CHAPTER I
INTRODUCTION

1.1 Background

Bank simply means a financial institution, which is engaged in monetary transactions. Basically, banks as intermediations between depositors and borrowers in an company which are distinguished from other types of financial firms by offering deposit and loan products, (Heffernan, 1980). The bank helps people in every sector of economy like trade, industry, agriculture etc. Therefore, we call a bank as a social institution also. A bank simply carries out the work of exchanging money, providing loan affecting deposits and transaction money.

An institution established by law, which deals in money and credit is called banks. When a bank performs multiple tasks, the efficiency and effectiveness of works Becomes weak. Hence different banks are established for different purpose. The commercial bank is the oldest form of bank. There is considerable change in the original form of commercial bank. In general, banks mean the commercial bank. Hence, the definitions of bank are also equally applicable to commercial banks. The Profit maximization is the main objective of these banks.

“Bank is an establishment for the custody of money received from or on behalf of its Customers. Its essential duty is to pay their drafts on it, its profits arise from its use the Money left unemployed by them”,(Thapa,2012)

A commercial bank is therefore any financial institution that receives, collects, transfer, pays, exchanges, lends, invests or safeguards money for its consumers. To accept money as deposit form it's customer and to lend such collected fund to individuals, businesses and individual communities are two major functions of a bank. When bank provides loan new business and industries is established which helps in the development of the country. In this way whole infrastructure of national development, direction of economy rate of progress is strengthened by banking system. The primary issue of development is to increase the investment in productive sector of economy. Such as industries and commercial, production, trade and commerce, international business, generation of individual income and expenditure, government revenue, etc.

Generally, bank refers to a commercial bank at present. Therefore, the activities of a commercial bank are synonyms to banking. Commercial banks pool scattered fund and channels it to productivity use. It can be of various forms such as deposits banks, saving banks, industrial banks, mixed banks, exam banks etc. In absence of commercial banks, it would have been impossible to meet the financial needs of the country.

Commercial bank plays a significance role in the development of national economy. A bank is a financial institution that primarily deals with accepts deposits and deals in credit. Here financial Institution refers to that business concern that is mainly confined to finance for the development, for the trade, commerce and industry so does the bank, trade, commerce and industry are the prime factors of the economic development. In Nepal, among the available financial institutions, banking industry dominates all. Thus, banks are vital part of national economy and a vehicle for the business and service enterprise. Modern bank performs many varieties of functions. Therefore, it is difficult to define the function of modern banks because of their complexity and versatility in operation.

Non-performing loan is the quantum risk assets those are not performing well and are in the verge of being written off at the cost of organization's profit earned or more correctly at the cost of stakeholder by this way or that way. Basically by reducing the value of the stakeholder wealth in every aspect Keeping these views into consideration this study will concentrate on the non-performing loan and it's impact on Nabil Bank, Global IME bank and Agriculture bank limited.

Non-performing loans reflect the health of the financial system affecting the profitability. A non-performing loan is any obligation or loan in which interest and the principal payments are more than 90 days overdue, more than 90 days' worth of interest has been refinanced, capitalized or delayed by agreement or if payments are less than 90 days overdue but payments are no longer anticipated (IMF, 2018). Non-performing loan refers to those unproductive assest of any firm that cannot be converted into cash within specific time limit. It is the loan made by a bank or financial company on which interest payments and principal repayments are not being made on time.

If the credit allowed by banks and financial institutions turns bad, it creates NPL. NPL percentage in assest portfolio shows the health of a bank. The performance of any financial institution is greatly measured with the coverage of NPL in that particular institution. Since the prime sources of income for the bank are generated through income from loan and advances, increase in non-performing loan may lead bank in the verge of collapse. The loan and advances which is overdue for 3 months or more should be treated as NPL (NRB Directives, 2011).

One of the major concerns of the nation is to accelerate their development process and thereby increase the welfare of the people. So this is apparent that among the various components for economic progress, Financial Institutions plays vital role. Basically it works as financial intermediary by taking deposit and lending that money to deficit group of society. Investment activities drive the economy condition of the country. The more investment to the productive sector the more overall economic growth is achieved.

