Simonson (1999) and Koch and Macdonald (2000) pointed out that the activities in the process of commercial and industrial (C&I) loans follow eight steps; **the first step** is the application, which is conducted by a loan officer. Initially, the loan officer obtains as much information as possible about the situation of the borrower, for example, his or her previous credit history, current outstanding loans, and current financial statement and income source. **The second step** is the credit analysis conducted by the credit department. Loan officer conduct a comparative and historic analysis of the company's financial data and internal analyst prepares a recommendation report for the loan officer about whether the loan should be granted or rejected. In the **third step,** the loan officer obtains the credit analysis report and determines whether the report accurately describes the borrowing capacity and characteristics of the borrower. **The fourth step** is the loan operation. Here it is necessary to prepare primary notes, agreements, collateral or non-collateral agreements. In **the fifth step,** the loan officer obtains the borrower's signatures and receives collateral; then the loan operation is closed and the loan proceeds. **The sixth step** is the recording of the loan conducted by the loan operation and credit department staff and check whether it is within the loan policy or not. **The seventh step** is loan servicing and administration conducted by a loan operation operator, a loan officer, a credit department staff member, and a financial analyst. The loan operation staff person prepares the loan payment notices to notify the borrower and is responsible for receiving periodic payments. In **the eight steps,** the loan officer may receive periodic delinquency information and need to follow up on this with borrowers. The loan officer also needs to adjust loan terms and conditions as deemed necessary, and to take legal action if non-collectible procedures and foreclosure on the loan are followed. When the entire lending process has come to an end, the output comes with the profit earning status of the loan, which is also used to measure lending performance. Sound lending decisions are based on the 6C principles. These 6 C's are character, capacity, capital, collateral, conditions and control which are also important reference points for banks when making a credit analysis to decide whether or not a borrower is worthy of a loan. In short while approving loan bank follow following activities.

- Loan appraisal
- Loan approval,
- Documentation,
- Disbursement
- Loan monitoring
- Credit recovery

Loan officer should consider purpose of loan, source of repayment, length of maturity, financial strength and character of borrower, adequacy of capital, quality of financial statements and accounting procedures, ability to meet current obligations, quality of management, completeness of documentation, references and past credit history, quality of collateral, if any, relationship with bank in lending process.

2.1.5 Structure of asset and liabilities of commercial banks:

Banks collects funds from various sources (sources of fund) and use it in various sectors(uses of fund).The most important sources of finance for commercial banks are various types of deposit and borrowing and uses of fund by commercial banks shows total loan and advances constitute maximum share through the time period. Moreover investment on securities is the portfolio that these resources were used in. Thus loan and advances and investment stood as an important portfolio for commercial banks. Banks assets are total reserve, loan and advances, investment and other assets whereas liabilities are total demand, borrowing, other liabilities and capital.

Table 2.1.5.1 Growth of Major Balance Sheet Indicators (%)

Particulars	Mid-July								
	2001	2002	2003	2004	2005	2006	2007	2008	2009
Borrowing				12.46	23.77	34.61	22.32	17.55	12.73
Deposits	21.95	3.96	11.51	13.12	9.81	15.42	19.28	30.10	32.55
Investment	40.59	43.36	31	8.64	18.95	33.76	14.53	18.11	17.46
Loans and Advances	15.94	19.54	11.35	11.67	13.38	10.22	26.55	34.37	30.37

Source: Bank and Financial Statistics, NRB

Various research variables are reviewed in these sections which are mentioned below:

1. Total Assets:

Entry of new banks in financial system has increased business i.e. by the end of fiscal year 2008/2009 total assets of commercial banks increased by 43.30% as compared with 15.51% in previous year.

2. Loan and Advances:

One of the important functions of a commercial bank is to grant loans and advances. A loan is a kind of advance made with or without security at agreed rate of interest.Loans are debts and the most profitable assets of the banks. In a commercial bank, loan is considered as a "cow" since it provides highest rate of return than other government securities. An advance is a credit facility provided by the bank to its customers. It differs from loan in the sense that loans may be granted for longer period, but advances are normally granted for a short period of time. This is the major income earning assets of Nepali banks. Similarly share of loan and advances to total assets decreased to 49.02 % in mid-July2009 from 53.45% in mid-July2008.Data shows that loan and advances has been increasing from F/Y 2002 to 2009. As on mid July 2009, the proportion of loans, investment and cash and bank balance to total assets was 59 percent, 20 percent and 13 percent respectively (Source NRB report 2008/2009).Commercial banks in Nepal are using more funds in loan and advances rather than investment. In fact loan and advances are classified as earning assets because it earns interest, dividend and commissions. Hence in commercial banks, total of these two earning assets together was more than 80% and rests of deposit are in cash reserve, bill discounting and purchase.

3. Total Deposit:

In the words of Eugene, bank's deposits are the amounts that it owes to its customer. Survival and development of banks are mainly influenced by their ability to attract deposit. Deposits are the main inputs for loan output (Rao, 1988).It is main source of fund in order to grant loan and make investment. The very nature of the banking business is so sensitive because more than 85% of their liability is deposits from depositors (Saunders and Cornett, 2005).To collect deposit, banks provide various facilities by opening different types of accounts and offer interest on deposit. Deposits are categorized as time deposits, saving deposits, current deposits, call deposits, margin deposits, etc. Current deposits and margin are non-interest bearing deposits while all other deposits are interest bearing. Determinants of deposit are increasing saving rate, higher industrial and agricultural production and economic growth (Bhattacharyay, 1989).In Nepal deposit is in increasing trend since 2002. The deposit of the banking industry has been dominated by the savings deposit and term deposits. Deposit has occupied dominant place of 69.40% followed by and borrowing 2.26% in mid-July 2009 .However respective share of deposit, and borrowing in the previous year were 75.18% and 2.54%.This shows that commercial banks are heavily dependent on deposit and indicates increasing saving of economy(Source NRB report 2008/2009).

4. Total Investment:

Jack Clark defines investment as "a commitment of money that is expected to generate additional money". Banks invest deposits and borrowing in government securities, share, debenture that gives interest and dividend .This is secondary source of income for a bank. Investment may be on other companies share and debentures. The banks have been predominantly investing in the government securities like the treasury bills and government bonds. This investment in government securities provides liquidity benefits to the banks. The other areas of investment include inter-bank placement and investment in shares and debentures respectively. Banks are not allowed to invest in the shares and debentures of the banks and the financial institutions licensed by the NRB (Annual report, NRB: 2009). Total investment of commercial banks in mid-July 2009 is increased by 61.31%. In mid July

2009, loan and advances increased slightly at rate of 31.44% as compare to previous year. Data shows it is also in increasing trend.

5. Total Borrowing:

Commercial bank borrow fund from commercial banks, NRB, foreign banks and financial institutions and other financial institutions. One of the major sources of fund for commercial banks is to borrowing from central bank to meet their short term requirement i.e. meet day to day cash needs and to fulfill credit requirement. Bank borrows from central bank are usually based on two theories: profit and need theories. Profit theory suggests borrowing at bank rate and investing on high rate in market. Need theory suggest borrowing to provide liquidity in banking system and fill gap of credit and deposit (Sethi, 1989). Since 2002, Borrowing as a source of fund is seems to be in increasing trend .In mid July 2009 borrowing increased by higher rate of 27.15% compared to 13% in previous year. Commercial banks borrow money for purpose of investing in various sectors.

6. Liquid Fund:

Liquid fund includes cash balances, bank balances and money at call. Of the components of liquid funds, balance held abroad registered a growth of 29.9 Percent in the review year compared to a growth of 21.1 percent in the previous year. But, the growth of commercial banks' cash in hand slowed down to 18.7 percent in the review year compared to a growth by 71.9 percent in the previous year. Contrary to a growth of 5.6 percent last year, deposits of commercial banks with the NRB increased by 92.2 Percent in the review year.

7. Interest Rate:

Interests Rates of the commercial banks as on mid July 2009 are shown in the following table. Saving rates offered by the commercial banks were in the range from 2% per annum to 7.5% per annum at the end of mid July 2009. Deposit rates in saving and term deposits were observed to be in the range from 2% per annum to 9.5% per annum. Similarly Lending rates offered by the commercial banks were in the range from 6.5% to14.0% per annum.Interest rate are decided by banks depending upon on the tenure of deposit and liquidity position.

8. Total Income:

Among all the sources of income, it can be seen that net interest income (interest income less interest expenses) contributes largest followed by commission and fee based income and income from fluctuation in exchange rate. Interest income, the significant proportion of income, constituted 81 percent of total income in the review year. Banks also earn income from commitment fees which are charged on the unused portion of a loan, and prepayment penalties which protect bank's revenue .The total income of the banking industry increased by 44 percent to Rs.48.86 billion in 2008/09. Interest income, the significant proportion of income, constituted 81 percent of total income in the review year.

2.1.6 Classification of Loan and Advances

Table 2.1.6.1: Product wise Classification of Loans and Advances of commercial banks

Loan Products	Percent of Total Loan
Term loan	15
Overdraft	18.10
Trust receipt loan/Import loan	7.58
Demand and other working capital	21.64
Real estate loan	11.80
Margin nature loan	2.24
Housing loan	7.23
Hire purchase loan	6.23

Deprived sector loan Bill purchase	2.96 0.76
Other product	6.47
Total	100

Source: Banking and Financial Statistics, 2009(NRB)

2.1.7 Non performing loan (NPL):

Regmi (2059) states that growth of financial institutions and activities lend to stiff competitions within the industry which brought NPLs. An asset which ceases to generate income to the bank is called as Non Performing Assets (NPA).Using collected fund into loan generate large income for most of the commercial banks but only performing loan help in income generation .So NPAs are referred as a bad loan or prone to become bad loan having stopped giving return i.e. interest and principal in time. NRB supervision department defines NPA as “loan and advances whose credit quality has deteriorated such that full collection of principal and interest in accordance with the contractual repayment terms of the loan or advances is in question”.

Why loan goes bad? Following are some major reasons pointed out by author:

1. Lack of credit risk management strategy
2. Non acceptance of KYC concept
3. Stiff competition
4. Undue influence
5. Lack of clear credit standard.

Non-performing loans can be treated as undesirable outputs or costs to a bank, which decrease the bank’s performance and profit. Controlling non-performing loans is very important for both the performance of an individual bank and the economy’s financial environment. (McNulty, Akhigbe, and Verbrugge, 2001).A wise old banker has rightly said that “any fool can lend money, but it takes a lot of skill to get it back. Remember that no loan is free of risk and no bank would be able to continue business if it never made risky loans. Berger and DeYoung (1997) employed techniques to test the relation between loan quality and a bank's cost efficiency. They found intertemporal relationships between loan quality and cost efficiency in both directions. They indicated that high levels of problem loans caused banks to increase costs in monitoring, working out, and/or selling off those problem loans. Thus, those non-performing loans tended to decrease the cost efficiency of banks.

A. The causes of non- performing loans in banks

According to Gorter and Bloem (2002) non-performing loans are mainly caused by an inevitable number of wrong economic decisions by individuals. In their study, Fernandez, Jorge and Saurina, (2000) state that even though bank supervisors are well aware of this problem, it is however very difficult to persuade bank managers to follow more prudent credit policies during an economic upturn, especially in a highly competitive environment. They claim that even conservative managers might find market pressure for higher profits very difficult to overcome. According to a study by Brownbridge (1998), most of the bank failures were caused by non-performing loans. One of the most impacts of NPL is on bank profit.

2.1.7.1 Recovery of loan:

As Nepali saying goes “holaki bhanda gayo bulaaki”.This should be take seriously by the borrower. Loan Recovery is an important function of loan management. Every bank should have efficient and effective recovery mechanism. The core function of banks are not just taking deposit and making loan. Thus we can say that successful lending is based not on making loan but on minimizing risk in collecting them back. Even after all the efforts the banks fails to recover the loan, it can write-off the loan that meets certain requirements. This should be mentioned in loan policy and after getting approval from NRB loan can be written off. Loans that are overdue by more than 5 years should be compulsorily written off. However write off of a particular loan does not mean the borrower is free from his/her liabilities to repay the loan.

2.1.7.2 Prudential norms with regard to credit

Loan classification and provisioning enables banks to monitor quality of their lending and take remedial actions to reduce NPL.As per NRB directives bank shall classify all loan and advances into categories based on quality and time-period of credit which is given in table below. Higher non-performing loan ratio indicates worse management of assets. If the ratio is low, it indicates a favorable credit and loan management position. Non performing loan of commercial banks declined to 3.53% in mid July 2009 from 6.08 in same previous year i.e. total NPL is Rs.13574.6 million. Banks are required to create loan loss provisions on gross value of outstanding loans as per their quality of their loan portfolio. The loan loss provisions being higher than NPL indicates that the proportion of good loan is getting higher in the total credit portfolio and Non- performing loan (NPL) are getting lower. However, the NPA ratio of the private banks on mid July 2009 was 1.59 percent. However this ratio had been below 5 percent for last five years and was in decreasing trend. NPL of Nepalese Banking system is 3.53% in 2009 which is still higher than international standard. As per NRB policy research report (2007), higher level of NPL indicates the systematic crisis in financial system .It is indicator of insolvency, credit crunch, and abnormality.

- Further report mention causes of NPL. Both internal and external factors .Internal factors are risk management deficiencies in the banks and financial developments, weak corporate governance, poor accounting and auditing standard, poor recovery efforts. External factors are lack of financial discipline, weak credit culture, and political influence and connected lending.
- What has been done? NRB has introduced a number of policies to mitigate the problem of NPL through various directives.

2.1.8 Credit risk management (CRM):

The core function of bank is not just taking deposit and making loan. For most banks, loans are the largest and most obvious source of credit risk because credit risk arises from non-performance of borrower. Successful lending is based not on making loan but on minimizing risk in collecting them back. Commercial banks lending involves credit risk in their loan portfolios. So there is need of credit risk management. Dahal (2002) defines credit risk as a risk of non-payment of interest and principal by the security issuer. As per Sim (2006), prior research finds that banks manage credit risk for two main purposes: to enhance interest income (profitability) and to reduce loan losses (bad debts) which results from credit default. Credit risk management has to be based on knowledge for it to have any real meaning. Edwards says in his book that everybody from the Chief Executive should understand that:

“Credit means trust and trust has to be based on knowledge for it to have any real meaning.”(Edwards 2004) Gathering, analyzing and making decisions based on that knowledge is credit management. The credit risk management process can be divided into five phases (Weber and Fenchel, 2008). In the rating phase, borrower creditworthiness is evaluated together with personal credibility in order to determine probability of default, i.e. probability that borrower will not be able to repay the loan.

In the costing phase, banks quantify expected losses based on identified probability of default and some other factors. In the pricing phase, the identified costs (expected losses) are incorporated in the loan conditions: the borrowers are charged based on their expected losses in order to compensate for lending losses. In work-out phase, so-called bad loans (loans that can not be paid back fully) are managed with the aim to reduce the losses or work on getting borrowers to remedy their financial situation. CRM is concerned with identification, measurement, monitoring and control of the credit risk. Banks perform credit risk analysis which can be defined as the possibility that a borrower will whether fail or not to meet its obligation in accordance with the agreed terms. Bank collects deposit and lends it making money with the spread interest rate between the deposit and loan. In such a circumstances the deposit raised by the banks are payable under any situation, but the loans that have been disbursed may not come back which could lead the bank to lose money. If we see banking industry world wide credit risk weighs 55-65% of total risk. However in Nepal credit risk weighs almost 80% of total risk" (Boss Magazine: 2010). Each bank should set risk limit after assessing its risk and the risk bearing capacity. The task of risk management should be given to independent risk management committee which identifies monitor and measure risk.

David and Dionne (2005) have found in their research just having credit evaluation in order to reduce risk nay not sufficiently reduce total portfolio risk. In order to minimize this risk bank has to diversify its loan portfolio.

Rose (2002) has given some indicators of credit risk:

- Ratio of NPL to total loan
- Ratio of annual provision for loan loss to total loan.

CRM can be done with sound loan review and internal credit risk rating system and credit officer can examine as many points as possible but must include basic five Cs are; character, credibility, capital, collateral and cycle (economic conditions) while giving loan to customer's and consequently can earn more interest and reduce bad debts(NPL). As per risk management guidelines issued by NRB, credit risk does not necessarily occur in isolation. The same source that endangers credit risk for the bank may also expose it to other risk. For instance a bad loan portfolio may attract liquidity problem. In fact loan department of every bank should monitor and manage concentration risk so as to ensure that loan has not given to limited sector or persons.

2.1.9 Directives of NRB in respect of lending activities of commercial banks:

a) Deprived sector lending of commercial banks:

With a view to provide freedom to commercial banks in the selection of their loan Portfolio, NRB phased out the priority sector-lending program since 2007/08. However, the NRB has continued deprived sector lending program in order to outreach credit access to the marginalized, backward, minorities, dalit, scheduled caste and deprived people. Banks are required to disburse at least 3% of their total loan portfolio in the deprived sector as directed lending.

b) Margin lending:

The amount of margin lending against the security of shares must be within the limit of fifty percent of the average of closing share price of 180 working days or fifty percent of the current market price, whichever is the lower. If value of the shares in collateral falls below 50 percent of the limit due to the changes in price of the shares, banks should make a margin call to the concerned borrowers limit. If the borrowers are unable to deposit the margin in the given period, banks and financial institutions should initiate to sell such shares to recover the loan within seven days after the given period. If shares are not sold through the secondary market, banks and financial institutions must maintain 100 percent loan loss provision for such lending.

c) Restriction on credit (loan):

Diversity of risk is a fundamental principal of sound CRM. Banks must not over-impose to a particular sector and to a group of borrower. In order to minimize credit risk NRB has imposed restriction on credit to companies, individuals, and firms black listed by credit information bureau (CIB), until they are lifted from the list. Rapid growing concern over the loan exposure of financial sectors on real estate and housing loan, Nepal Rastra bank issued a directive according to which, financial institutions now cannot lend more than 25 percent on real estate sector and their exposure to real estate and housing loan should not cross over 40 percent. The NRB also instructed the financial institutions to lend money for housing and real estate not exceeding 60 percent of the fair market value of the property. As per the NRB directives, financial institutions have to reduce real estate loan to 15 percent by mid-July 2011 and to 10 percent by mid-July 2012. Similarly financial institutions have to downsize both real estate and housing loan to 30 percent by Mid-July 2011 and to 25 percent by mid-July 2012. As per NRB estimates, the commercial banks have invested 20 percent on average in the real estate sector. Some of the banks have even higher percentage of exposure in the real estate. According to NRB, out of 26 commercial banks, seven have invested more than 25 percent of the total loan in real estate sector.

2.2 Review of Empirical study:

This part includes review of books, article, previous studies or review of thesis.

2.2.1 Review of article

Godwin Norense and Osarumwense Asemota (2009) has clearly mentioned about loan management model in the article "Approximate Maximum Likelihood Commercial Bank Loan Management Model" that the socio-economic conditions surrounding the operations of a commercial bank are dynamic. These will affect the amount of loans commercial banks can offer and also the amount of cash balances at their disposal. A bank's market share determines to a large extent its ability to diversify its portfolio. This is due to that fact that, public confidence has to be maintained. Loss of public confidence will arise if the bank is unable to honor depositor's withdrawals. To a certain degree, the market share determines the portfolio diversification, which the Central Bank (consequence of reserve requirements) will allow the bank. The demands for loans are always on the increase as the economy expands. Thus, any attempt to develop a model for credit lending must include uncertainty factor, to account for loan management dynamics. Further, the availability of cash and loanable funds are important to the successful operations of a commercial bank. However, if there is excess cash, it could lead to a waste of resources unless properly channeled in to loans. As a result, a commercial bank has to hold a certain amount of cash that will meet with depositors withdrawal requirements and other liquidity needs of the commercial bank”

Further he has used stochastic loan management model which describes the dynamic behavior of a commercial bank. The following equations can, therefore, be considered:

W x|C ⊓|In (1)

L D x|D Γ|W Z|R (2)

L x|ℑ|D (3)

Where:

DL = Deposit liabilities

W = Net worth

C = Capital

In = Retained Reserve

R = Reserve as prescribed by the Central Bank and also affected by the frequency of withdrawal by depositors

L = Amount of loans

D = Disposable assets

ℑ = Fraction of the disposable asset, that can be given out (0<ℑ<1)

Model developed in this research should be more useful to commercial banks operating in large cities and heavily industrialized areas, because they are more susceptible to disturbances and random fluctuations than are rural or semi-urban banks. This assertion is essentially so, because it would be a credible cash deposit base measuring instrument for assessing both the assets and liability positions of the commercial bank for timely and quality decision making capabilities. Additionally, it will be a valuable tool in the planning and policy decisions of bank managers since it will enable them determine excess cash, which could be invested as loans to earn more assets without jeopardizing public confidence.

Ramesh lal shrestha in his article “A study in deposit and credit of commercial banks in Nepal.” concluded that credit deposit ratio of would be 51.30% if other things remaining same in 2004 AD which was the lowest under the period of review. So he suggests that the commercial banks should try to give more credit entering new fields as far as possible.

Jahangir, Shill and Haque (2007) stated that the traditional measure of profitability through stockholder’s equity is quite different in banking industry from any other sector of business, where loan-to-deposit ratio works as a very good indicator of banks' profitability as it depicts the status of asset-liability management of banks. But banks' risk is not only associated with this asset liability management but also related to growth opportunity. Smooth growth ensures higher future returns to holders and there lies the profitability which means not only current profits but future returns as well. So, market size and market concentration index along with return to equity and loan-to-deposit ratio grab the attention of analyzing the banks’ profitability.

Radhakrishna Poudyal (2003) in his article “Bank credit and debt recovery” states that “Bank create credit mainly out of deposit, shareholder’s capital, own borrowing and begin with the client prepare credit proposal and submit it to the board, subsequently bank completer appraisal of proposal,approve credit-limit and disburse installement.Bank credit should be recovered from the client in time and fetch return in the form of interest”. Loan management includes credit policy of respective financial institutions; its loan approval process, documentation, stipulation of the disbursement procedure, project appraisal system, additional collateral, loan monitoring and follow up, legal consideration etc.Bank and financial associations generally base their loan approval on the basis of credit appraisal report (ibid).

Dahal (2009) giving a short glimpse on his article “Experience of the Nepalese Commercial Banks and Challenges Ahead” figured out following:

“It is sad to note that collateral based lending instead of cash flow based lending is still prevalent. This speaks the need of a comprehensive risk management system in a bank. All the bank need to work in this direction to assure the public that they have adopted all the possible measures to keep their money safe. Moreover, regulating authorities should create an environment whereby the banks can make lending decisions based on the financial statement of the borrowers”

Khadka (2007) in his article “Analysis procedures in Nepalese bank and financial institution” says that lending portfolio of the banks will also be high within the limited business group that certainly increases concentration risk of the bank. Besides some commercial banks, almost all other more than 75% lending goes among top groups. This in fact nothing but a name lending which doesn’t scan business virus.

Article “Credit as well as credit risk management in banks” published in **ICAI journal (2005)** mention that it is very much essential to conduct credit investigation before taking up a proposal for consideration. This preliminary study should lead to valuable information on borrower’s integrity, honesty, reliability, credit worthiness, management competency, expertise, associate concern, guarantor, etc. A due diligence report shall invariably accompany the credit proposal evaluation. Banks have to strictly adhere to the KYC (Know Your Customer) norms to ensure bonafide identification of borrows and should also follow the prescribed Fair Practice Code on Lenders Liability, by evolving their own best practices to be followed by the field functionaries, so as to avoid complaints from customer at a later date. This article attempts to focus on not only credit management but also credit risk management. Till recently, all the activities of banks were regulated and hence operational issues were not conducive to risk taking. The financial sector, now, wears a relaxed and liberated look. Banks have grown from being a financial intermediary, in the past, to a risk intermediary, at present. In credit, risks are co-related and exposure to one risk may lead to another having deeper ramification and hence, the real mantra for prudent banking lies in successfully managing the risks in an integrated and pro-active manner to optimize the exposure already taken or to be assumed by the bank

Henri Heinola has expressed his view in the research report " credit management of bank" in this way:- "Usually, it is thought that credit management's main objective is to avoid any bad debts but this is not true, especially when a company's goal is to maximize profitability and sales. The company might incur some bad debts but the additional sales would make it worthwhile to the point where the profits from the additional sales cover the bad debts incurred."

Edwards (2004) in his article Credit management needs to weigh the benefits of giving credit to the risks associated with it. Money costs money so there has to be benefits involved in giving credit to a customer in order to be able to manage with the costs that giving credit generates. (Edwards 2004, 19) Edwards says, "The best thing would be for everyone to be able to accept the definition of credit as being something (money) which is bought from a supplier, at a price, in just the same way as any other goods or services are bought".

Thapa (2008), Deputy Director of NRB, Bank and Regulation Department says in his article "financial inclusion" that access to credit is not sufficient indicator of financial inclusion. There could be multiple level of financial inclusion. The commonly used normal indicators are bank branch network, deposit and loan account, availability of appropriateness and importantly various social indicators. Further he indicates as per priority sector lending policy, commercial bank, development bank and finance companies are required to lend 3%, 1.5% and 1% of their total outstanding loan to underprivileged people of society.

Alan (1990) clarifies the relationship between credit crunch and bad debts. According to him a credit crunch is a situation when financial intermediaries particularly banks becomes reluctant to lend to private sector. Many of the conditions of credit crunch were present in us in the early 1990s and are still predominant in Japan owing to the escalation of bad loans and the reluctance by banking sector to flow credit to private sector.

David Woo (2001) in the article written by him entitled" Two approaches to reduce NPL during financial crisis", published by IMF in the book "Building strong banks through surveillance and resolution". According to him NPL are generally a manifestation of weakness in the corporate sector (obligor of the asset) and immediate source of problem in the financial sector(holder of the assets).Effective assets management policies need to be recognize these linkages and the interdependence between two sectors .In this sense, assets management policies can't be independently formulated and must be convinced in the context of a comprehensive framework for the restructuring of financial and corporate sectors.

In a study of loan losses of US banks, **McGoven (1993)** argued that 'character' has historically been a paramount factor of credit and a major determinant in the decision to lend money. Banks have suffered loan losses through relaxed lending standards, unguaranteed credits, the influence of the 1980s culture, and the borrowers' perceptions. It was suggested that bankers should make a fairly accurate personality-morale profile assessment of prospective and current borrowers and guarantors.

As per IMF report (2008) nearly 60% of bank loan are secured by real estate .However Nepalese banks are giving small portion of loan as keeping stock as collateral i.e. only 3% of total loan.

2.2.2 Review of Thesis:

This part includes review of studies conducted by other previous researcher, their objectives and finding in the related topic.

Shrestha (2005) in her thesis entitled "Credit management with special references to Nepal SBI bank" has set following objectives:

- To analyze effectiveness of credit policy
- To Measure the credit performance
- To measure the liquidity position

Research finding are;

- Increasing growth ratio of deposit, loan and advances and investment shows good performance and the major portion of non interest bearing deposit consists of current deposit and this deposit is particularly maintained by business enterprises.

Increasing loan and advances and investment to total deposit ratio of the bank shows there is not maximum utilization of the fund.

- Due to increasing volume of loan and advances, the provision for doubtful debts is also increasing during the study period
- The studies shows low contribution made by lending and investment and high contribution by other fee based activities in total income and significant relationship between deposit and loan shows that bank is successfully mobilizing deposit as loan
- NPL is in decreasing trend and bank has given priority to industrial and commercial sector lending and has good lending procedure

Bista (2010) has conducted research in the topic "Loan management of SCBL and NABIL banks" .His research objectives are;

- To examine trend of the deposit and loan of SCBL and NABIL
- To study liquidity position and its impact on loan.

Major finding are

- The liquidity position of Nabil and Standard chartered bank are normal.
- There is high degree of correlation between deposit and loan and advances of SCBL and low correlation in respect of NABIL. So SCBL has mobilize its deposit as loan successfully
- SCBIL bank deposit was not successfully mobilized in income generating sector.

Lamichana (2008) has conducted thesis in the topic "A Comparative study of deposit mobilization of HBL and EBL" .Research objectives are

- To find out relation between total deposit with loan,total investment,net profit and interest rate
- To analyze the proportion of the loan and advances of EBL and HBL
- To find out investment volume of EBL and HBL

His research findings are

- Contribution of deposit to net profit is higher in banks
- EBL has highest capacity to repay its short term liabilities since it has strong liquidity ratio .so overall activity ratio of EBL is better than HBL. It shows how effectively the bank is managing its resources
- Earning capacity of EBL is better than HBL because as per research profitability ratio of EBL is high.

Kafle (2009) in his research entitled Non-performing loans of Nepalese commercial banks has objectives as follows

- To know the problems of the non performing loan(NPL) and its effects in the ROA and ROE of the commercial banks
- To find out whether the Nepalese commercial banks are following the NRB directives regarding loan loss provision for non performing loan or not.
- To make necessary suggestions and recommendations

He found that no banks have been following NRB directives regarding loan loss provisions. He also concludes that the return on assets (ROA) and return on equity (ROE) of bank depends on NPL. Similarly, High degree of negative correlation coefficient between NPL and ROA and the NPL and ROE clearly indicates that there is inverse relation between them.

Dhunghana (2002) has conducted research in the topic Comparative study on investment policy of Nepal Bangladesh Bank and other Joint venture Banks tries to compare the investment policy of NB Bank with HBL and SBI has following objectives

- To study the fund mobilization and investment policy with respect to fee based off-balance sheet transaction and fund based on balance sheet transactions.
- To evaluate the liquidity, efficiency of assets management and profitability position, the trend of deposit utilization towards total investment and loan and advances, growth ratios of loan advances and total investment with respect to growth ratio of total deposit and net profit.

The major findings of the study are

- NBBL has not good deposit collection, it does not have made enough cash and bank balances .It has made negligible amount of investment in government securities.
- The asset management ratios were highly variable which reveals NBBL has not followed stable policy.
- NBBL ratio of OBS operation to loan and advances lower than that of HBL but its ratio is greater than that of NSBI.
- profitability position of NBBL is comparatively not better than that of HBL but better than NSBI
- The credit risk of NBBL is higher than that of HBL and NSBI. Bank profitability solely depends on interest charged by bank but the high interest rate risk of NBBL shows that bank is failure to maintain this. Trend of deposit collection, investment and net profit of NBBL were not better than HBL but better than NSBI

Bhandari (2004) has conducted research in the topic Investment policy of commercial bank with special references to NSBI has objectives as follows:

- To evaluate liquidity, assets management efficiency, portfolio management and profitability position
- To analyze deposit utilization and its relation with investment and profit
- To determine growth rate of deposit, loan, investment, and profit to determine proportion of loan loss provision to total loan
- To evaluate NPL of NSBI

The following are the major finding of the study

- NSBI has good liquidity position.
- From analysis of assets management, bank has utilize about 80% of the deposit into income generating assets and most of them are in the form of loan Similarly.60% of total assets are used for income generating purpose but rest fund are ideal. So it shows lack of policy for proper utilization of costly fund.
- From activity ratio view, quality of loan becoming deteriorating and NPL is also increasing.
- Following stable lending policy, most of the loan is given to industrial and commercial purpose.
- From profitability view, interest income has contributed more than 8% to total income of bank while fee-based OBS transactions has contributed only 6%.Only 3% income is generated from the investment made by the bank. Return on loan,

total income to total assets ratios are in decreasing trend. So investment policy is not appropriate.

- Deposit collection is in increasing trend but loan are increasing aggressively than deposit collection. The growth rate of loan is about 70% more than the rate of growth of deposit.
- There is strong positive correlation between loan and advances and deposit

Gupta (2003) has conducted research in the topic Deposit and reinvestment problem of Nepalese commercial banks with special references to NSBI and EBL

Research objectives are

- To study deposit position of banks
- To analyze reinvestment position
- To analyze gap between deposit and loan and advances

The major findings of the study are

- Most of the deposits are idle and banks are investing these funds in other sectors as government securities at maximum of 4% interest rate while the cost of fund are bearing is 6%.
- SBI deposit increased highly from 1997-2001, which leads to improve bank policy. Investment of SBI is also fluctuating highly during the study period.
- Percentage growth in loan and advances of NSBIL is lower than investment.
- Liquidity position of EBL is slightly better than SBI, EBL has made enough investment on government securities and maintain moderate investment policy

- From assets management, EBL is comparatively successful in managing its assets as compare to NSBIL and from results of profitability and risk; EBL is in better position than NSBIL.
- There is significant relationship between deposit, investment and loan of NSBIL and EBL

Khanal (2005) in his thesis entitled Impact of NPL on the performance of Nepalese commercial banks with special reference to Nabil,NIB, EBL,NSBL and BOK

Research objectives are

- To present and analyze data relating to NPL and performance of sample banks.
- To find out solution to minimize NPL

The major findings of the study are

- It be said that economic slowdown and recession, overvaluation of properties provided as collateral, family credit analysis and decision, negative attitude of borrower are major causes of NPL in Nepalese commercial banks.
- It was found that no banks have been maintaining loan loss provision as per NRB directives. comparison with
- It was found that no banks have been maintaining loan loss provision as per NRB directives
- There is negative correlation between NPL and loan and advances of NBL, NIBL, NSBI, EBL which indicates green signal that NPL of these banks are decreasing with increment in loan

Regmi (2004) has conducted thesis in the topic Study on credit practices of joint venture commercial banks with special references to NSBIL and NBBL"

Research objectives are

- To analyze the portfolio behavior of lending and measuring the ratio of loan and advances made in different sectors
- To determine the impact of deposit in liquidity and its effects on lending practices
- To examine lending efficiency and its contribution in profit
- To analyze trend of deposit utilization towards loan and profit.

Major finding of the study are

- Liquidity position of NSBIL is higher than NBBL
- NBBL asset management is better than NSBI but total investment of NSBIL is higher than NBBL.
- NBBL has more credit flow to government enterprises than EBLL
- Average ratio of loan loss provision to total loan of SBI is higher .Credit risk of NSBIL is high and operating performance of NBBL is better than NSBIL.
- There is significant correlation between deposit and loan of both bank and between total income and loan.
- In case of SBI, there is no significant relation between loan and profit.
- Trend of deposit and loan of both banks are in increasing trend.

Maharjan (2005) has conducted thesis in the topic Loan management of Nepalese commercial banks (with special references to BOK, NSBIL, NABIL and NIBL)

Research objectives are

- To examine trend in deposit and loan and understand level of NPL
- T o examine investment made by sample banks in priority and deprived sector

The major findings of the study are

- Sample banks has not made investment in priority and deprived sector upper NRB directives.
- Deposit growth rate of NSBI on an average during F/Y 2000-2004 remain poor. But loan trend was little bit satisfactory
- All the sample banks except BOK failed to reduce NPL as of international acceptable norms
- NSBIL was unable to maintain loss provision for other types of loan except pass loan.
- Simple regression analysis shows that variables ROA and ROE depends on the level of NPL and loan loss provision

Poudel (2002) has conducted thesis in the topic a study on liquidity and investment position of EBL and Nabil banks

Research objectives is to examine the investment and liquidity policy of EB L and Nabil

Finding of the study are

- In aggregate, liquidity position of EBL is comparatively better than Nabil.
- EBL has not been successful for mobilizations of fund on investment. Most of the funds of EBL are invested in government securities.

2.2.3 Review of books:

In this section, I have reviewed the various books relevant to my studies .Loan management and implementations of sound policies are among the most important responsibilities of banks directors and management. Well conceived lending practices are essentials if a bank is to perform its credit creating function effectively and minimize the risk inherent in any extension of credit." he further adds that the formulation of lending policies for all the banks should have adequate and careful consideration over community needs, size of loan portfolio, Character of loan, credit worthiness of borrower and assets pledged to security borrowing, interest rate policy etc.

Edwards (2004) in his book Credit management handbook has express his view that credit management needs to weigh the benefits of giving credit to the risks associated with it. Money costs money so there has to be benefits involved in giving credit to a customer in order to be able to manage with the costs that giving credit generates. Edwards further says, "The best thing would be for everyone to be able to accept the definition of credit as being something (money) which is bought from a supplier, at a price, in just the same way as any other goods or services are bought". In order to avoid unnecessary bad debts and costs related to late payments, it is important to assess the credit worthiness of a customer. He further states that there are two main reasons for customers' credit worthiness evaluation, profit reasons and sales reasons. By profit reasons, he means possible delays in payments or bad debts that affect the profits and by sales reason he means that it is also useful to know the ability of the customer to buy your products.

The Chartered Institute of Management Accountants has published a case about improving cash flow using credit management where they suggest using the 80/20 rule and prioritizing the research on customer credit worthiness based on that. “The 80/20 rule suggests that 20% of your customers will generate 80% of your revenue, so it is suggestible to list accounts in descending order of value and give the top slice a full credit check on a regular basis. The smaller ones do need attention, but are a lower priority, unless monitoring reveals poor payment performance.” (The Chartered Institute of Management Accountants has published material about improving cash flow using credit management2009).

Mittra (2003) has mentioned in his book that changes in loan and investment largely determine changes in volume of total bank deposit .When commercial bank increase their total loan and investment, there tends to be corresponding increase in bank deposit. He tries to mention relation between loan and deposits of the bank.

AS per Comptroller’s Handbook (1998), Loan portfolio management (LPM) is responsible for determining whether the bank has an effective loan portfolio management process. The historical emphasis on controlling the quality of individual loan approvals, minimizing risk and managing the performance of loans continues to be essential. But better technology and information systems have opened the door to better management methods. To manage their portfolios, bankers must understand not only the risk posed by each credit but also how the risks of individual loans and portfolios are interrelated. Until recently, few banks used modern portfolio management concepts to control credit risk. Now, many banks view the loan portfolio in its segments and as a whole and consider the relationships among portfolio segments as well as among loans. These practices provide management with a more complete picture of the bank's credit risk profile and with more tools to analyze and control the risk. LPM includes determining whether the risks associated with the bank's lending activities are accurately identified and appropriately communicated to senior management and the board of directors, and, when necessary, whether appropriate corrective action is taken. Banks should assess the risk/return relationship at both the individual loan and portfolio level. In addition to establishing strategic objectives for the loan portfolio, senior management and the board are responsible for setting risk limits on the bank's lending activities. Risk limits should take into consideration the bank's historical loss experience, its ability to absorb future losses, and the bank's desired level of return.

Rose, kolari and Fraser (2002) in the book, financial institution: understanding and managing financial services says: "Banks earn interest on loans and investments; they pay interest to the depositor when interest rate changes there may be an effect on income if a bank holds rate sensitive assets.: and liabilities .If for example a bank holds more rate sensitive assets and liabilities when interest rate rises, profit will improved because the bank will receive more in increased interest revenue than it will pay out in rising costs. The reverse would be true during a period of falling interest rates".

Bank and financial institutions also tends to borrow short and lend long. In other words, funds are borrowed from depositor for short period than they are lent to consumer in doing so bank maximize their profit from interest rate differentiation between higher long term and lower short-term interest rate **(NRB Samachar, 2062)**

2.3 Research Gap:

In recent years, financial scenario and financial performance has been changed due to entry of number of banks and financial institutions in the country. So competition has pushed banks to adopt differentiation strategy to compete and survive in the market. Thus it is essential to make study effectiveness of loan management of commercial banks by taking sample of Everest and SBI banks to support in fulfilling research gap. There are lots of article on investment policy of banks, loan and deposit of commercial banks but nobody has made study in loan management with references Everest and SBI banks.

SECTION 3

RESEARCH METHODOLOGY

Kothari (2009) says Research methodology is a way to systematically solve the research problem. Thus when we talk of research methodology we not only talk of the research methods but also consider the logic behind the methods we use in the context of our research study and explain why we are using particular method or techniques so that results are capable of being evaluated either by the researcher himself or by other. Whatever research methodology is adopted for the research, reliability and validity issues have to be considered (Creswell 2003). Reliability and Validity are tests of the trustworthiness of the measurement instruments used in research (Babbie 2000).

This chapter includes research method used to conduct research on the selected topic, research design, sources of data, period of study and method of analysis. The study is based on historical data disclosed by annual report of NRB. Comparison of these two banks will be done only after 2002/2003 and most of the commercial banks have yet to hold the annual general meeting for the F/Y 2009/2010. So study will include data of F/Y 2002/2003 to F/Y 2008/2009.

3.1Research Plan and Perspective:

In order to make study reliable and valid, method and analysis used will be carefully planned and emphasis will be given while designing questionnaire. This help to reduce personal bias, error of observer and participant's bias. Regarding research perspective I will also be analyzing and describing how loan management affects banking performance and banking services.

3.2 Research Ethics:

The research will include primary data, but it will not include any personal information on individuals. Before sending out the questionnaires, I will check them with my supervisor. There is no any personal undue pressure during my entire research work and all participants who are involved in this study were fully informed about the objectives of the study.