Financial institutions play intermediary role for mobilization of fund from non-productive sector to more productive sector. Major function of bank is to invest the money or depositor in such a project, which generates more net present value to bank. Further banks provide various facilities to entrepreneur to smoothen their business. Banks have made the possible to consume a product in Nepal, which has been made in other part of the world. For example, to export and import, the letter of credit (L/C) has been transacted through commercial banks.

After economic liberalization in country banking sector has face significant changes. Huge amount of direct investment has been made in banking sector. Economic liberalization has enabled the country to start several commercial banks. Before this Nepal had very few banks, which were rendering financial services but it was not sufficient to fulfill the requirement of that time. After economic liberalization the speed of economic growth has been recorded high. In one hand the open market system has brought cutthroat competition in banking sector and in other hand banks are still busy to cartel in exchange rate through informal organization like Foreign Exchange Dealers Association of Nepal (FEDAN) and customer are still deprived of getting benefit of open market.

Bank lower part of balance sheet consists of assets of bank, which generally consist of some liquid assets, some short-term call money, some investments, some fixed assets and the major portion of total assets is consist of loan and advances.

Total assets of bank can be divided in to two parts performing assets and non-performing assets. Performing assets are those assets which direct generates cash to organization or indirectly helps to generate cash of it facilitates the set ups for quality and quantity productivity. Loan and advances is direct contributor to banks income whereas cash in vault, balance in other bank, fixed assets and other assets are the facilitators which helps the daily operation of bank, Performing assets and positive value to bank as well as to Nation.

Non-performing assets refers to that portion of bank assets which is not generating cash to bank. Accumulated loss, Non-banking assets and non-performing loan are some example of non-performing assets. Non-performing loan is such loan, which fails to pay its interest to bank with in stipulated time. Non-performing loan has negative impact in banks growth as well as in economic growth. In one hand it stops the interest earnings of banks and in other hand it causes the bank to make certain percent provision (for possible loss of principle) from the operating profit. Increasing non-performing loan has impact on banks profitability.

1.2 Focus of the study

The study will focus on increasing non-performing loan is one of the emerging problems of Nepalese commercial banks. This study mainly focused on non-Performing loan of selected banks. It studies the ratio like loan and advances To total assets, loan and advantages to total deposit, non-performing to total Loan and advantages, provision held to non-performing loan, which indicates The performance and provides comparable forum on non-performing loan. It Also tries to show the effect on profitability of commercial banks and related NRB directives, which is concerned towards the rendering loan and loan loss Provision. The total NPL of Nepalese commercial banks are growing rapidly and it is the main cause to failure of bank.

The current political scenario is instable and security has been major issue of country which was compelled the lots of manufacturing company to close down their business. This is not good symbol for banks because most of manufacturing company utilize bank loan to finance their current assets as well as for their long-term project. If the situation persists the situation. Nepal Rastra Bank has taken over the management of the bank due to non-recovery of their borrower would not be able to repay their loan and interest in time, which obviously creates a big problem to the bank. Nepal Bangladesh Bank can be taken as an example for this loan and large portion of non-performing loan. Further the bank is going to merge with Nepal Credit and Commerce Bank and Nepal Sri Lanka Merchant Bank. It is obvious that the good performance of loan is the only factor, which energizes the bank for overall development and long-term solvency. Therefore the mainly focuses on the performance of loan of Nepalese commercial banks which encompass through the analysis of performing and non-performing loan, cause and effects of the performance of loan to the overall profitability of the bank.

A country's prosperity largely depends upon the economic activities of that country and the financial institution play a vital role to smoothen the economic activities. There is a perfect positive correlation between the economic growth of a country and the exercise of different financial instrument of that country. In contest of Nepal, commercial banks are the pioneer and market dominant in respect of trade of capital market and security instruments. In the light of this statement we can say that the successful operation of commercial banks in inevitable for the economic development of Nepal in present scenario. The threat to the current Nepalese banks is the performance of their loan. The major portion of their investment is in lending sector and there is always a challenge to management to maintain their loan portfolio productive sufficient to operate bank successfully and pay reasonable return to their shareholders. In this study, NPL of commercial Banks are presented, analyzed, summarized and stated finding and recommendation.