3.3 Research Design:

Research work is designed to obtain answer of all research questions. Research design is an overall framework or plan for the activities to be undertaken during the course of a research study. This research has adopted descriptive and analytical research method to analyze and interpret data. A descriptive study is chosen to describe characteristics of the population. The questions to be asked in descriptive research are how/ or what. Loan management falls within this framework. This method is used to describe the nature of a situation, as it exists at the time of the study and to explore the cause/s of particular a phenomenon. The aim of descriptive research is to obtain an accurate profile of the people, events or situations. The descriptive method is advantageous for the researcher due to its flexibility; this method can use either qualitative or quantitative data or both,

3.4 Population and Sample:

Population of interest is called target population. In this study target population is chosen from banking industry**.** Presently there are 27 commercial banks operating in Nepal.

These banks are population for the study and sample of two banks are taken using random sampling method in order to achieve objectives .Convenient sampling techniques have been adopted to conduct this study. As per Baskota (2004) sample is any number selected to represent the population according to some rule. Selecting a sample means selecting elements from target population for the ultimate purpose of drawing general conclusion about the entire number of elements.

3.5 Nature and Sources of Data:

In order to meet research objective, data which has been collected for the analysis purpose are of primary and secondary in nature but study is more based on secondary data. Primary data collected through questionnaire are of qualitative nature.

3.5.1 Primary Data:

Primary data has been collected from instrument i.e. structured Questionnaire(containing 21 questions) which was distributed to 10 branch managers of each sampled banks within kathmandu valley. Out of 20 distributed Questionnaire, only 16 Questionnaire were returned. Standard Questionnaire was designed by using five point likert scales, ranking scale and multiple choice-type questions. However due to qualitative nature of data, 5 point likert scale has been extensively used to get answers of the respondents. The questionnaires will be sent by e-mail. I will send the questionnaires well in advance, to ensure the time will be enough for the respondents to fill them in and for me, to analyze them.

3.5.2 Secondary Data:

Secondary data is the data that already exists which has been collected by some other person or organization for their use, and is generally made available to other researcher free.Secondary data has been downloaded from www.nrb.org.np, an official web site of

NRB.This study is based on the historical data disclosed by annual reports of commercial banks and Nepal Rastra Bank. In addition, some other data has been collected from journal papers including both online and journal papers sourced in the library, books, the Internet, magazines and newspaper articles and official statistics. However, secondary data may not always answer that specific question of a research

3.6 Research Variables:

For the sake of simplicity of entire research process only one independent variable i.e. loan has been considered for analytical purpose .Similarly deposit, investment, income, interest and borrowing have been taken as independent variables. In between these dependent and independent variables, bank policy and strategy is considered as moderating and intervening variables. Relationships between these variables are studied in correlation and regression analysis.

3.7 Data Analysis

Data analysis consists of categorizing data, coding them, tabulating and then drawing statistical inferences keeping in mind the objectives to be fulfilled. It includes closely related operations like summarizing the collected data and organizing in such a manner that they will yield answers to the research questions. This study has used percentage, graphs, tables, charts, correlation and regression analysis for analysis of data collected. **SPSS software** is used for the results of correlation coefficient and regression. The study has used financial and statistical tools to analyze data.

3.7.1 Financial Tools

Financial tools include ratio analysis and various ratios are calculated by using financial statement of selected banks which helps to determine organization profitability, leverage, liquidity and performance. A ratio may be defined as a fixed relationship between two numbers. Ratio analysis is a process whereby key figures are related to each other and compared over different accounting period or compared with ratios derived from other companies, particularly those in the same or similar business." They are simple to calculate, easy to use, and provide a wealth of information that cannot be gotten anywhere else," James O. Gill noted in his book Financial Basics of Small Business Success. But, he added, "Ratios are aids to judgment and cannot take the place of experience. They will not replace good management, but they will make a good manager better. However, financial ratios are short term measure of performance and are not appropriate for the measurement of long term performances of bank (Sherman and gold, 1985: oral and yolalan, 1990). The basic inputs to ratio analysis are from the banks income statement and balance sheet. Ratio can be expressed in terms of percentage, times, proportion and quotient.

Lending Efficiency Ratios

1. Loan Loss Provision to Total Loan Ratio
2. Non Performing Loan to Total Loan Ratio

Asset Management Ratios

3. Loan and Advances to Total Deposit
4. Investment to Total Deposit Ratio
5. Loan and Advances to Total Assets Ratio

Profitability Ratios

6. Interest Income to Total Income Ratio
7. Interest Income to Interest Expenses Ratio
8. Interest Income to Total Assets Ratio

Leverage Ratios

9. Total Borrowing to Total Assets

10. Total Liabilities to Total Capital Ratio

Liquidity Ratios

11 .Cash and Bank Balances to Total Deposit Ratio

12. Balance with NRB to Total Deposit Ratio

13. Liquid Fund to Total Deposit Ratio

Growth Rate

14. Growth of Total Deposit

15. Growth of Loan and Advances

16. Growth of Total Investment

17. Growth of Total Income

18. Growth of Borrowing

1) Loan Loss Provision to Total Loan Ratio

Control of loan loss ratio is an important part of loan management and banks always try to minimize it. Poorly administered loan management has significant impact on earning and capital. This ratio indicates adequacy of allowances for loan and trend in collecting loan and the performance .It is obtained by the ratio of loan loss provision to the total loan. It is computed as follow:

$$Loan\,loss\ provision\ \mathrm{X}\frac{Loan\,loss\ provision}{Total\ loan}$$

2) NPL to Total Loan Ratio

It shows relation between NPL and total loan. This ratio is calculated as below:

$$NPL \text{ to Total Loan Ratio } X \frac{\text{NPL}}{Total \text{ Loan}}$$

3) Total Loan to Deposit Ratio (CD Ratio)

This ratio shows how much of public deposit were lent out as a loan and advances .In other words this ratio indicates how far has a bank able to create credit using it deposit as a base .Higher ratio indicates credit creating capabilities .It is computed as follow

$$Total \text{ Loan to Deposit Ratio } X \frac{\text{Total Loan}}{Deposit}$$

4) Investment to Total Deposit Ratio

This ratio measures the position of investment on total deposit. It is computed as follow

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

5) **Loan and Advances to Total Assets Ratio**

It measures position of loan and advances on total assets. It is also one of the indicator of credit risk. Its formula is as follow

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

6) Interest Income to Total Income Ratio

It is measured by dividing interest income by total income as follows:

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

7) Interest Income to Interest Expenses Ratio

This ratio is measured by dividing interest income to interest expenses.

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

8) Interest Income to Total Assets Ratio

It measures the position of the interest income on total assets .It is computed as follow

$$\text{Interest Income to Total Assets Ratio X}\frac{\text{Interest Income}}{\text{Total Assets}}$$

9) Total Borrowing to Total Assets Ratio

It shows the volume of total borrowing in total assets portfolio.

$$\text{Total Borrowing to Total Assets Ratio X}\frac{\text{Total Borrowing}}{\text{Total Assets}}$$

10) Total Liabilities to Total Capital Ratio

This ratio shows proportion of total liabilities in total capital structure

$$\text{Total Liabilities to Total Capital Ratio X}\frac{\text{Total Liabilities}}{\text{Total Capital}}$$

11) Cash and Bank Balances to Total Deposit Ratio

It shows liquidity position and shows percentage of cash and bank balance in total deposit.

$$\text{Cash and Bank Balances to Total Deposit Ratio X}\frac{\text{Cash and Bank Balances}}{\text{Total Deposit}}$$

12) Balance with NRB to Total Deposit Ratio

This ratio is calculated by dividing balance with NRB by total deposit.

$$\text{Balances with NRB to Total Deposit Ratio X}\frac{\text{Balances with NRB}}{\text{Total Deposit}}$$

13) Liquid Fund to Total Deposit Ratio

This ratio is calculated by dividing liquid fund by total deposit.

$$\text{Liquid Fund to Total Deposit Ratio X}\frac{\text{Liquid Fund}}{\text{Total Deposit}}$$

14) Growth Rate of Total Deposit

High volume of deposit signifies higher capacity for lending. It measures growth of the deposit during seven year study period

15) Growth Rate of Loan and Advances

Growth in loan and advances indicates the possibilities of higher earning in future but in long term it may lead to increase in NPA. So increased in loan of a newly established bank and old bank should be analyzed differently. It measures growth of loan during study period

16) Growth Rate of Total Investment

It measures growth of investment during study period.

17) Growth Rate of Total Income

It measures growth of total operating income during study period

18) Growth Rate of Borrowing

It measures growth of total borrowing during seven years study period

3.7.2 Descriptive Statistical tools:

Statistical tools include mean, correlation, trend analysis and regression analysis.

1. Arithmetic Mean:

It is the most common and widely used average. It can be defined as the sum of observations divided by the number of the observations (Baskota, 2004).

Mathematically,

$$\bar{X} \, X \, \frac{\phi x}{N}$$

2. Correlation coefficient:

Correlation analysis is primarily concerned with measuring the direction and strength of linear relation among the variables and this strength of relationship between variables are carried out by simple correlation coefficient, denoted by r. In this study Karl Pearson's Correlation has been used to find out relationship between variables and examine effects of one variable on other variables. The value of correlation coefficient (r) can be calculated from n pairs of observation(x, y) according to the following formula:-

$$\text{Correlation coefficient(r)} = \frac{n \sum X Y - \sum X . \sum Y}{[n \sum X^2 - (\sum X)^2] \quad [n \sum Y^2 - (\sum Y)^2]}$$

Where

r = correlation coefficient

n = Number of years

$\sum X$ = Sum of X series

$\sum Y$ = Sum of Y series

$\sum X Y$ = Sum of X and Y series

$\sum X^2$ = Sum of square of X series

$\sum Y^2$ = Sum of square of Y series

X and Y are financial variables of selected banks.

It shows positive or negative relationship between variables. The value of correlation coefficient lies between +1 and -1. The magnitude of correlation coefficient indicates the strengths of linear relation while its sign indicates the direction. A high numerical value of correlation coefficient that is the value close to +1 or -1 represents a strong linear relation. A value of correlation coefficient close to zero means that the linear association is very weak

Condition	Decision
When r =1	There is positive correlation
When r = -1	There is negative correlation
When r lies between "0.7 to 0.999"	There is high degree of positive correlation
When r lies between "0.5 to 0.6999"	There is moderate degree of correlation
When r is less than 0.5	There is low degree of correlation

Following relationship between variables is studied:

- Correlation between loan and advances and deposit.
- Correlation between Investment and loan
- Correlation between total income and loan and advances
- Correlation between borrowing and loan

3. Regression analysis:

The subject of regression analysis concerns the study of relationship among variables. The cause and effect relationship between variables is clearly indicated by regression analysis than by correlation. Regression analysis is used in statistics to estimate unknown value of one variable from known value of other variables. In regression there are two types of variables, the variable whose value is influenced is called dependent variable and the variable which influences the value is called independent variable. A regression problem involving a single predictor arises when we wish to study the relation between two variables x and y and use it to predict y from x. The variable x acts as an independent variable and y as a dependent variable. According to least square estimates, the regression between two variables can be calculated by using the following formula:-

$Y = a + bX + e$

Where Y = Dependent variable

X = Independent variable

a = the intercept of the line with y- axis (the Value of Y when X is zero)

b= Slope of the line or change in y per unit change in x

e = residual (error) value (the difference between the predicted and actual responses)

Using regression line for prediction:

The equation of the regression line is commonly used to predict the value of dependent variable Y for a given value of independent variable X. However regression equation should be used for prediction and estimation with utmost care and caution (Gupta, 2005).

4. Testing of Hypothesis

Hypothesis set in previous chapter is tested (two tailed) through t-test with 95% level of confidence.

5. Standard error of estimate:

It is used to measure the reliability of the expected regression equation.

It is denoted by $S_{xy.}$ Smaller the value, higher the reliability of fitted regression equation..

3.7.3 Primary data

Primary data was collected through well designed structured questionnaire .There are total 21 questions which are in yes/no, ranking and likert scale types. Questionnaire was distributed to various branch managers of NSBIL and EBL within Kathmandu valleys only due to limited time .Questions are of qualitative nature.

SECTION 4

DATA PRESENTATION AND ANALYSIS

Data collected from secondary sources are in raw form .It is necessary to arrange these data so that it can be interpreted and understood to the researcher and reader of this thesis. For this data are scanned, cleaned and organized. Different types of data need different method of representation. There are number of method which can be used to present and interpret the data. However the simple and easy way is to present data in the form of chart, graph and tables. Also, the analysis and interpretation of the information and data produced from questionnaire is also contained in this chapter and the data results of the study will be analyzed by determining their corresponding ratio, percentage, mean, correlation and regression. In addition Pie charts and line chart has been used to illustrate some of the analyzed data.

4.1 Financial Analysis

Financial statements are the single most important external information source when making a large credit decision. The financial statements need to be official and audited. With a few simple calculations, you will know the profitability, liquidity and solvency position. Financial analysis is done using EXCEL program in computer.

4.1.1 Measurement of Lending Efficiency:

The efficiency ratio is a useful tool in determining how effectively a bank is generating revenue. Lending efficiency indicates how effectively bank has utilizes its resources and also shows overall performance of bank. In other words, it is concerned with how well lending process has been managed and controlled. Thus higher ratio indicates less efficient lending performance or low quality of loan and vice-versa.

Sector wise loan classification
Table 4.1
Deprived Sector Loan Ratio

Banks	Fiscal year				
	2004/05	**2005/06**	**2006/07**	**2007/08**	**2008/09**
NSBIL	0.034197	0.030904	0.02965	0.029463	0.029177
EBL	0.029549	0.030302	0.027122	0.028562	0.030015

Source: Annex 1

Fig 4.1 Deprived Sector Loan Ratios of NSBIL

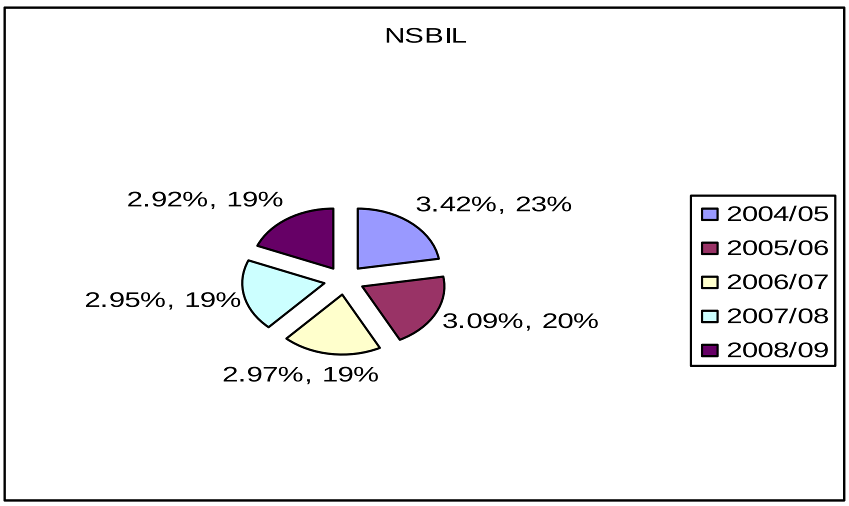
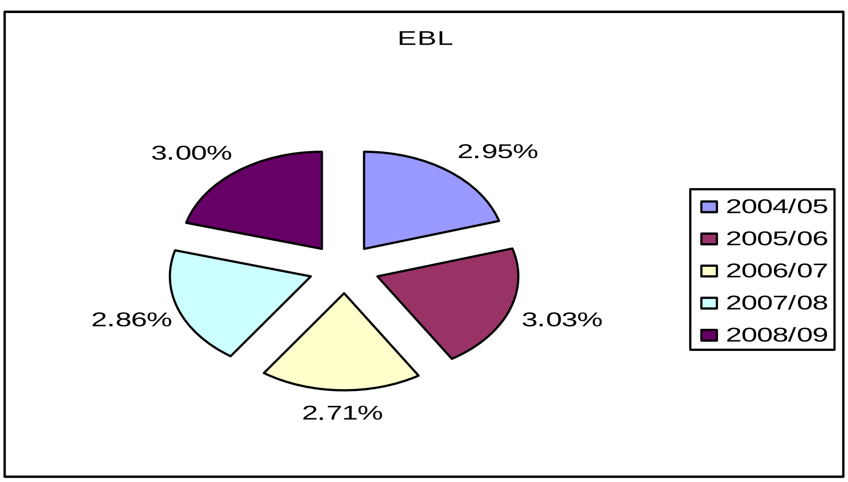


Fig 4.2 Deprived Sector Loan Ratios of EBL



Interpretation: Above figure shows that NSBIL has given 3.42% loan to deprived sector and it is in fluctuating trend .However lowest percentage is 2.92 in F/Y 2008/2009 whereas highest percentage is 3.42% in F/Y 2004/2005.In case of EBL, it has provided lowest i.e. 2.71% loan to priority sector in F/Y 2006/07 but in F/Y 2005/06 it has granted highest loan i.e. 3.03%.

Table 4.2
Priority Sector Loan Ratio

Banks	Fiscal year				
	2004/05	**2005/06**	**2006/07**	**2007/08**	**2008/09**
NSBIL	0.1338	0.097604	0.039174		
EBL	0.094321	0.086448	0.009214	0.000594	0.004195

Source: Annex 2

Fig 4.3 Priority Sector Loan Ratio of NSBIL

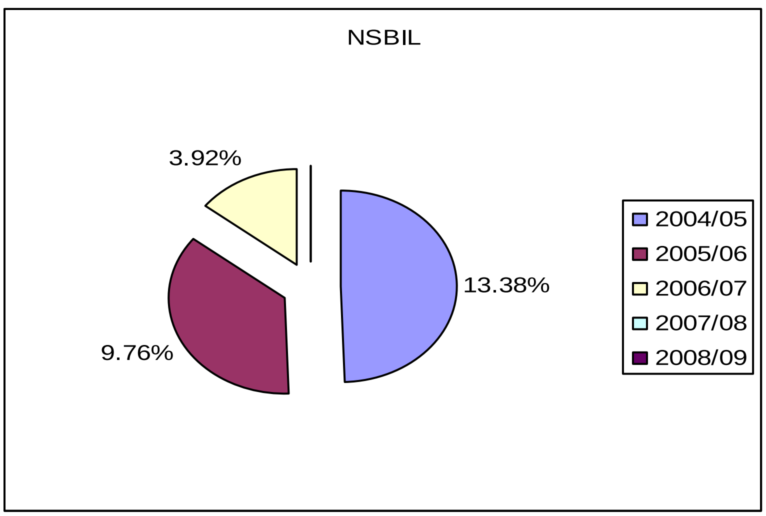
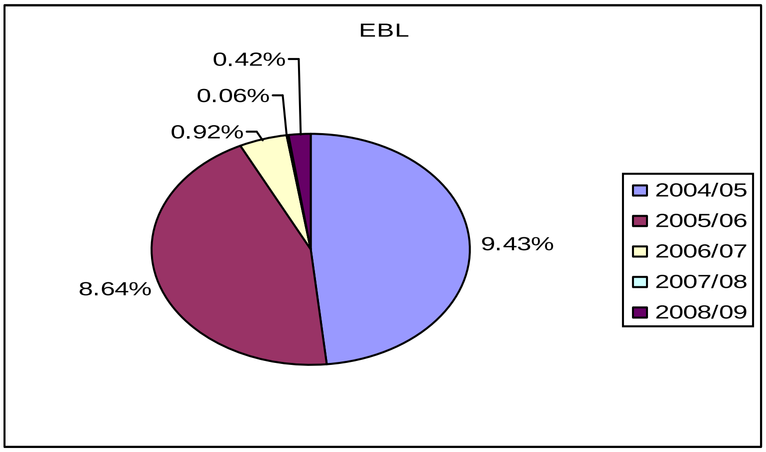


Fig 4.4 Priority Sector Loan Ratio of EBL



Interpretation: The above table shows percentage of loan provided to priority sector which includes agriculture, cottage industries and services. Similarly above figure shows that NSBIL has given highest 13.38% loan provided in 2004/05 but banks has not provided any loan in F/Y 2007/2008 and 2008/2009.In case of EBL, bank has given 9.43% loan to priority sector out of its total loan in the year 2004/2005 .However only 0.06% loan is granted in F/Y 2007/2008.

4.1.1.1 Loan Loss Provision to Total Loan Ratio:

Control of loan loss is an important part of loan management and bank always try to minimize it .Banks has to make provisions as per NRB directives. Provision shows increasing probability of being non performing loan in volume of total loan. High ratio shows high proportion of loan loss provision and chances of reducing profit. This ratio indicates adequacy of allowance for loan and trend in collection of loan and the performance in loan portfolio. It is obtained by the ratio of loan loss provision to the total loan. High provision shows difficulties in loan recovery.

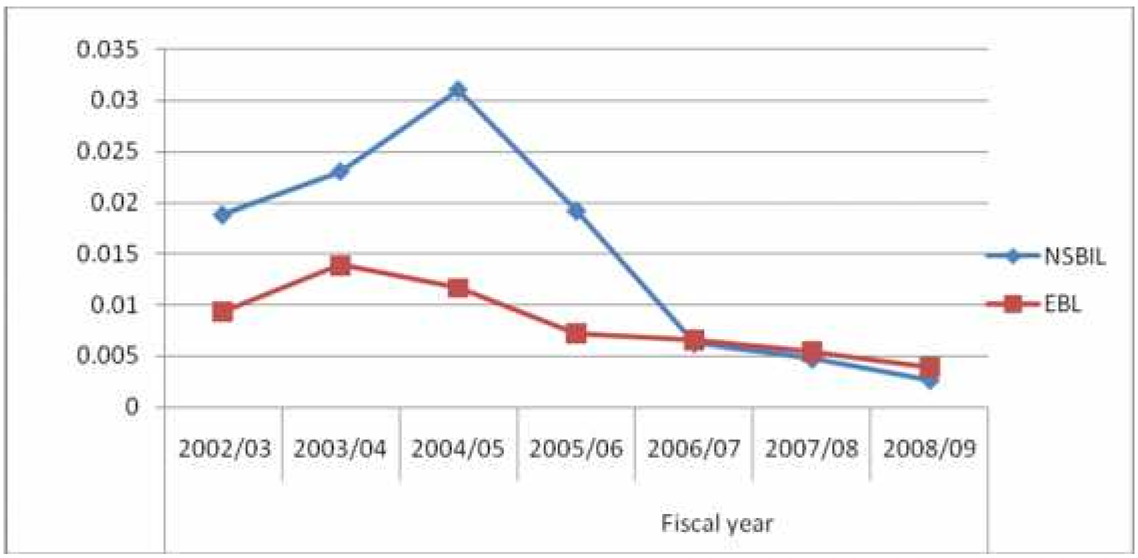
Table 4.3
Loan Loss Provision to Total Loan Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean

NSBIL	0.018836	0.023082	0.0311	0.019229	0.006276	0.004744	0.002667	0.0151
EBL	0.00932	0.013898	0.011672	0.007189	0.006564	0.005417	0.003897	0.0083

Source: Annex 3

Fig 4.5 Loan Loss Provision to Total Loan Ratio



Interpretation: It is observed from the above table that ratio is highest in NSBIL that is 0.0311 in F/y 2004/05 but thereafter it is in decreasing trend. Moreover lowest ratio is in F/Y 2008/2009. Similarly in case of EBL ratio is in fluctuating year by year. Highest ratio is i.e. 0.0138 in F/Y 2003/2004 and it is lowest in 2008/09. However on average EBL has lowest loan loss provision ratio than NSBIL. It is signal of low credit risk and good lending efficiency.

4.1.1.2 NPL to Total Loan Ratio:

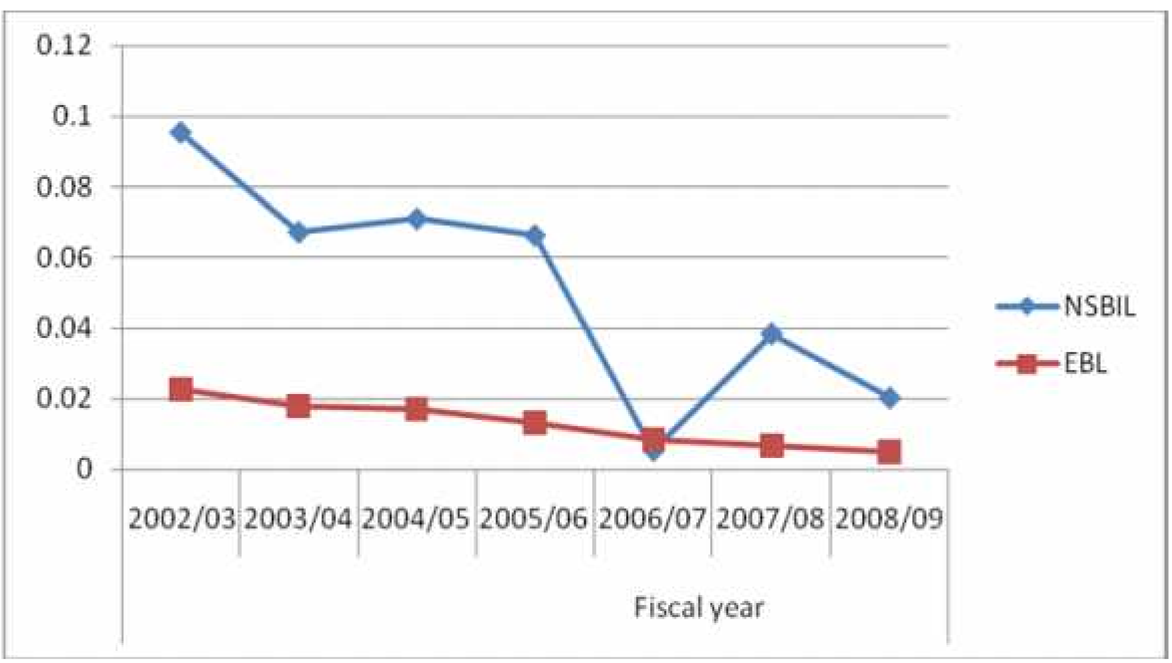
NPA is not only crucial to the bank but also to the economy because failure of bank not only affects its promoter and shareholder but also affects thousand of depositor who has deposited their money. It is the indicator of the quality of assets of commercial banks. The increasing trend of these ratios shows the deteriorating position of banks .In fact high ratio reduces profit also. Higher NPL indicates that banks take more risk in their operations and investment.

Table 4.4
NPL to Total Loan Ratio:

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.0955	0.0672	0.071	0.0663	0.0052	0.0384	0.0202	0.052
EBL	0.022653	0.017804	0.016907	0.013182	0.008282	0.006598	0.004917	0.012906

Source: Annex 4

Fig 4.6 NPL to Total Loan Ratio:



Interpretation: Above table and figure explains that NPL of NSBIL is decreasing from F/Y 2005/06 which indicates good quality of assets and sound NPL management practices of bank. However in case of EBL also NPL is decreasing trend since F/Y 2002/2003 which shows best quality of assets and low credit risk. But on an average, EBL has lowest ratio as compare to NSBIL. Thus overall lending efficiency of both banks is in good position.

4.1.2 Asset Management Ratios

Reed, cottler and gill in their book commercial banking mentioned that asset management refers to distribution of fund among cash, investment, loan and other assets and allocation is restricted by law and regulation. Loan and advances, investment are major assets of bank and they earns interest and dividend and other income. So they are called earning assets whereas deposits and borrowing are liabilities for the bank since bank has to pay interest on it. Thus this ratio shows how well bank has managed its assets for income generation purpose. In fact, high ratio indicates effective and optimum utilization of banking assets. Bank must be able to manage its assets properly to earn high profit without disturbing liquidity position. Following are some ratios

4.1.2.1 Loan and Advances to Total Deposit Ratio:

Bank uses fund collected from deposit and borrowing in providing various loan to customers. It Indicates the percentage of a bank's loans funded through deposits (measures funding by borrowing as opposed to equity). It measures to the extent to which the bank is successful to mobilize its total deposits in loan for the purpose of income generation purpose. Higher ratio shows better mobilization of deposits and vice-versa. A high loan-to-deposit ratio indicates that a bank has fewer funds invested in readily marketable assets. However, cannot also be too low as loans are considered the highest and best use of bank funds (indicates excess liquidity).

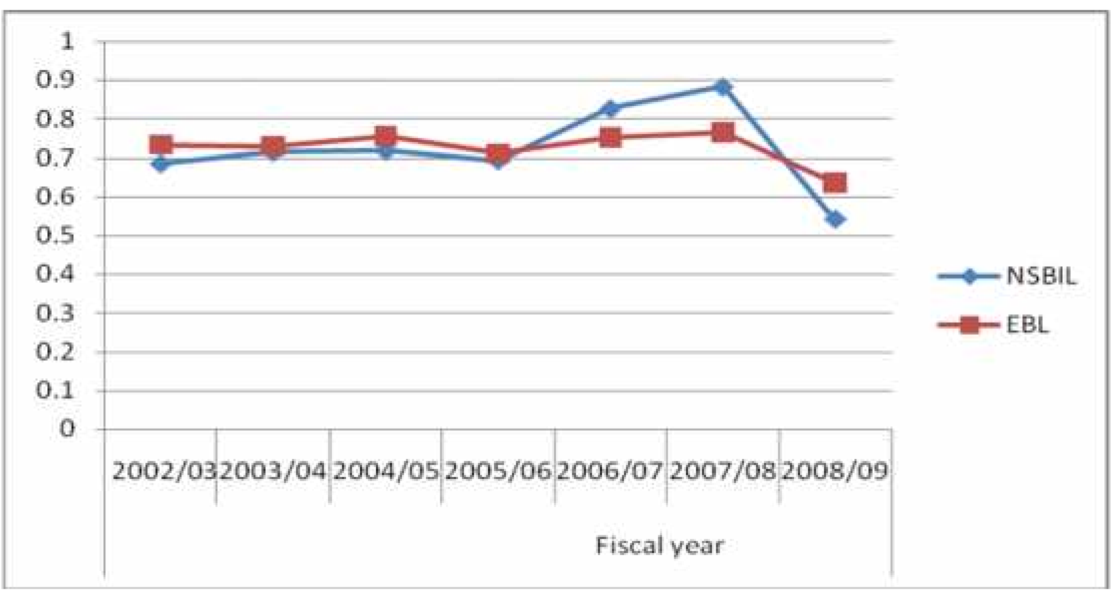
Table 4.5

Loan to Deposit Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.68509	0.714564	0.718	0.693211	0.826581	0.883219	0.541247	0.7231
EBL	0.733157	0.729687	0.754496	0.710114	0.751341	0.764884	0.634811	0.725499

Source: Annex 5

Fig 4.7 Loan to Deposit Ratio



Interpretation: Above table shows that ratio of NSBIL is in fluctuating trend. The highest ratio is 0.8832 in FY 2007/2008 and lowest is 0.5412 in FY 2008/2009.However in case of EBL highest ratio is 0.7648 in FY 2007/2008 and lowest ratio is 0.6348 in FY 2008/2009. Ratio of both banks is in fluctuating trend but on an average EBL has highest ratio as compare to NSBIL. All this analysis concludes that on an average EBL has better mobilization of deposit as a loan as compare to NSBIL. In other side high Loan to deposit ratio led to permanent rise of deposit interest rate and also increases credit risk and liquidity risk.

4.1.2.2 Investment to Total Deposit Ratio

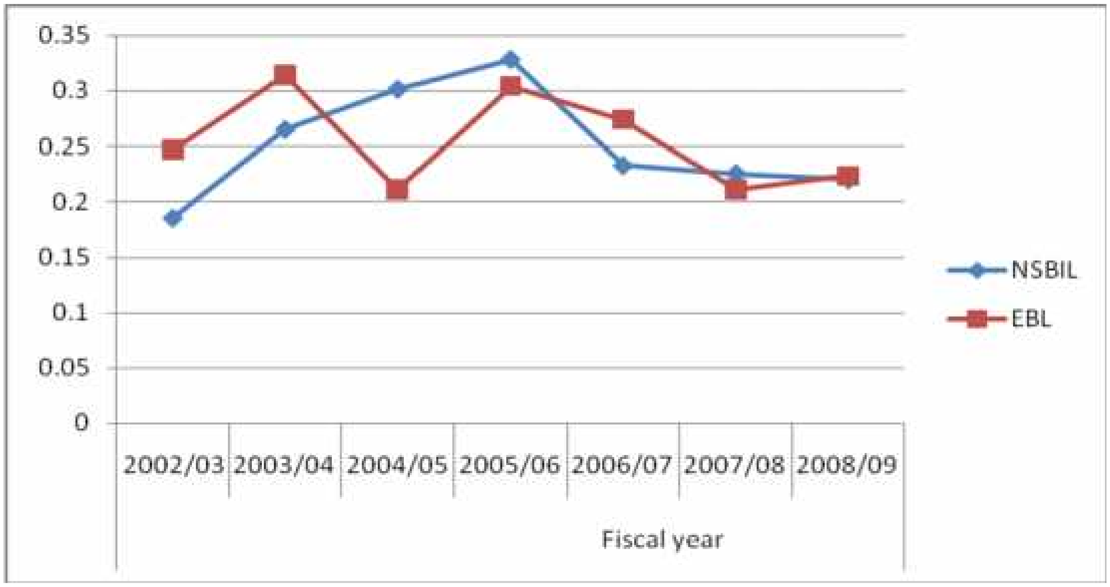
Apart from giving loan, bank invest deposit and borrowing in purchasing various government securities, share, debenture and bond or in other financial institutions. Investment is less risky than giving loan. It shows volume of investment in the structure of total deposit. High ratio indicates high success to mobilize deposit in securities and other financial institutions and vice-versa.

Table 4.6
Investment to Total Deposit Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.185085	0.264995	0.3013	0.328191	0.232362	0.225213	0.219592	0.251
EBL	0.247048	0.314446	0.210834	0.304331	0.274071	0.211023	0.223107	0.255

Source: Annex 6

Fig 4.8 Investment to total Deposit ratio



Interpretation: It is observed from the above table that ratio is highest in NSBIL that is 0.3281 in FY2005/2006 and lowest ratio is 0.1850 in FY 2002/2003. In case of EBL highest ratio is 0.3144 in

FY2003/2004 and lowest ratio is 0.2108 in FY 2004/2005. Moreover on an average EBL has highest ratio as compare to NSBIL. Thus it can be conclude that EBL has mobilized its deposit as investment in various share, debenture and securities and has better asset management.

4.1.2.3 Loan to Total Assets Ratio

Loan occupies major portion in total assets of bank. The loan to assets ratio measures the total loans outstanding as a percentage of total assets. The higher this ratio indicates a bank is loaned up and its liquidity is low. In other words, high ratio indicates good performance of the bank in mobilizing its fund by the way of lending function. Similarly higher the ratio, the more risky a bank may be to higher defaults.

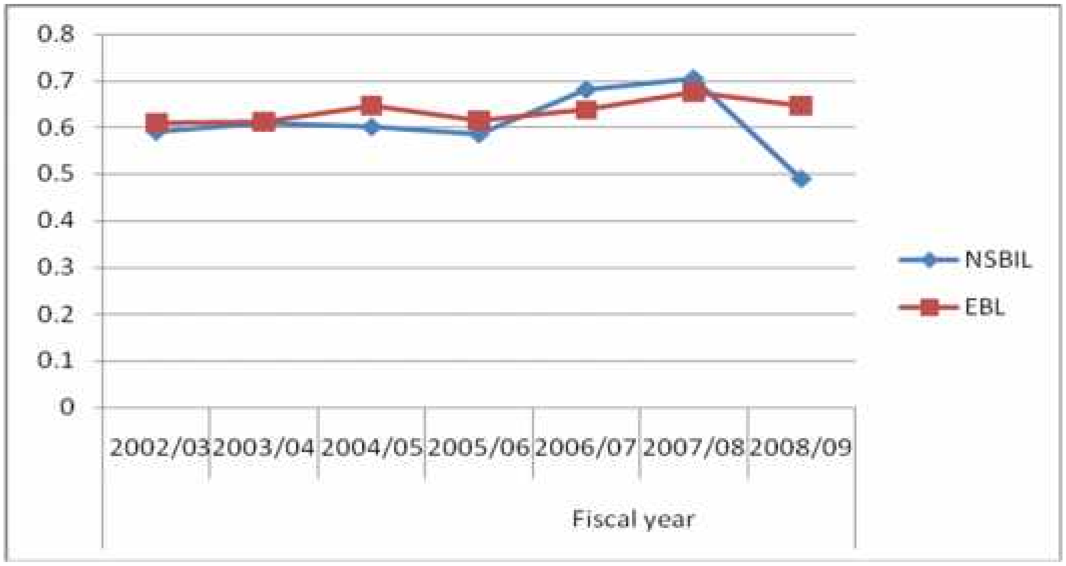
Table 4
Loan to Total Assets Ratio

Banks	Fiscal year	

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.5906	0.6094	0.6006	0.5851	0.6805	0.7048	0.4894	0.6086
EBL	0.6096	0.6124	0.6461	0.6141	0.6375	0.6755	0.647	0.6346

Source: Annex 7

Fig 4.9 Loan to Total Assets Ratio



Interpretation: Above table and figure explains that highest share of Loan of NSBIL was 0.7048 in FY 2007/2008 and lowest is 0.4894 in FY 2008/2009.However in case of EBL, highest ratio is 0.6755 in FY 2006/2007 and its lowest ratio is 0.6096 in FY 2002/2003.But since FY 2005/2006 ratio of both banks were fluctuating. Moreover on an average EBL has highest ratio as compare to NSBIL. Thus it means EBL has better performance in mobilizing its fund by the way of lending activities and also better asset management but excessive high ratio is risky which may with higher defaults.

4.1.3 Profitability Ratio:

Main objective of every bank is to earn profit .Profit is a major indicator of efficient operation of an organization. This ratio shows operating and financial performance or efficiency. Profitability ratios are used to assess a business's ability to generate earnings as compared to its expenses and other relevant costs incurred during a specific period of time. The largest source of income for a bank is net interest revenue (interest income from lending activity less interest paid on deposits and debt). The second most important source is from investing activity. For most of these ratios, having a higher value relative to a competitor's ratio or the same ratio from a previous period is indicative that the company is doing well. Higher ratio shows better operational efficiency and vice-versa. In analyzing profitability a banker is looking primarily at the ability of company as a going concern to use money borrowed by it in an efficient manner so that loan can be given to customer.

4.1.3.1 Interest Income to Total Income Ratio:

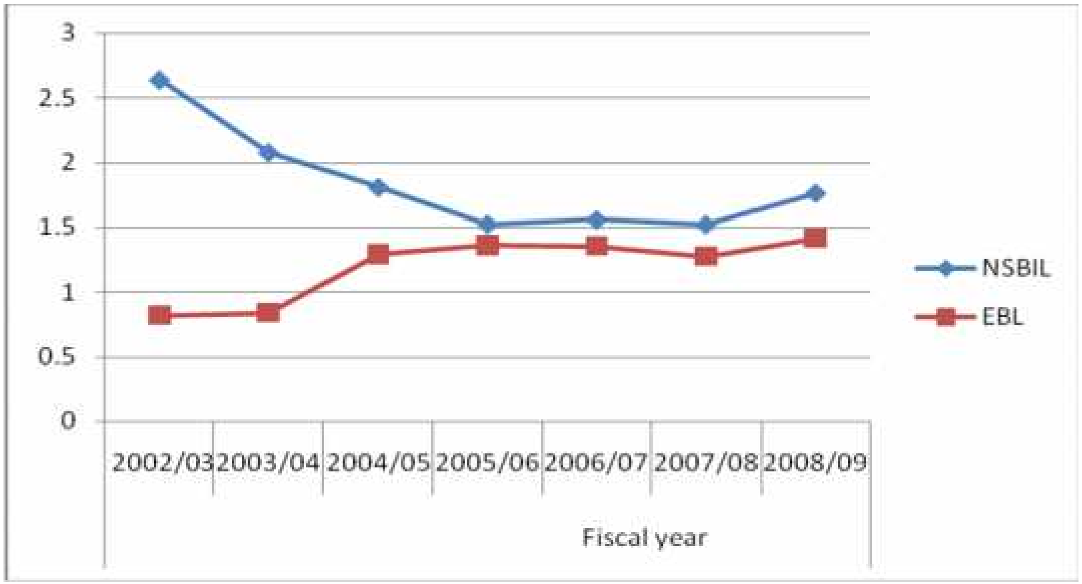
Interest income is a major source of income for a bank. It measures how well banks are using fund for generating profit. Similarly it shows efficiency in using fund in fee-based activities. High ratio indicates high contribution made by lending and investing activities in total income and vice-versa.

Table 4.8
Interest Income to Total Income Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	2.640175	2.076742	1.80774	1.524458	1.557825	1.52104	1.762406	1.8415
EBL	0.818742	0.837197	1.292727	1.364354	1.360234	1.27999	1.415445	1.1955

Source: Annex 8

Fig 4.10 Interest Income to Total Income Ratio



Interpretation: From the above table it is found that interest income to total income ratio in NSBIL is highest in the FY 2002/2003 i.e. 2.6401 and lowest ratio is 1.52104 in FY 2007/2008 whereas in case of EBL highest ratio is 1.4154 in FY 2008/2009 and lowest ratio is 0.818742 in F/Y 2002/2003..But NSBIL has highest ratio during entire study period than EBL. On an average, NSBIL has highest ratio as compare to EBL. This concludes that in NSBIL interest income has highest contribution in total income than EBL .In other words NSBIL is largely dependent in lending activities and investment.

4.1.3.2 Interest Income to Interest Expenses Ratio:

Bank collects interest on loan and advances and used to pay interest on deposit and borrowing. Thus this ratio shows ability of the bank to meet its expenses from interest income. It measures the differences between interest rate offered and interest rate charged. The spread between the interest income and interest expenses is main foundation for banks.

Table 4.9

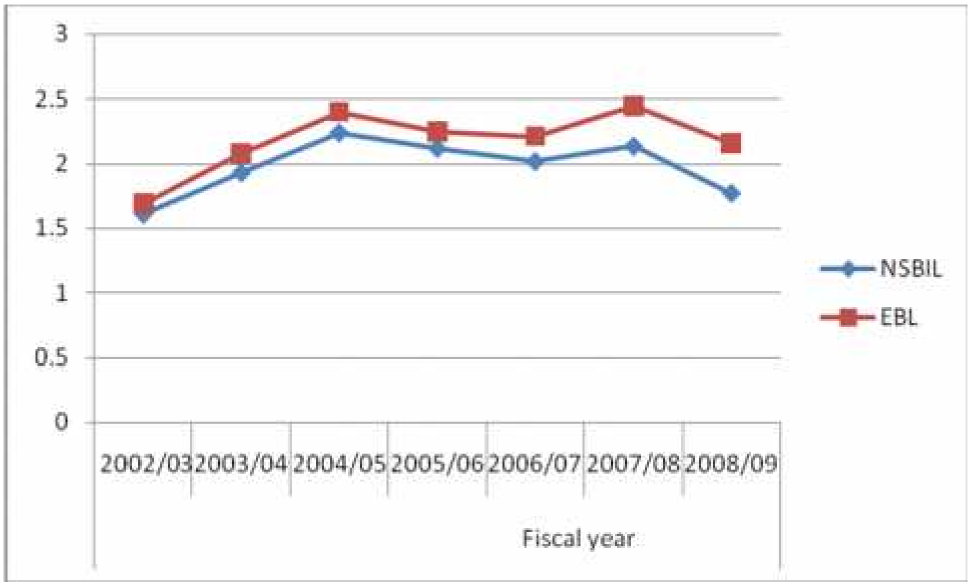
Banks	**Fiscal year**	

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	1.609691	1.928727	2.238022	2.117033	2.015992	2.13338	1.770882	1.9734
EBL	1.690855	2.077496	2.401134	2.250667	2.212845	2.448048	2.15902	2.1772

Interest Income to Interest Expenses Ratio

Source: Annex 9

Fig 4.11 Interest Income to Interest Expenses Ratio



Interpretation: From the above table it can be analyzed that the ratio of EBL is highest over study period than NSBIL. Highest ratio for EBL is 2.4480 in FY 2007/2008 and lowest ratio is 1.6908 in FY 2002/2003 but for NBSIL highest ratio is 2.2380 in FY 2004/2005 and lowest ratio is 1.6096 in FY 2002/2003.But on an average EBL has highest ratio than NSBIL. This indicates that EBL has more ability to meet its expenses from interest income than NSBIL.

4.1.3.3 Interest Income to Total Assets Ratio:

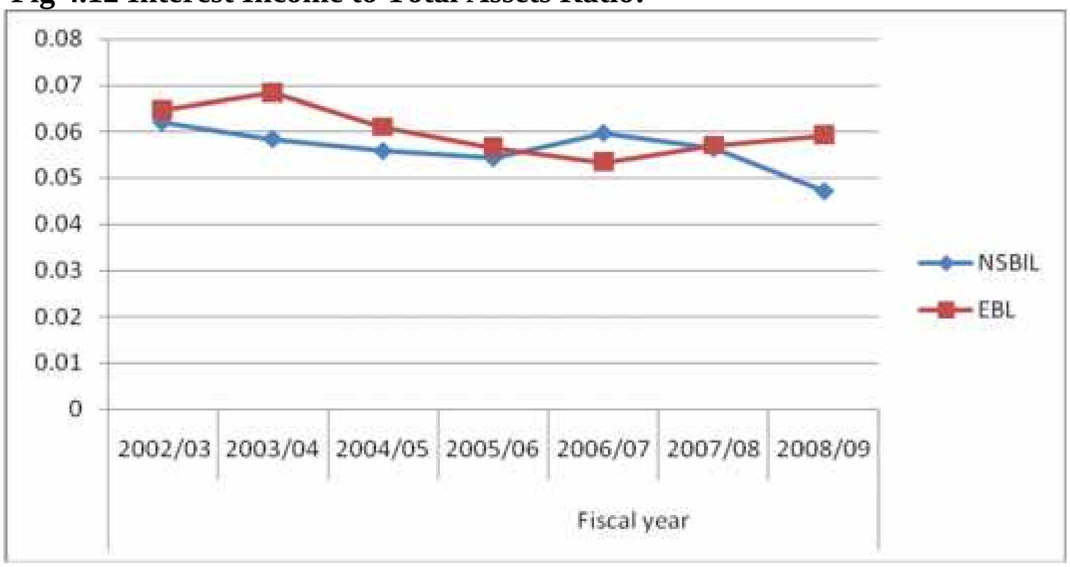
Bank earns interest from loan and investment. This ratio measures the contribution made by the interest income in total assets. This ratio is the actual measure of the bank’s performance as an intermediary, as it examines the bank’s ability in mobilizing lower cost funds and investing them at a reasonably higher interest. It indicates how effectively the assets of a business are utilized to generate income. Higher ratio shows better ability to generate interest income from loan and investment.

Table 4.10
Interest Income to Total Assets Ratio:

Banks	Fiscal year							
	2002/03	**2003/04**	**2004/05**	**2005/06**	**2006/07**	**2007/08**	**2008/09**	**Mean**
NSBIL	0.062083	0.05848	0.055906	0.054367	0.059787	0.056466	0.047238	0.353839
EBL	0.0646	0.068402	0.060998	0.056607	0.053396	0.057042	0.059236	0.369508

Source: Annex 10

Fig 4.12 Interest Income to Total Assets Ratio:



Interpretation: Above table shows that ratio of both banks were consistent during study period .EBL has highest ratio than NSBIL. On an average EBL has highest ratio .So it is clear that EBL has ability in mobilizing lower cost funds and investing them at a reasonably higher interest and assets are effectively utilized to generate income than NSBIL

4.1.4 Leverage Ratio:

It is known as capital structure ratio. This ratio indicates mix of fund provided by owner and lender. Increase in leverage means increase in risk and return. It shows debt servicing capacity, strength and weakness of the organization. From organization view, lower ratio is more preferable.

4.1.4.1 Total Borrowing to Total Assets Ratio

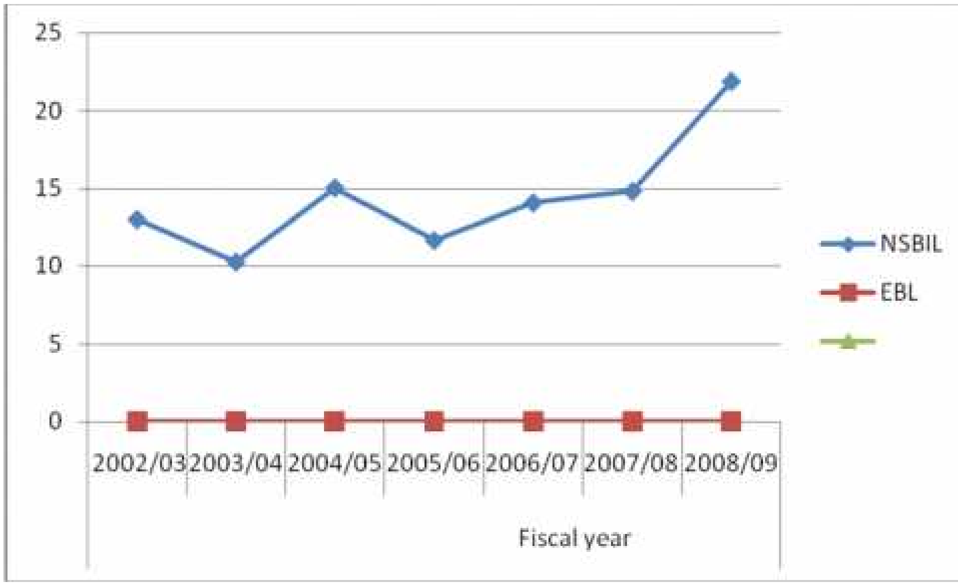
Commercial banks borrow fund from NRB or other financial institutions .This ratio shows relation between borrowing and total assets .It measures proportion of borrowing in total volume of assets. Higher ratio shows higher contribution made by borrowing in total assets composition.

Table 4.11
Total Borrowing to Total Assets Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	12.9805	10.2532	15.0085	11.6412	14.043	14.7747	21.8554	14.3652
EBL	0.0254407	Nil	Nil	Nil	Nil	Nil	0.0084514	0.00484

Source: Annex 11

Fig 4.13 Total Borrowing to Total Assets Ratio



Interpretation: The above table shows ratio of NSBIL is highly fluctuating during study period but EBL has borrowed fund only in FY 2002/2003 and FY 2008/2009.So NSBIL has higher ratio than EBL.This means NSBIL has made more borrowing and contribution of borrowing in total assets portfolio is highest in FY 2008/2009 and lowest is in FY 2003/2004.

4.1.4.2 Total Liabilities to Total Capital Ratio

This ratio measures portion of total liabilities in total capital of a bank. In order words it shows the amount by which the company is leveraged. It indicates how much of a company's assets are provided through debt.

Table 4.12

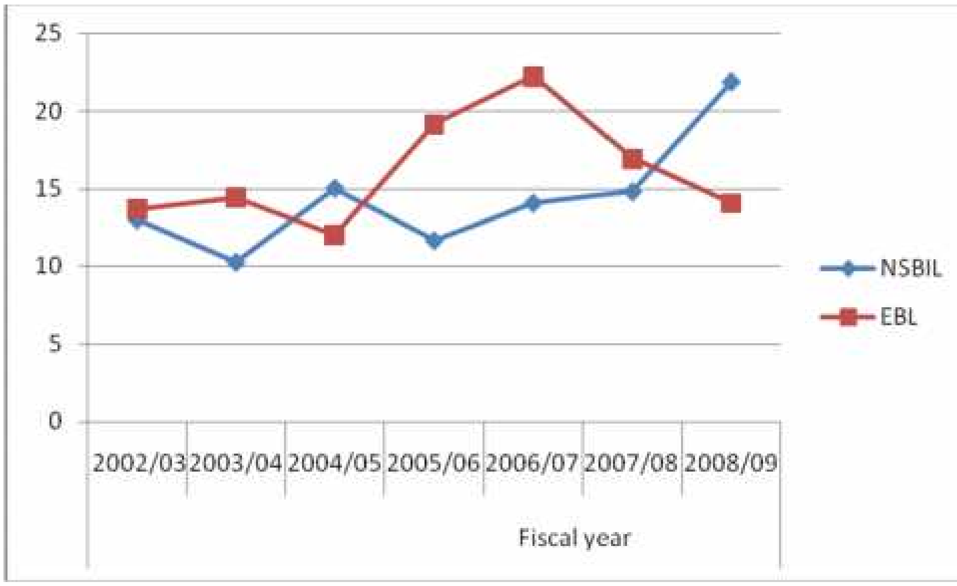
Banks	Fiscal year	

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	12.980489	10.253166	15.00852	11.641221	14.043035	14.774732	21.855423	14.3653
EBL	13.71523	14.43162	12.0291	19.17031	22.24219	16.95245	14.07727	16.08831

Total Liabilities to Total Capital Ratio

Source: Annex 12

Fig 4.14 Total Liabilities to Total Capital Ratio



Interpretation: Above table shows that ratio of NSBIL and EBL is in fluctuating trend .Highest ratio of NSBIL is 21.8554 in FY 2008/2009 and lowest ratio is 10.2531 in FY 2003/2004.However in case of EBL highest ratio is 22.24219 in FY 2006/2007 and lowest ratio is 12.0291 in FY 2004/2005.But in an average EBL has highest ratio than NSBIL. This means that EBL is more levered.

4.1.5 Liquidity Ratio:

The ability of the firm to meet its short term payment commitments is called liquidity. These ratios are used to ascertain short term solvency position of the firm. Lack of adequate liquidity is often one of the first signs that a bank is in serious financial trouble (Rose 1999). Both liquidity deficit and much more liquidity surplus indicate the problem in the financial health of a commercial bank. Much more liquidity surplus hurts the profitability of the commercial bank by reducing the return on assets. Similarly, liquid deficit also hurt in the reputation of the banks. Therefore, commercial banks should balance between the profitability and liquidity risk. In the case of commercial banks, first type of liquidity risk arises when depositors of commercial banks seek to withdraw their money. The second type of liquidity risk arises when demand for unexpected loans can not be met due to the lack of the funds.

4.1.5.1 Cash and Bank Balances to Total Deposit:

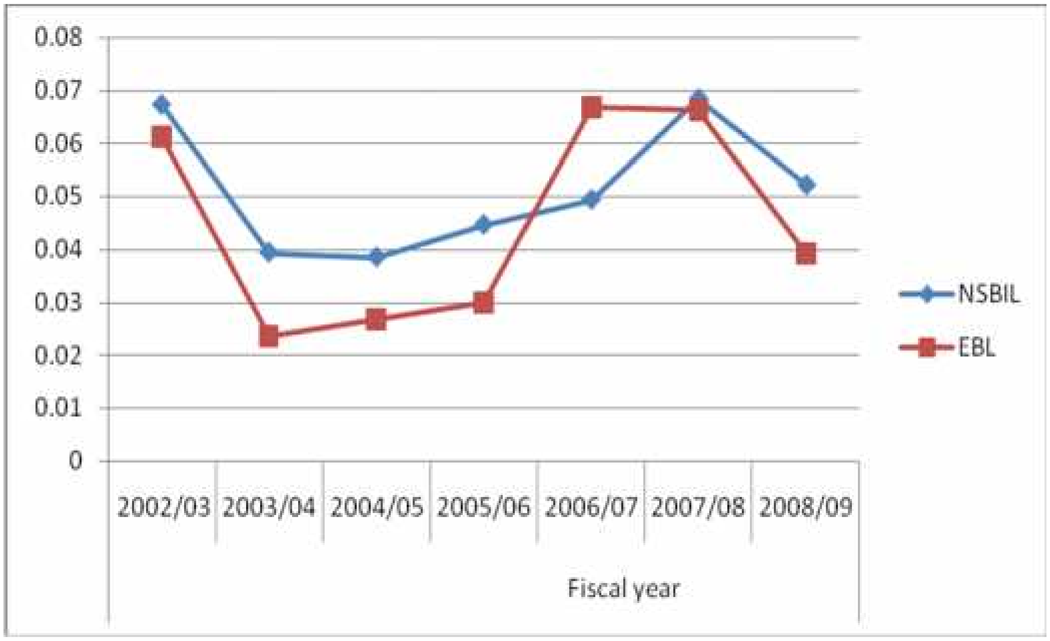
Cash and bank balances are most liquid assets and it shows percentage of most liquid fund with the bank to make immediate payment to the depositor. If the ratio is high, it means more idle cash with bank and if ratio is low, it shows inability to make payment to depositor. If cash is insufficient to meet the demands of customers, especially depositors withdrawals and credible borrowers, it could lead to loss of public confidence and consequent run on the commercial bank leading to bank failure. As a result, a commercial bank has to hold a certain amount of cash that will meet with depositors withdrawal requirements and other liquidity needs of the commercial bank.

Table 4.13 Cash and Bank Balances to Total Deposit Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.067365	0.03945	0.038559	0.044722	0.049454	0.068474	0.052214	0.051463
EBL	0.061126	0.023507	0.026771	0.029955	0.066711	0.066193	0.03918	0.044778

Source: Annex 13

Fig 4.15 Cash and Bank Balances to Total Deposit Ratio



Interpretation: It is observed from the above table that the ratio is highest in NSBIL that is 0.068 in FY 2007/2008 i.e. 0.0684 and lowest is 0.03855 in FY 2004/2005. But in case of EBL highest ratio is 0.066193 in FY 2006/2007 and lowest ratio is 0.0235 in FY 2003/2004. On an average NSBIL has highest ratio than EBL. This concludes that NSBIL has more cash ideal but better liquidity position than EBL.

4.1.5.2 Liquid Fund to Total Deposit Ratio:

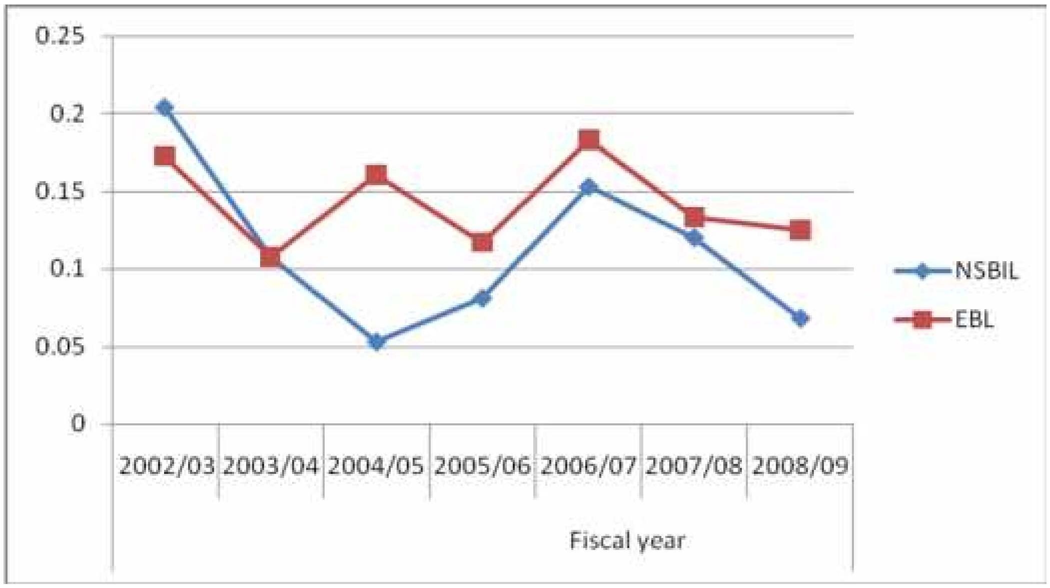
Liquid fund comprises of those assets which can be converted into cash within a short period of time without any decline in their value .Cash in hand, balance with NRB, balance with other banks, money at call and investment in government securities is included in calculating total liquid fund of a bank. This ratio measures banks ability to discharge its liabilities (Interest on deposit) in an adverse condition without undergoing its liquidity risk.

Table 4.14
Liquid Fund to Total Deposit Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.204145	0.107664	0.053104	0.081303	0.153295	0.120419	0.068351	0.112611
EBL	0.172682	0.107851	0.160849	0.117342	0.183089	0.133398	0.12503	0.142892

Source: Annex 14

Fig 4.16 Liquid Fund to Total Deposit Ratio



Interpretation: Above table shows that ratio of both banks are fluctuating. But on an average EBL has higher ratio as compare to NSBIL. This means EBL has better ability to discharge its liabilities without undergoing its liquidity risk. So it has better liquidity position.

4.5.1.3 Balances with NRB to Total Deposit Ratio

Balances with NRB are also liquid fund of a bank. This ratio measures the percentage of balance with NRB to pay interest to depositor.

Higher ratio shows better liquidity position and vice-versa.

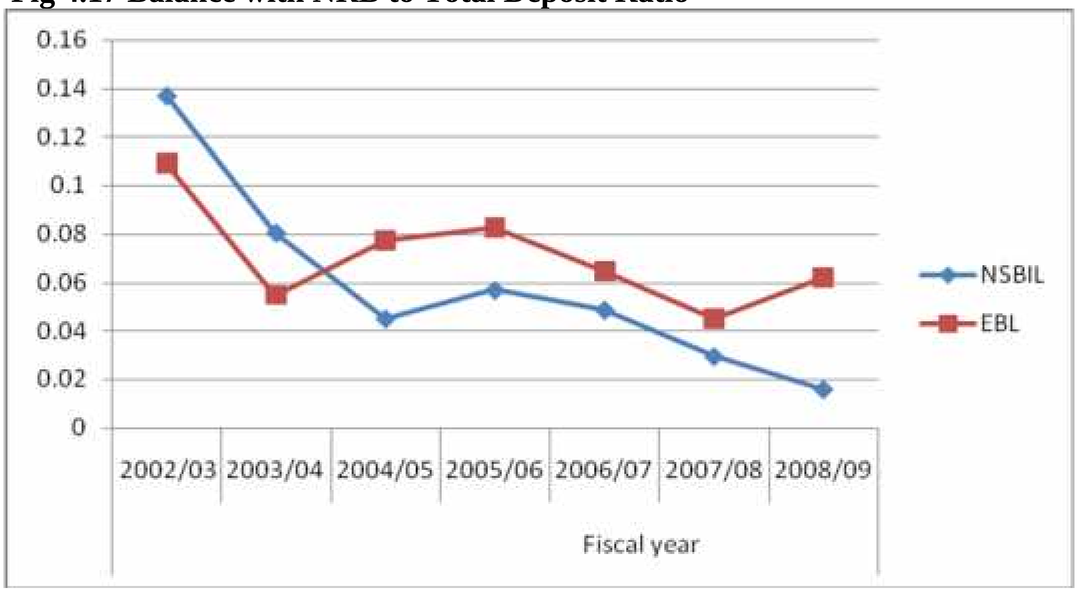
Table 4.15

Balance with NRB to Total Deposit Ratio

Banks	Fiscal year							
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	Mean
NSBIL	0.137076	0.080637	0.045065	0.05691	0.048638	0.029442	0.015886	0.059094
EBL	0.109087	0.054842	0.077213	0.082559	0.064785	0.045083	0.061938	0.070787

Source: Annex 15

Fig 4.17 Balance with NRB to Total Deposit Ratio



Interpretation: Above table shows that ratio of NSBIL is in decreasing trend but that of EBL is fluctuating. However on an average EBL has higher ratio than NSBIL. This means EBL high balances with NRB to pay interest to depositor and also better liquidity position.

4.2 Analysis of Growth Rate:

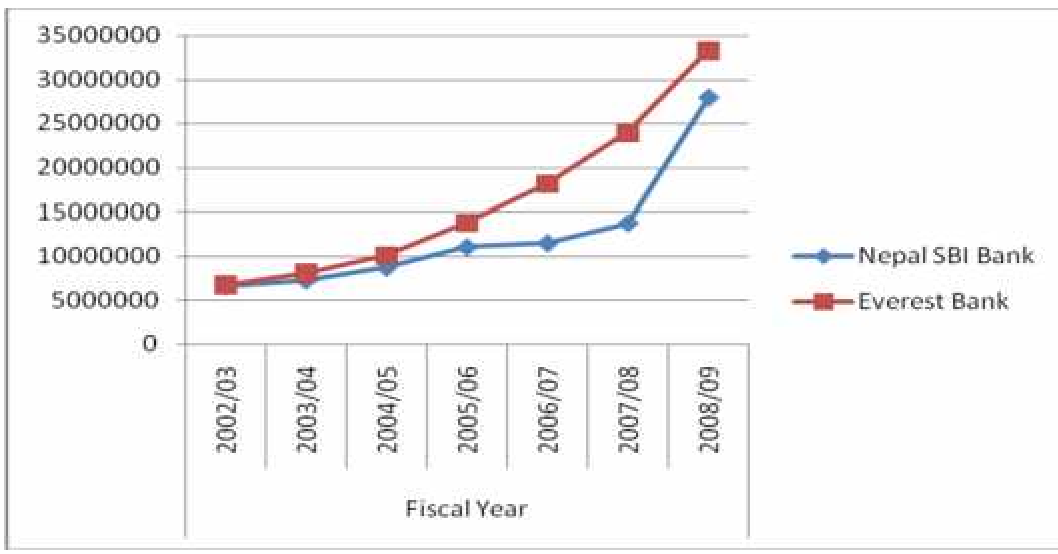
It examines and analyzes the expansion and growth of the various research variables over the period of time. It indicates increase or decrease in deposit, loan, interest and income. Thus it analyzes growth rate of deposit, loan, interest and income. Growth rate are directly related with fund mobilization and investment decisions of the bank.

4.2.1 Growth rate of Deposit: Deposit is main source of fund for the banks. Banks uses fund collected from deposit to provide loan and make investment

Table 4.16 Growth of Deposit (Rs '000')

Bank	Fiscal Year						
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Nepal SBI Bank	6522817	7198327	8654774	11002041	11445286	13715395	27957221
Everest Bank	6694964	8063902	10097691	13802445	18186254	23976298	33322946

Fig 4.18 Growth of Deposit



Interpretation: It is reflected from the table that almost every year's loan and advances of NSBIL and EBL has increased from the previous year. As for comparision, EBL has been able to collect higher deposit during study period than NSBIL.Depsit collection of both banks are in increasing trend but trend is increasing more faster in EBL than NSBIL.So we can conclude that EBL has good performance than NSBIL

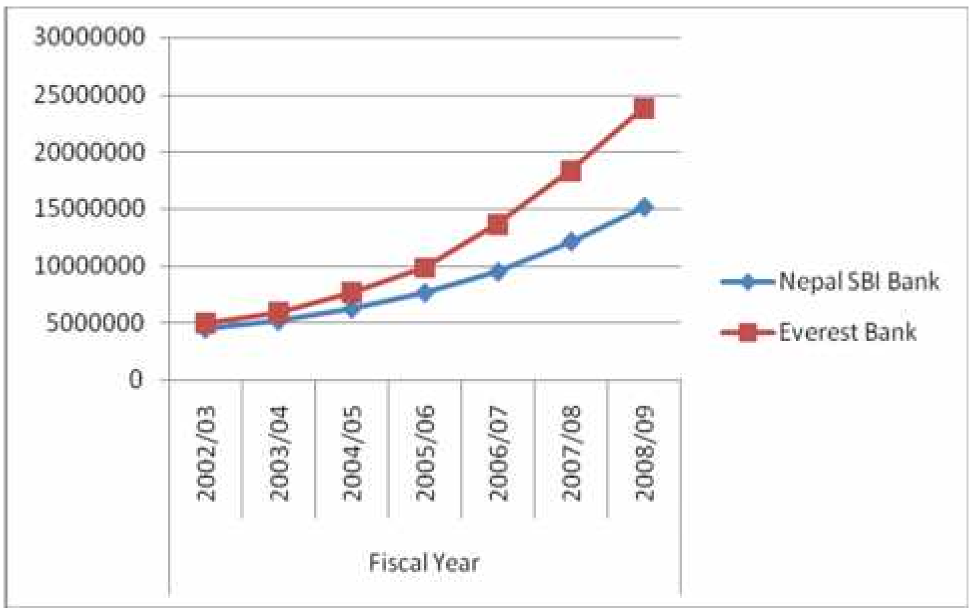
4.2.2 Growth rate of Loan and Advances

Loan and advances are principal function of a commercial bank and contribute highest income in the form of interest to the bank.

Table 4.17 Growth of Loan (Rs'000')

Bank	Fiscal Year						
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Nepal SBI Bank	4468719	5143662	6213879	7626736	9460451	12113698	15131748
Everest Bank	4908401	5884124	7618670	9801308	13664082	18339085	23884674

Fig 4.19 Growth rate of Loan and Advances:



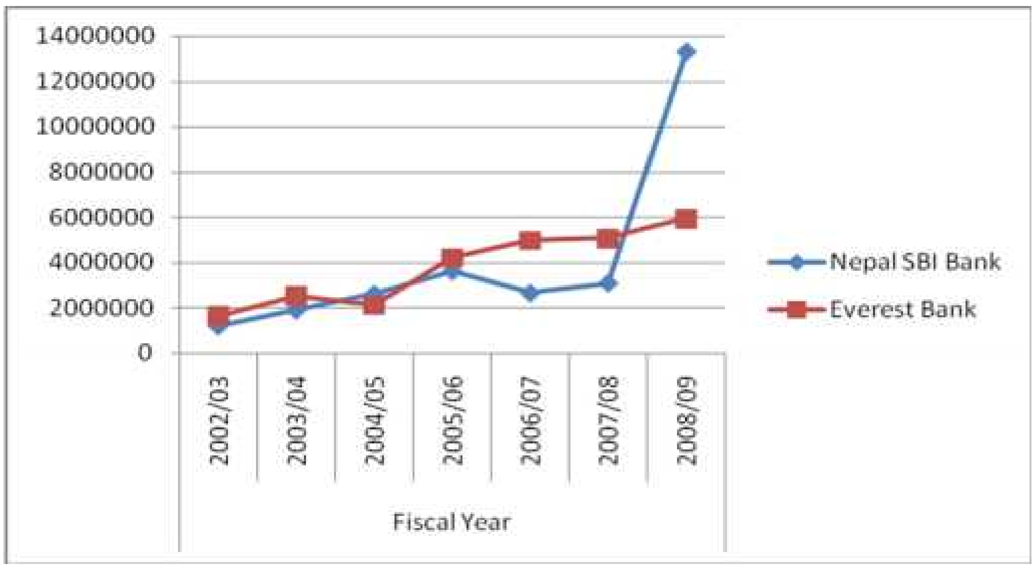
Interpretation: Above table shows that loan and advances of both banks are in increasing trend but it is increasing faster in EBL than NSBIL during seven years period.

4.2.3 Growth Rate of Investment: Commercial bank makes investment in government securities, share, debenture and other financial institutions. Growth ratio of investment of NSBIL and EBL has been given below

Table 4.18 Growth of Investment (Rs'000')

Bank	Fiscal Year						
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Nepal SBI Bank	1207275	1907521	2607680	3610775	2659453	3088887	13286182
Everest Bank	1653978	2535658	2128932	4200515	4984315	5059557	5948480

Fig 4.20 Growth Rate of Investment



Interpretation: Above table shows that investment of NSBIL is in increasing trend up to FY 2005/2006 but decreases in FY2006/2007 again thereafter it increases. However in case of EBL investment increases only from FY 2005/2006

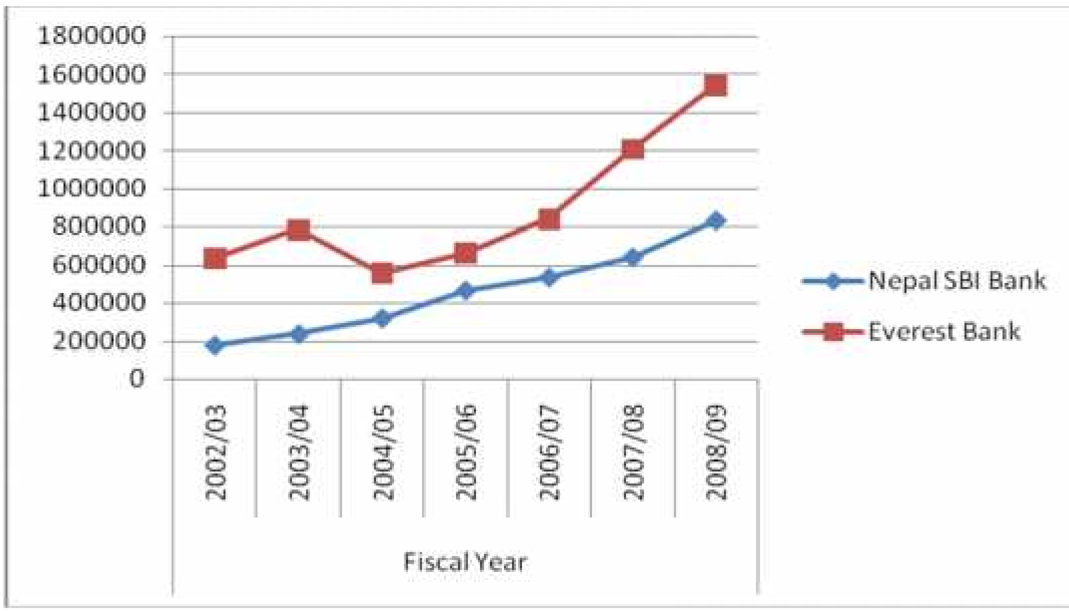
4.2.4 Growth Rate of Total Income

Banks earns income from granting loan and advances and investment in the form of interest and dividend. High ratio shows growth of income of banks.

Table 4.19 Growth of Total income (Rs'000')

Bank	Fiscal Year						
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Nepal SBI Bank	177920	237679	319942	464899	533511	638059	828666
Everest Bank	635332	785059	556419	662153	841332	1209898	1544966

Fig 4.21 Growth Rate of Total Income:



Interpretation: During the study period NSBIL has been able to mark a rising trend in its total income but in case of EBL it is in fluctuating trend.However income of EBL is increasing faster from FY 2006/2007.Highest income for NSBI and EBL is 828666 and 1544966 in FY 2008/2009.

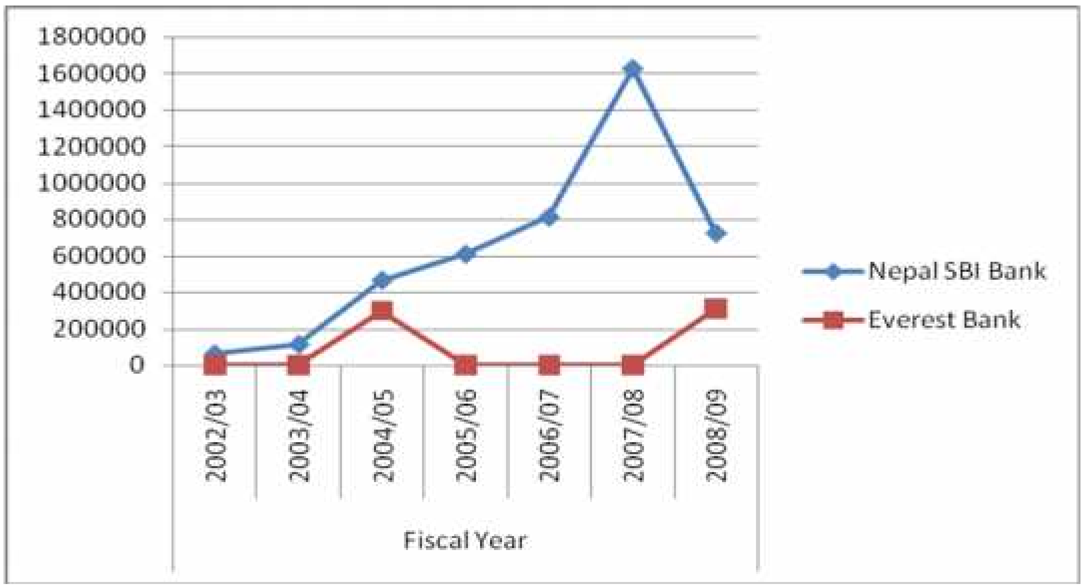
4.2.5 Growth Rate of Borrowing;

Bank borrow fund from government, NRB and other financial institutions. So it is one of the sources of fund for the commercial banks.

Table 4.20 Growth of Borrowing (Rs'000')

Bank	Fiscal Year						
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09
Nepal SBI Bank	65826	117178	469629	612428	815365	1627480	727466
Everest Bank	Nil	Nil	300000	Nil	Nil	Nil	312000

Fig 4.22 Growth Rate of Borrowing



Interpretation: Above table shows that Borrowing of NSBIL is in increasing trend only up to FY2007/2008 but in FY 2008/2009 it declines. However in case of EBL, bank has borrowed fund only in FY 2004/2005 and 2008/2009.

4.3 Statistical analysis:

Correlation and regression analysis

If the change in the value of one variable is accompanied by the change in the value of other, the variables said to have relationship. Regression coefficient tells you how much the dependent variable is expected to increase (if the coefficient is positive) or decrease (if the coefficient is negative) when that independent variable increases by one. In this section, various relationships between research variables are studied. Both correlation and regression results are directly obtained through **SPSS software.**

4.3.1 Correlation between Deposit and Loan and Advances

Bank mobilizes deposit for the purpose of investment and lending. Deposits are considered as raw material in banking system. It measures how much change in one variable affects other variable. It shows degree of relationship between loan and deposit. Here loan is dependent variable and deposit is independent variable.

Result of correlation between Deposit and Loan

Table 4.21

Banks	R	R square
NSBIL	0.920[a]	0.847
EBL	0.998[a]	0.996

a. Predicators :(Constant), Deposit

Table 4.22 the result of regression analysis

Banks	Model	Unstandardized coefficients		Sig
		B	Std. Error	
NSBIL	1 (Constant) Deposit	2536528.3 0 .490	1312260.7 0.093	0.111 0.003
EBL	1 (Constant) Deposit	151443.42 0.728	368105.54	0.698 0.00

a. Dependent Variable: Loan

Interpretation: From the above table 4.21, it is observed that the overall correlation (R) of NSBIL is 0.920. Relatively correlation between deposit (Independent variable) and loan (Dependent variable) is less than 1.Furthe r lies between 0.7 to 0.999. So there is high level of positive linear relationship between loan and deposit. Coefficient of determination R square of NSBIL is 0.847 which indicates that deposit has only 84.7% role in loan and rest is by other unforeseeable factor. Similarly correlation between loan and deposit of EBL is 0.998.So it shows high level of positive linear relationship between variables. However, by application of coefficient of determination the value of R^2 is 0.996 which indicates that deposit has only 99.6% role in loan and rest is by other unforeseeable factor. From above table 4.22 we can conclude that regression coefficient 'b' is positive i.e. 0.490 for NSBIL which indicates that one percentage increase in deposit leads to 49% increase in loan. In case of EBL regression coefficient is also positive i.e. 0.728 which shows that one percentage increase in deposit leads to 72.8% increase in loan.

Test of Hypothesis 1

Null Hypothesis (H0)	1. There is no significant relation between Loan and Deposit of NSBIL 2. There is no significant relation between Loan and Deposit of EBL
Alternative Hypothesis (H1)	1.There is significant relation between Loan and Deposit of NSBIL 2. There is significant relation between Loan and Deposit of EBL
Correlation coefficients (r) NSBIL EBL	 0.920 0.998
Calculated Value(tcal) NSBIL EBL	 5.266 36.734
Tabulated Value (t tab) NSBIL EBL	 2.571 2.571
Degree of Freedom (d.f.)	5

Level of significance (α)	5%
Decisions	Since T-tab <T-cal value of NSBIL, H0 is rejected that means H1 is accepted. So there is significant relation between Loan and Deposit of NSBIL Since T-tab <T-cal value of EBL, H0 is rejected that means H1 is accepted. So there is significant relation between Loan and Deposit of EBL

Detail calculation is shown in annex 19

4.3.2 Correlation between Investment and Loan and Advances

Most of banks give first priority to loan and then only excess fund are used for investment. Thus availability of fund for investment depends on lending policy. So increase and decrease in loan directly reduces or increase the volume of investment. This correlation measures the degree of relationship between investment and loan and advances of NSBIL and EBL. Here investment is independent variable and loan is dependent variable.

Result of correlation between Investment and Loan

Table 4.23

Banks	R	R square
NSBIL	0.811[a]	0.658
EBL	0.921[a]	0.849

a. Predicators :(Constant), Total Investment

Table 4.24 the result of regression analysis

Banks	Model	Unstandardized coefficients		Sig
		B	Std. Error	
NSBIL	1 (Constant) Investment	5498065.0 0.764	1373584.9 0.246	0.010 0.027
EBL	1 (Constant) Investment	-2646830 3.871	2989826.1 0.731	0.417 0.003

a. Dependent Variable: Loan

Interpretation:

From the above table 4.23, it is observed that the overall correlation (R) of NSBIL is 0.811. Relatively correlation between investment (Independent variable) and loan (Dependent variable) is less than 1.Furthe r lies between 0.7 to 0.999. So there is high level of positive linear relationship between loan and investment. Coefficient of determination R square (R^2) of NSBIL is 0.658 which indicates that investment has only 65.8% role in loan and rest is by other unforeseeable factor. Similarly correlation between loan and investment of EBL is 0.921.So it shows high level of positive linear relationship between variables. However, by application of coefficient of determination the value of R^2 is 0.849 which indicates that investment has only 84.9% role in loan and rest is by other unforeseeable factor. From above table 4.22 we can observe that regression coefficient 'b' is positive i.e. 0.674 for NSBIL and 3.871 for EBL.

Test of Hypothesis 2

Null Hypothesis (H0)	1. There is no significant relation between Loan and Investment of NSBIL 2. There is no significant relation between Loan and Investment of EBL
Alternative Hypothesis (H1)	1. There is significant relation between Loan and Investment of NSBIL 2. There is significant relation between Loan and Investment of EBL
Correlation coefficients (r) NSBIL EBL	 0.811 0.921
Calculated Value(tcal) NSBIL EBL	 3.104 5.297
Tabulated Value (t tab) NSBIL EBL	 2.571 2.571
Degree of Freedom (d.f.)	5
Level of significance (α)	5%
Decision	Since T-tab <T-cal value of NSBIL, H0 is rejected that means H1 is accepted. So there is significant relation between loan and investment of NSBIL Since T-tab <T-cal value of EBL, H0 is rejected that means H1 is accepted. So there is significant relation between Loan and Investment of EBL

Calculations are shown in Appendix 19

4.3.3 Correlation between Total Income and Loan and Advances

The correlation between total income and loan and advances measures the degree of relationship between these two variables. It shows percentage change in loan and its effects on income. Here loan is dependent variable and total income is independent variable

Results of correlation between income and loan

Table 4.25

Banks	R	R square
NSBIL	0.989[a]	0.977
EBL	0.935[a]	0.875

a. Predicators :(Constant), Total Income

Table 4.26 the result of regression analysis

Banks	Model	Unstandardized coefficients		Sig
		B	Std. Error	
NSBIL	1 (Constant) Total Income	973596.62 16.666	573287.79 1.135	0.150 0.00
EBL	1 (Constant) Total Income	-4286170 18.300	2947440.1 3.100	0.206 0.002

a. Dependent Variable: Loan

Interpretation: From the above table 4.25, we can conclude that the overall correlation R of NSBIL is 0.989, determine coefficient of correlation R square is 0.977. Relatively correlation between total income (Independent variable) and loan (Dependent variable) is less than 1.Furthe r lies between 0.7 to 0.999. So there is high level of positive linear relationship. Similarly correlation between income and loan of EBL is 0.935.Thus there is also high level of positive linear correlation between these variables. From above table 4.26 we can see that regression coefficient ‘b’ is positive for NSBIL and EBL.

Test of Hypothesis 3

Null Hypothesis (H0)	1. There is no significant relation between Loan and Income of NSBIL 2. There is no significant relation between Loan and Income of EBL
Alternative Hypothesis (H1)	1. There is significant relation between Loan and Income of NSBIL 2. There is significant relation between Loan and Income of EBL
Correlation coefficients (r) NSBIL EBL	 0.989 0.935
Calculated Value(tcal) NSBIL EBL	 14.681 5.903
Tabulated Value (t tab) NSBIL EBL	 2.571 2.571
Degree of Freedom (d.f.)	5
Level of significance (α)	5%
Decision	Since T-tab <T-cal value of NSBIL, H0 is rejected that means H1 is accepted. So there is significant relation between loan and income of NSBIL. Since T-tab <T-cal value of EBL, H0 is rejected that means H1 is accepted. So there is significant relation between Loan and Income of EBL.

Detail calculation is shown in annex 19

4.3.4 Correlation between Borrowing and Loan

The correlation between total borrowing and total loan measures the degree of relationship these two variables. Here borrowing is independent variable but loan is dependent variable.

Result of correlation between borrowing and loan

Table 4.27

Banks	R	R square
NSBIL EBL	0.718[a] 1.000[a]	0.515 1.000

a. Predicators :(Constant), Total Borrowing

Table 4.28 the result of regression analysis

Banks	Model	Unstandardized coefficients		Sig
		B	Std. Error	
NSBIL	1 (Constant) Total Borrowing	5205078.8 5.349	1851437.3 2.320	0.037 0.069
EBL	1 (Constant) Total Borrowing	-399031430 1355.500	0.000 0.000	. .

a. Dependent Variable: Loan

Interpretation: It is clear from the table 4.27 it is clear that the overall correlation R of NSBIL is 0.718, determine coefficient of correlation R square is 0.515. Relatively correlation between borrowing (Independent variable) and loan (Dependent variable) is less than 1.Furthe r lies between 0.7 to 0.999. So there is high level of positive linear relationship. Similarly correlation between borrowing and loan of EBL is 1.00.Thus there is also positive correlation between loan and borrowing. From above table 4.28 we can find that regression coefficient ‘b’ is positive for NSBIL and EBL.

Test of Hypothesis 4

Null Hypothesis (H0)	1. There is no significant relation between Loan and Borrowing of NSBIL 2. There is no significant relation between Loan and Borrowing of EBL
Alternative Hypothesis (H1)	1. There is significant relation between Loan and Borrowing NSBIL 2. There is significant relation between Loan and Borrowing EBL
Correlation coefficients (r) NSBIL EBL	 0.718 1.00
Calculated Value(tcal) NSBIL EBL	 2.305 0.0
Tabulated Value (t tab) NSBIL EBL	 2.571 2.571
Degree of Freedom (d.f.)	5
Level of significance (α)	5%
Decision	Since T-cal <T-tab value of NSBIL, H0 is accepted that means H1 is rejected. There is no significant relation between Borrowing and loan of NSBIL. Since T-cal <T-tab value of EBL, H0 is accepted that means H1 is rejected. There is no significant relation between Borrowing and loan of EBL.

Detail calculations are shown in annex 19

4.4 Primary data analysis

Questionnaires were distributed to 10 branch managers of NSBIL and 10 branch mangers of EBL within Kathmandu valley. However responses were received only from 8 branches of NSBIL and 8 branches of EBL (see details in annex16).

Following information was obtained and summarized from the questionnaire

- It is found that 100% respondent states that credit control procedures are known to other departments in both NSBIL and EBL.
- 100% respondents have mention that loan policies are communicated to all the concerned staffs and they rely on in doing work. However, 56.25% respondents strongly agree that lending policies make the task of dealing with the clients request easy and 43.75% simply agree with this statement. 50% strongly agree that lending policies help them to monitor the performance of loan.
- In NSBIL 37.50% customers offer trading loan and 31.25% customers offer housing loan and 31.25% offer personal loan. Similarly in case of EBL 37.50% offer trading loan, 25% offer housing loan, 18.75% offer personal loan and rest 12.50% offer hire purchase loan.
- 62.50% respondents of NSBIL states that highest percentage of loan is provided to corporate sector and second priority is given to small and medium sized enterprises. However in case of EBL 75% has placed corporate loan as most priority sector.
- From the responses of questionnaire it is found that first priority is given to income source for credit analysis and then collateral. Similarly personal guarantee and personal behaviors were given lesser importance. Moreover, 81.25% respondents agreed with the statement that deposit is the most important factor affecting loan and

advances and rest 18.75% has mentioned investment as most important factor. All of the 16 branch mangers say deposit has been utilized properly in profitable sector. Gap between deposit and loan is in decreasing trend in EBL.

- Most important factor responsible for growth of NPL is poor appraisal, then weak monitoring and recovery and finally high volume of loan. Legal system has been one of the most important obstacles in loan recovery and then lack of infrastructure. However 100% respondents have mentioned that NPL is not a serious problem in both banks.
- NSBIL and EBL have up to date information about loan repayment. From the analysis of questionnaire responses, it is clear that NSBIL has set up own NPA department at corporate office for loan collection.
- In order to assess the creditworthiness of the new customer, income source is the minimum factor and likewise audited financial statement and credit agency report are also important.
- NSBIL and EBL have good credit risk management mechanism. In NSBIL credit risk are properly identified and managed through analysis of background, Income, personal guarantee and past record of the customer. In case of EBL credit risk is analyzed through the financial statement of the business and compare with acceptable level of risk and also industry analysis is conducted.75% says that credit risk is critical for NSBIL and 25% says liquidity risk is critical likewise 62.25% says that credit risk is critical for EBL and 37.75% says liquidity risk.

5.1 Summary

A modern financial system is important in the economy in order to pool and utilize financial resources, reduce cost and risk, expand and diversify opportunities, increase productivity and facilitate economic growth. Similarly growth of financial services sector is important for economic growth. Banking sector provides these financial services and commercial banks provides various banking and financial services to the customers. Commercial banks take deposits from individual and institutional customers, which they then use to extend credit to other customers. They make money by earning more in interest from borrowers than they pay in interest to those whose deposits they accept.

Basically banks in Nepal have been facing following problems in credit and investment sector. They provide loan against only fixed collateral but fails to focus on easy recovery part. Banking sector doesn't have qualified credit staffs and credit appraisal /analysis regarding borrower and any business entity have not been done according to financial norms and internationally accepted standard.

Loan management is simply management of loan and advances. Success of banking business depends on the efficient and effective management of loan. Poor loan management has proved to be one of the major causes of bank failure throughout the world. Thus loan management is always a challenging task in banking since it involves risk linked with credit operations.

Main objective of research is to analyze loan management practices of commercial banks and come out with solid recommendation to enhance loan management. However specific objectives are (a) to assess loan management process, system and practices.(b) to evaluate capability of loan management to reduce the impact of non-performing loan.(c) to assess loan disbursement and its recovery.(d) to examine interest rate on loan and deposit and repayment of loan.(e) to explore relationship between loan, deposit, investment, income, borrowing and their impact on profit and performance of bank.(f) to analyze different benefits that the loan management might bring.

Research work is designed to obtain answer of all research questions. This research has adopted descriptive and analytical research method to analyze and interpret data. Total 27 commercial banks are population for the study and sample of two banks are taken using random sampling method. In order to meet research objective, data which has been collected for the analysis purpose are of primary and secondary in nature but study is more based on secondary data and data of seven years were selected for study. Primary data collected through questionnaire is of qualitative nature

The study has used financial and statistical tools to analyze data collected. Financial tools include ratio analysis i.e. Lending Efficiency Ratios, Asset Management Ratios, Profitability Ratios, Leverage ratios and Liquidity Ratios and statistical tools are mean, correlation and regression.

5.2 Finding:

1. **From lending efficiency ratio analysis**

- It is found that NSBIL and EBL have been able to maintain deprived sector loan ratio as set by NRB as ratio is near to 3% for deprived sector lending but both banks are not investing fund to priority sector as per NRB directives. According to NRB directives, the priority sector lending should be 12% of the total lending and the deprived sector lending should be 3% of total lending.

- From the analysis of loan loss provision to total loan ratio, it is found that NSBIL has lowest loan loss provision as compare to EBL. However on average EBL has lower loan loss provision ratio than NSBIL.
- Similarly, NPL to total loan ratio of both banks are in decreasing trend but on an average, EBL has lowest ratio as compare to NSBIL. So EBL has good non performing loan management and better quality of assets .In other hand it is found that credit risk management of EBL is better than NSBIL. The result reveals that EBL is able to manage credit efficiently as a result recovery is quite good

2 From asset management ratios analysis

- Loan to deposit Ratio of both banks is in fluctuating trend but on an average EBL has highest ratio as compare to NSBIL. So EBL has been able to mobilize its deposit efficiently as compare to NSBIL .So EBL has been able to manage its assets effectively. Although there is not any standard for CD Ratios in Nepal, a ratio of 75% can be accepted to be adequate. As such both banks are somehow nearer to this standard.
- Similarly investment to total deposit ratio of EBL is highest as compare to NSBIL during study period. It is found that EBL has successfully mobilized its deposit through investment.
- Further loan to total asset ratio of both banks is also fluctuating during study period but on an average EBL has highest ratio as compare to NSBIL. Thus it is found that EBL has better performance in mobilizing its fund by the way of lending activities

3. From profitability ratio analysis

- NSBIL has highest interest income to total income ratio during entire study period than EBL. It is found that in case of NSBIL, interest income has highest contribution in total income than EBL. NSBIL is largely dependent on lending activities and investment but EBL low interest income to total income shows low contribution made by lending and investment and high contribution by other fee based activities in total income
- Similarly EBL has highest interest income to interest expenses ratio than NSBIL. This indicates that EBL has more ability to meet its expenses from interest income than NSBIL.
- Further interest income to total assets ratios of both banks were fluctuating during study period but average ratio of EBL is higher than NSBIL. EBL has ability in mobilizing lower cost funds and investing them at a reasonably higher interest and assets are effectively utilized to generate income.

4 From leverage ratio analysis

- NSBIL has higher total borrowing to total assets ratio than EBL .However EBL has borrowed fund only in FY 2002/2003 and 2008/2009.So in NSBIL borrowing has more contribution in total assets. So NSBIL is more levered firm.
- Similarly total liabilities to total capital ratio of NSBIL and EBL were in fluctuating trend. But in an average EBL has highest ratio than NSBIL. This means that EBL assets are more provided through debt.

5. From liquidity ratio analysis

- On an average NSBIL has a highest cash and bank balance to total deposit ratio than EBL. Thus it is found that NSBIL has more cash ideal but better liquidity than EBL. As EBL has maintained the ratio of cash and bank balance to total deposit considerably lower than NSBIL, it is recommended to increase cash and bank balance to meet loan demand.
- Similarly EBL has higher liquid fund to total deposit ratio as compare to NSBIL and balances with NRB to total deposit ratio of EBL is higher than NSBIL. Thus the bank has been able to maintain the confidence of investors and depositors.

6. From correlation and regression analysis

- There is high level of positive relationship between loan and deposit, between loan and investment and between loan and total income of NSBIL and EBL.
- Similarly regression analysis of loan and deposit, loan and investment and loan and total income of both banks are significant
- But result shows that regression analysis of loan and borrowing is not significant for both banks.

7. From growth ratio analysis

- Growth ratios of deposit of both banks are in increasing trend but comparatively EBL has been able to collect deposit than NSBIL.
- Similarly growth of loan and advances of both banks are in increasing trend but comparatively EBL has provided more loan than NSBIL during seven year study period.

- Further growth of total investment NSBIL is in increasing trend up to FY 2005/2006 and decreases in FY2006/2007.Thereafter it increases. But in case of EBL investment increases only from FY 2005/2006.
- Growth of total income and of NSBIL is in incresing trend but in case of EBL it is fluctuating trend during seven year period.
- Borrowing of NSBIL is in increasing trend only up to FY2007/2008 but in FY 2008/2009 it declines but in case of EBL it has borrowed fund only in FY 2002/2003 and 2008/2009.

5.3 Conclusion

This study shows that there is a significant relationship between bank performance and loan management. The availability of cash and loanable funds are important to the successful operations of a commercial bank. However, if there is excess cash, it could lead to a waste of resources unless properly channeled in to loans. If cash is insufficient to meet the demands of customers, especially depositor’s withdrawals and credible borrowers, it could lead to loss of public confidence and consequent run on the commercial bank leading to bank failure. As a result, a commercial bank has to hold a certain amount of cash that will meet with depositor’s withdrawal requirements and other liquidity needs of the commercial bank.

Research Question one: How effectively these two banks have followed lending policies? From the primary data collection it is concluded that both NSBIL and EBL staffs has been following lending policies effectively.

Research Question two: Whether trend of loan and advances and deposits are in satisfactory position or not? From the analysis of growth rate of loan and advances and deposit of two banks it is concluded that growth of loan and deposit are in increasing during study period. However EBL has been able to collect more deposit and use it to provide loan as compare to NSBIL. Thus trend of loan and deposit is in satisfactory position.

Research Question three: How these banks measure liquidity and impact of loan and deposit on liquidity? Liquidity is measured by cash and bank balances to total deposit ratio, liquid fund to total deposit ratio. From the ratio analysis it is concluded that NSBIL has better liquidity position than that of EBL.

Researches Question four: How bank measure lending performance and efficiency? Lending efficiency is measured by loan loss ratio and NPL ratio. From the analysis it is concluded that on an average EBL has lower loan loss provision ratio than NSBIL. NPL to total loan ratio of both banks are in decreasing trend but comparatively EBL has lowest ratio as compare to NSBI. It is also concluded that both banks are not investing fund to priority sector as per NRB directives.

It can be concluded that loan and advances are the profitable assets for the banks and also it is very risky too. Due to this reason, the loan and advances should be effectively managed and controlled. Loan management deals with managing loan and advances with maintaining adequate liquidity position. This study shows that there is a significant relationship between bank performance and loan management. Better loan management results in better bank performance. Thus, it is of crucial importance that banks practice better loan management and safeguarding the assets of the banks and protect the investors' interests. The study summarizes that banks used different kind of loan management tools and techniques to manage their credit risk, and that they all have one main objective, i.e. to reduce the amount of loan default which is a principal cause of bank failure. The study also reveals that banks with good or sound credit risk management and loan policies have lower loan default ratios (bad loans) and higher interest income (profitability).The main conclusion of this research paper is that loan management can contribute to solving the problem of increasing non performing loan and help to manage loan, deposit and investment so as to improve overall performance of organization.

5.4 Recommendation

Based on above finding and conclusion, the following recommendations have been made

1. The loan loss provision ratio and credit risk of EBL is lower than that of NSBIL. However NPL of both banks are decreasing but NPL is lower in EBL than NSBIL, it is recommended for NSBIL to adopt good loan monitoring system, follow up of borrower and recovery of loan in time to reduce NPL further.

2. The ratio of loan to deposit, Investment to deposit and loan to total assets of EBL is higher as compare to NSBIL .It shows large portion of fund invested as loan and negligence to invest in other sector. However NSBIL has not been able to utilize its deposit as loan and advances. It is strongly recommended for NSBIL to make maximum utilization of fund by adopting loan portfolio diversification strategy and follow liberal credit and investment policy to invest more percentage of deposit as loan and makes investment in different areas, institutions and securities.

3. EBL has ability in mobilizing lower cost funds and investing them at a reasonably higher interest and assets are effectively utilized to generate income than NSBIL. This indicates that EBL has more ability to meet its expenses from interest income than NSBIL. So it is recommended for NSBIL to enhance its operating and financial efficiency

4. EBL needs to increase its net income by increasing deposits, decreasing cost and expanding more branches. As the net income of EBL is fluctuating, the bank should try to keep it at a stable point.

5. As the liquidity position of EBL is higher than that of NSBIL. So they are recommended to look upon new area of lending and investment. As EBL has maintained the ratio of cash and bank balance to total deposit considerably lower than NSBIL, it is recommended to increase cash and bank balance to meet loan demand.

6. Although most of the banks have recently expanded their branches all over the country but some of them do not have branches in rural areas of the country. So they are recommended to open branches in rural areas and make core banking services available to the rural peoples. In spite of political instability and Maoist problem, there is huge potentiality to invest in hydro sector, tourism, small and cottage industries and agriculture.

7. Necessary steps should be taken to improve the reporting system for easy transfer of funds. In this context, the need for introducing Management Information System (MIS) may be explored.

8. EBL and NSBIL are recommended to be serious towards research and development. NABIL should research for more profitable areas and for more deposits. The innovation

on profitable sectors may lead a bank to bright future. So, NABIL should research for such sector and develop it.

9. Deposits mobilization programs on TV's, radio; newspapers should be carried out to motivate the people. Pamphlets, posters should be distributed to male the people aware of banking business. Such motivational programs help the people aware of banking business.

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ANNEXES

Annex 1

Sector wise loan classification
Deprived Sector Loan Ratio

FY	Nepal SBI Bank			Everest Bank		
	Deprived sector loan	Total Loan	Ratio	deprived sector loan	Total Loan	Ratio
04/05	212500	623879	0.340611	225124	7618670	0.029549
05/06	235700	7626736	0.030904	297000	9801308	0.030302
06/07	280500	9460451	0.02965	370600	13664082	0.027122
07/08	356900	12113698	0.029463	523800	18339085	0.028562
08/09	441500	15131748	0.029177	716900	23884674	0.030015

Source: Annual Report of Bank Supervision Department of NRB

Annex 2

Priority Sector Loan

FY	Nepal SBI Bank			Everest Bank		
	Priority sector loan	Total Loan	Ratio	Priority sector loan	Total Loan	Ratio
04/05	831300	623879	0.1338	718601	7618670	0.094321
05/06	744400	7626736	0.097604	847300	9801308	0.086448
06/07	370600	9460451	0.039174	125900	13664082	0.009214
07/08	Nil	12113698		10900	18339085	0.000594
08/09	Nil	15131748		100200	23884674	0.004195

Source: Annual Report of Bank Supervision Department of NRB.

Annex 3

Loan Loss Provision to Total Loan Ratio

FY	Nepal SBI Bank			Everest Bank		
	Loan Loss Provision	Total Loan	Ratio	Loan Loss Provision	Total Loan	Ratio
02/03	84173	4468719	0.018836	45746	4908461	0.00932
03/04	118725	5143662	0.023082	81780	5884124	0.013898
04/05	193243	6213879	0.0311	88927	7618670	0.011672
05/06	146657	7626736	0.019229	70466	9801308	0.007189
06/07	59377	9460451	0.006276	89696	13664082	0.006564
07/08	57464	12113698	0.004744	99340	18339085	0.005417
08/09	40349	15131748	0.002667	93085	23884674	0.003897
Average (Mean)			0.0151			0.0083

Source: Annual Report of Bank Supervision Department of NRB.

Annex 4

NPL to Total Loan Ratio

FY	Nepal SBI Bank			Everest Bank		
	NPL	Total Loan	Ratio	NPL	Total Loan	Ratio
02/03	4269000	4468719	0.0955	111190	4908461	0.022653
03/04	345820	5143662	0.0672	104760	5884124	0.017804
04/05	441020	6213879	0.071	128810	7618670	0.016907
05/06	505300	7626736	0.0663	129200	9801308	0.013182
06/07	48800	9460451	0.0052	113170	13664082	0.008282
07/08	464900	12113698	0.0384	121000	18339085	0.006598
08/09	305660	15131748	0.0202	117450	23884674	0.004917
Average (Mean)			0.052			0.012906

Source: Annual Report of Bank Supervision Department of NRB

Annex 5
Loan to Deposit Ratio

FY		Nepal SBI	Bank	Everest	Bank	
	Loan	Deposit	Ratio	Loan	Deposit	Ratio
02/03	4468719	6522817	0.68509	4908461	6694964	0.733157
03/04	5143662	7198327	0.714564	5884124	8063902	0.729687
04/05	6213879	8654774	0.718	7618670	10097691	0.754496
05/06	7626736	11002041	0.693211	9801308	13802445	0.710114
06/07	9460451	11445286	0.826581	13664082	18186254	0.751341
07/08	12113698	13715395	0.883219	18339085	23976298	0.764884
08/09	15131748	27957221	0.541247	23884674	33322946	0.634811
Average (Mean)			0.7231			0.725499

Source: Annual Report of Bank Supervision Department of NRB

Annex 6
Investments to Total Deposit Ratio

FY	Nepal SBI Bank			Everest Bank		
	Investment	Deposit	Ratio	Investment	Deposit	Ratio
02/03	1207275	6522817	0.185085	1653978	6694964	0.247048
03/04	1907521	7198327	0.264995	2535658	8063902	0.314446
04/05	2607680	8654774	0.3013	2128932	10097691	0.210834
05/06	3610775	11002041	0.328191	4200515	13802445	0.304331
06/07	2659453	11445286	0.232362	4984315	18186254	0.274071
07/08	3088887	13715395	0.225213	5059557	23976298	0.211023
08/09	13286182	27957221	0.219592	5948480	33322946	0.223107
Average (Mean)			0.251			0.255

Source: Annual Report of Bank Supervision Department of NRB.

Annex 7
Loan to Total Assets Ratio

FY	Nepal SBI Bank			Everest Bank		
	Loan	Total Assets	Ratio	Loan	Total Assets	Ratio
3-Feb	4468719	7566327	0.5906	4908461	8052209	0.6096
4-Mar	5143662	8440406	0.6094	5884124	9608571	0.6124
5-Apr	6213879	10345373	0.6006	7618670	11792126	0.6461
6-May	7626736	13035839	0.5851	9801308	15959285	0.6141
7-Jun	9460451	13901200	0.6805	13664082	21432574	0.6375
8-Jul	12113698	17187446	0.7048	18339085	27149342	0.6755
9-Aug	15131748	30916682	0.4894	23884674	36916849	0.647
Average (Mean)			0.6086			0.6346

Source: Annual Report of Bank Supervision Department of NRB.

Annex 8
Interest Income to Total Income Ratio

FY	Nepal SBI Bank			Everest Bank		
	Interest Income	Total Income	Ratio	Interest income	Total Income	Ratio
02/03	469740	177920	2.640175	520173	635332	0.818742
03/04	493598	237679	2.076742	657249	785059	0.837197
04/05	578372	319942	1.80774	719298	556419	1.292727
05/06	708719	464899	1.524458	903411	662153	1.364354
06/07	831117	533511	1.557825	1144408	841332	1.360234
07/08	970513	638059	1.52104	1548657	1209898	1.27999
08/09	1460446	828666	1.762406	2186815	1544966	1.415445
Average (Mean)			1.8415			1.1955

Source: Annual Report of Bank Supervision Department of NRB.

Annex 9
Interest Income to Interest Expenses Ratio

FY	Nepal SBI Bank			Everest Bank		
	Interest Income	Interest Expenses	Ratio	Interest Income	Interest Expenses	Ratio
02/03	469740	291820	1.609691	520173	307639	1.690855
03/04	493598	255919	1.928727	657249	316366	2.077496
04/05	578372	258430	2.238022	719298	299566	2.401134
05/06	708719	334770	2.117033	903411	401397	2.250667
06/07	831117	412262	2.015992	1144408	517166	2.212845
07/08	970513	454918	2.13338	1548657	632609	2.448048
08/09	1460446	824700	1.770882	2186815	1012874	2.15902
Average (Mean)			1.9734			2.1772

Source: Annual Report of Bank Supervision Department of

Annex 10
Interest Income to Total Assets Ratio

FY	Nepal SBI Bank			Everest Bank		
	Interest Income	Total Assets	Ratio	Interest Income	Total Assets	Ratio
02/03	469740	7566327	0.062083	520173	8052209	0.0646
03/04	493598	8440406	0.05848	657249	9608571	0.068402
04/05	578372	10345373	0.055906	719298	11792126	0.060998
05/06	708719	13035839	0.054367	903411	15959285	0.056607
06/07	831117	13901200	0.059787	1144408	21432574	0.053396
07/08	970513	17187446	0.056466	1548657	27149342	0.057042
08/09	1460446	30916682	0.047238	2186815	36916849	0.059236
Average (Mean)			0.353839			0.369508

Source: Annual Report of Bank Supervision Department of NRB.

Annex 11
Total Borrowing to Total Assets Ratio

FY	Nepal SBI Bank			Everest Bank		
	Total Borrowing	Total Assets	Ratio	Total Borrowing	Total Assets	Ratio
02/03	65826	7566327	12.9805	Nil	8052209	
03/04	117178	8440406	10.2532	Nil	9608571	
04/05	469629	10345373	15.0085	300000	11792126	0.0254407
05/06	612428	13035839	11.6412	Nil	15959285	
06/07	815365	13901200	14.043	Nil	21432574	
07/08	1627480	17187446	14.7747	Nil	27149342	
08/09	727466	30916682	21.8554	312000	36916849	0.0084514
Average (Mean)			14.3652			0.00484

Source: Annual Report of Bank Supervision Department, NRB

Annex 12
Total Liabilities to Total Capital Ratio

FY	Nepal SBI Bank			Everest Bank		
	Total Liabilities	Total Capital	Ratio	Total Liabilities	Total Capital	Ratio
02/03	7566327	582900	12.980489	8052209	587100	13.71523
03/04	8440406	823200	10.253166	9608571	665800	14.43162
04/05	10345373	689300	15.00852	11792126	980300	12.0291
05/06	13035839	1119800	11.641221	15959285	832500	19.17031
06/07	13901200	989900	14.043035	21432574	963600	22.24219
07/08	17187446	1163300	14.774732	27149342	1601500	16.95245
08/09	30916682	1414600	21.855423	36916849	2066500	14.07727
Average (Mean)			14.3653			16.08831

Source: Annual Report of Bank Supervision Department of NRB.

Annex 13
Cash and Bank Balances to Total Deposit:

FY	Nepal SBI Bank			Everest Bank		
	Cash and Bank Balances	Deposit	Ratio	Cash and Bank Balances	Deposit	Ratio
02/03	439410	6522817	0.067365	409238	6694964	0.061126
03/04	283974	7198327	0.03945	189561	8063902	0.023507
04/05	333719	8654774	0.038559	270320	10097691	0.026771
05/06	492035	11002041	0.044722	413452	13802445	0.029955
06/07	566011	11445286	0.049454	1213222	18186254	0.066711
07/08	939151	13715395	0.068474	1587058	23976298	0.066193
08/09	1459767	27957221	0.052214	1377208	33322946	0.03918
Average (Mean)			0.051463			0.044778

Source: Annual Report of Bank Supervision Department of NRB.

Annex 14
Liquid Fund to Total Deposit Ratio

FY	Nepal SBI Bank			Everest Bank		
	Liquid Fund	Deposit	Ratio	Liquid Fund	Deposit	Ratio
02/03	1331600	6522817	0.204145	1156100	6694964	0.172682
03/04	775000	7198327	0.107664	869700	8063902	0.107851
04/05	459600	8654774	0.053104	1624200	10097691	0.160849
05/06	894500	11002041	0.081303	1619600	13802445	0.117342
06/07	1754500	11445286	0.153295	3329700	18186254	0.183089
07/08	1651600	13715395	0.120419	3198400	23976298	0.133398
08/09	1910900	27957221	0.068351	6164400	33322946	0.12503
Average (Mean)			0.112611			0.142892

Source: Annual Report of Bank Supervision Department of NRB.

Annex 15
Balance with NRB to Total Deposit Ratio

FY	Nepal SBI Bank			Everest Bank		
	Balance with NRB	Total Deposit	Ratio	Balance with NRB	Total Deposit	Ratio
02/03	894124	6522817	0.137076	730331	6694964	0.109087
03/04	580453	7198327	0.080637	442243	8063902	0.054842
04/05	390026	8654774	0.045065	779669	10097691	0.077213
05/06	626123	11002041	0.05691	1139515	13802445	0.082559
06/07	556678	11445286	0.048638	1178198	18186254	0.064785
07/08	403810	13715395	0.029442	1080915	23976298	0.045083
08/09	444139	27957221	0.015886	4787164	33322946	0.061938
Average (Mean)			0.059094			0.070787

Source: Annual Report of Bank Supervision Department of NRB.

Annex 16

Analysis of Interview Questionnaire for Bank Officials:

Q.No.2 Credit control procedures are known to other departments.

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
a) Yes	7	8	100%	100%
b) No	Nil	Nil		
Total	7	8		

Q.No.3 Loan policies are communicated to all the concerned staffs

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
a) Yes	7	8	100%	100%
b) No	Nil	Nil		
Total	7	8		

Q.No.5 I believe that you have lending policies rely on in doing your work?

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBI	EBL
a) Yes	7	8	100%	100%
b) No	Nil	Nil		
Total	7	8		

Q.No.9 Are you using your deposit properly in profitable sector?

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
a) Yes	7	8	100%	100%
b) No	Nil	Nil		
Total	7	8		

Q.No.13 Is non performing loan a serious problem in your bank?

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
a) Yes	7	6	100%	75%
b) No	Nil	2		25%
Total	7	8		

Q.No.15 Are you up to date with your loan repayments?

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
a) Yes	7	8	100%	100%
b) No	Nil	Nil		
Total	7	8		

Q.No.19 Do you have credit risk mechanism?

Options	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
a) Yes	7	8	100%	100%
b) No	Nil	Nil		
Total	7	8		

Q.No.18 For new customers, what is the minimum information required assessing the Creditworthiness of the customer? Do you use:

Options	No. of Responses	Percentage
(I) Credit Agency Reports a) Yes	12	75%
b) No	4	25%
Total	16	
(II) Audited financial statements a) Yes	13	81.25%
b) No	3	18.75%
Total	16	
(III) Income source a) Yes	16	100%
b) No	Nil	
Total	16	

Analysis of Likert scale questions

Question no. 4 Lending policies

Scale	1	2	3	4	5	Total
make task of dealing with the client's request easy	9	7				16
	56.25%					
Help me to monitor the performance of the loan	8	8				16
	50%	50%				
makes flexibility in handling the customer's request		4		5	7	16
		25%		31.25%	43.75%	
Following policies continuously	9	7				16
	56.25%	43.75%				
help me to make good loan decisions	6	10				16
	37.50%	62.50%				

Question no. 12

Obstacles in loan recovery

Scale	1	2	3	4	5	Total
There is shortage of adequate and skilled manpower			8	5	3	16
			50%	31.25%	18.75%	
The lack of infrastructure is a major obstacle in loan recovery		10	6			16
		62.50%	37.50%			
Lack of cooperation among the higher authority			4	12		16
			25%	75%		
legal system is weak	2	14				16
	12.50%	87.50%				

Ranking analysis

Question no. 7 Credit analysis

Criteria for credit analysis	1	2	3	4	5	Total
Income source	7	4	3			16
	43.75%	25%	18.75%			
Personal Background	2	4	5		5	16
	12.50%	25%	31.25%		31.25%	
Personal guarantee		3	3	5	5	16
		18.75%	18.75%	31.25%	31.25%	
Collateral	4	6	6			16
	25%	37.50%	37.50%			
Personal behaviors		4		3	9	16
		25%		18.75%	56.25%	

Question no.6 what kinds of loan do client offer the most?

Types of loan	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
Trading	6	6	37.50%	37.50%
Housing	5	4	31.25%	25%
Personal	5	3	31.25%	18.75%
Share loan				
Hire purchase loan		2		12.50%
Commercial		1		
Total	16	16		

Question 17 In which sector your organization is providing highest loan?

Sectors	No. of Responses		Percentage	
	NSBIL	EBL	NSBIL	EBL
Corporate sector	10	12	62.50%	75%
Large organization				
Medium sized organization				
Small-medium sized enterprises	6	4	37.50%	25%
Micro-enterprises				
Total	16	16		

Question no. 11
Factor responsible for growth of NPL

Scale	1	2	3	4	5	Total
Inefficient management			4		12	16
			25%		75%	
Competition			3%		13%	16
			18.75%		81.25%	
Poor appraisal	7	9				16
	43.75%	56.25%				
High volume of loan	4			12		16
	25%			75%		
weak monitoring and recovery	5	11				16
	31.25%	68.75%				

Q. No.8 What is the most important factor affecting loan and advances in your organization?

Variables	No. of Responses	Percentage
Deposit	13	81.25%
Investment	3	18.75%
Total Income		
Borrowing		
Total	16	100%

Q. No 21 what is the key risk factor do you think critical for the organization?

Variables	No. of Responses		Percentage	
	NSBIL	EBL	NSBSIL	EBL
Credit risk	12	10	75%	62.25%
Interest risk				
Liquidity risk	4	6	25%	37.75%
Price risk				
Total	16	16		

ANNEX 17

Tribhuvan University
Faculty of Management
St.Xaviers College
Maitighar, Kathmandu

Private and Confidential

EVEREST /NEPAL SBI BANK SURVEY QUESTIONNAIRE

Name of researcher: Prakash Thapa
Email address: luckythapa22@gmail.com
Name of college: St.Xavier's college
Department: Management

QUESTIONNAIRE FOR BRANCH MANAGER

I humbly request your time to complete the attached questionnaire on Master level research work in the topic loan management of EBL and NSBIL to assess the effectiveness of loan management practices and its impact on overall performance of bank. The study is being conducted as per partial requirement of MBS program of Tribhuvan University. Responses to this questionnaire will be used to develop general findings and conclusions. Responses to the questionnaire should be completed in as much detail as possible, and supported by relevant statistics and data where available. To enable the researcher to come up with a meaningful evaluation of the foregoing subject, please answer all the items in the questionnaire.

Thank you!

Name of respondent ______________________________

Qualification ______________________________

Position ______________________________

Name of Branch name ______________________________

No of years with the bank ____________________

No of years in present position ____________________

Direction: Please check the appropriate answer. If a question requires several answers as applicable in your case, please check accordingly. There is no right or wrong answer.

A. Credit Department Structure

1. Who are the senior members of the Credit Department, or who is the individual primarily responsible for making credit decisions?

Name	Designation	Year of experiences in credit

2. Credit control procedures are known to other departments.

☐ Yes ☐ No

B. Loan policies

3. Loan policies are communicated to all the concerned staffs

☐ Yes ☐ No

4. Please use the following likert scale in order to give us your response to the following Questions:-

1	2	3	4	5
Strongly Agree	Agree	I am not sure	I disagree	I strongly disagree

Lending policies

Institutional lending guidelines make the task of dealing with the client's request easy					
The institutional lending procedures help me to monitor the performance of the loan					
The lending guidelines deprive me of flexibility in handling the customer's request					
I have continuously followed lending policies					
lending policies help me to make good loan decisions					

5. I believe that you have lending policies rely on in doing your work?

☐ Yes ☐ No

6. What kind of loan do client offer the most?

☐ Trading ☐ Housing Loan ☐ Personal Loan ☐ Share Loan

☐ Hire purchase loan ☐ Commercial loan

C. Credit/Loan analysis

7. Could you please rank (1-5) the following criteria considered in the credit analysis?

Criteria	Rank
Income source	
Personal Background	
Personal guarantee	
Collateral	
Personal behaviors	

8. What is the most important factor affecting loan and advances in your organization? (Direction: Please use tick mark)

(a) Deposit (b) Investment (c) Income (d) Borrowing

9. Are you using your deposit properly in profitable sector?

☐ Yes ☐ No

10. The gapping between deposit and credit is increasing .why?

....

....

D. Non Performing Loan Management and Loan Recovery

11. In a scale of 1-5, rank the following factor responsible for growth of NPL in your organization.

Factors	Rank
Inefficient management	
Competition	
Poor appraisal	
High volume of loan	
weak monitoring and recovery	

12. Please use the following scale in order to give us your response to the following Questions:-

Obstacles in loan recovery

1	2	3	4	5
Strongly Agree	Agree	I am not sure	I disagree	I strongly disagree

There is shortage of adequate and skilled manpower					
The lack of infrastructure is a major obstacle in loan recovery					
Lack of cooperation among the higher authority					
legal system is weak					

If others, Please specify					

13. Is non performing loan a serious problem in your bank?

☐ Yes ☐ No

14. How your organization is managing Non-performing loan?

____

15. Are you up to date with your loan repayments? ☐ Yes ☐ No

16. Loan collection procedure ______________________________

____

Please attach separately any written loan procedures you may have and or any additional comments you may wish to make regarding your loan procedures.

E. Loan Diversification

17. In which sector your organization is providing highest loan?

☐ Corporate sector organization ☐ large organization

☐ Medium sized organization ☐ Small- medium sized Enterprises

☐ Micro Enterprises

F. Loan Evaluation

18. For new customers, what is the minimum information required assessing the creditworthiness of the customer? Do you use:

(I) Credit Agency Reports Yes ☐ No ☐

(II) Audited financial statements Yes ☐ No ☐

(III) Income source Yes ☐ No ☐

(IV) Other sources ____________

19. Do you have credit risk mechanism Yes ☐ No ☐

20. How credit risk are identified and managed in your organization?

____

____

21. What is the key risk factor do you think critical for the organization?

(Note: Please use tick mark sign)

a) Credit risk   b)   Interest risk   c) Liquidity risk   d)   Price risk

....

Signature

The End

ANNEX 18

REGULATORY MEASURES OF NRB ON ECONOMIC REPORT 2008/2009

1. Banks and financial institutions are not allowed to deposit and involve in credit transactions with other institutions involved in credit and deposit transactions as per other prevailing laws except to the "Bank and Financial Institution Act-2063". However, this provision will not be applicable to those institutions, which are involved in wholesale micro credit. Likewise, banks and financial institutions except their own certificate of fixed deposits are not allowed to provide loans against the certificate of deposits issued by other banks and financial institutions. Renewal of such loans against the certificate of deposits issued by other banks and financial institutions, if already are in existent, are not allowed after the maturity date. Further, Banks and financial institutions, while accepting deposits from individuals, firms and other institutions are not allowed to provide other facilities such as fees and commissions besides the interest payment on such deposits and are required to pay interest on deposits quarterly if they are charging interest on loans on quarterly basis

2. Borrowings of banks and financial institutions should not exceed one-third of total deposit mobilization. However, this provision will not be applicable to 'D' class licensed institutions.

3. "A", "B" and "C" class banks and financial institutions, which have already provided loans to the deprived sector as per the requirement of 3, 2 and 1 percent respectively, can deposit 0.25 percent, 0.5 percent, 0.75 percent and remaining balances of one-third amount of deprived sector loan by mid-May 2009, mid-July 2009, mid-Oct 2009 and mid-Jan 2010 respectively to the account opened in its own institution under the name of "Youth and Small Enterprises Self-Employment Fund of the Ministry of Finance, GON". However, this provision will not restrict the banks and financial institutions to deposit the amount exceeding this requirement. The amount deposited under the fund will be eligible to count under deprived sector. Moreover, the loan under the fund will be counted as a good loan and banks can classify the loan as claims on the government as per BASEL II. "B" and "C" class licensed institutions can assign zero risk weight to such loans.

4. Loans up to Rs 0.2 million provided by banks and financial institutions to the youth and small entrepreneurs as per "Youth and Small Enterprise Self-Employment Fund" bylaw will be counted as a loan under the deprived sector. The housing and real estate credit disbursed on the following conditions to the persons eligible for deprived class will be treated as deprived sector credit: (a) credit upto Rs 0.4 million provided directly or indirectly to group or person with secured collateral.