1.3 Statement of Problems

Most of the loan had been defaulted from the long back when the economy situation was achieving a higher level of economic growth. Their track record is not good and even in time they have not paid the bank as per agreement. It is a business principle that entrepreneur has full right over profits and losses of the business if any. If there will be a continuous loss in the business, or any symptoms of losses are envisaged then the borrower should either change the business or stop the operations to control future losses. This is because; borrower has to meet the obligation of loss from its own resources. In such case, borrowers need to liquidate their assets for debt servicing. Growing NPL is really a big problem for whole the nation's economy. And the share NPL is from these three largest commercial banks. So the root cause of NPL should be analyzed. The effect of NPL on bank's profitability is to be examined.

Commercial bank being the financial institutions plays significant role by collecting deposit and lending these funds in the productive sectors as lending and investment. Economic development of the country is directly related to the volume of investment made and return obtained by the bank. Due to lack of experts to analyze the risk and return of investment and maintain optimum portfolio investment problem has become very serious for the least development country like Nepal.

The core baking business is mobilizing the deposits and utilizing it for lending to industry. Lending business is generally encouraged because it has the effect of funds being transferred from the system to productive proposes which results into economic growth. However lending also carries credit risk, which arises from the failure of borrower to fulfill it's contractual obligation during the course of transactions. It is well known fact that the bank and financial institution in Nepal face the problem of swelling non-performing loans and the issue is becoming more and more unmanageable.

Commercial banks and financial institutions in Nepal have been facing several problems like lack of smooth functioning of economy. Different policies and guidelines of NRB, security problem, over liquidity caused by lack of good lending opportunities, poor information system, increasing nonperforming loans etc. In the present context where Nepalese banks are facing the problem of increasing NPL, more amounts have to be allocated for loan loss provision. The provision amount is taken out by deducting from the profit of the bank, the bank's profit might come down.

The credit extended by the commercial bank to agricultural and industrial sector is not satisfactory to meet the present need. Commercial banks have not been able to meet the needs of middle- and lower-class business yet. They are located only in urban areas and still there are a lot of operational hassles to sanction the loan. Nepotism and favoritism also effect the lending decision of the commercial bank, granting loan against insufficient collateral, overvaluation of pledged had and building, risk averting decision regarding loan recovery and negligence in recovery of overdue loan in some of the basic loopholes in Nepalese bank.

Commercial banks investment has been found to lower productive due to the lack of supervision regarding whether there is poor utilization of their investment or not. Lack of farsightedness in policy formulating and absence of strong commitment towards its proper implementation has caused many problems to commercial banks. The guidelines in themselves are not sufficient unless properly implemented.

The rules and regulations are the only tools of NRB to supervise and monitor the financial institutions. Currently the banking sector is facing various problems one of them, the banking has been victims of non-performing loan. Due to instable political condition, insecurity and other factor industries of Nepal are closing down. Lending carries credit risk, which arises from the failure of borrower to fulfill its obligation within time.

Therefore, the study will try to solve the confusion pertaining to identify the loan category for adequate provision according to latest guidelines of NRB and the study will further sights the analytical views towards the cause and effect of non-performing loan. This indeed will be beneficial for the professional working in this field and investor and shareholders who want to know the financial position of the bank. This research is focused on these areas particularly. This study has identified the following research questions regarding to NPL with special reference to Nabil bank limited, Global IME limited bank and Agriculture development bank limited; -

1. What is the proportion of Non-performing loan in total Assets, total deposit and total lending of selected Nepalese commercial bank.?

2.What is the relationship between loan and loan loss provision in the commercial bank?

3.What is the trend of non-performing loan, loan loss provision in the selected Nepalese commercial banks?

4.What is the impact of non-performing loan in the performance of commercial bank?

1.4 Purposes of the study

The gradually increasing NPL has now become a major issue for every commercial bank. Every bank has now put the NPL management under top priority. Thus, in present context analyzing the cause and implication of NPL obviously shall the use full for banking sector. The basic objective for this study is to analyze and identify the impact, cause and consequences of NPL. The following objectives have been considered as specific objectives of this study.

1.To evaluate the proportion of Non-performing loan in total Assets, total deposit and total lending of commercial bank.

2.To evaluate the relationship between loan and loan loss provision in the commercial bank.

3.To present the trend of non-performing loan, loan loss provision in the Nepalese commercial banks.

4.To analyze the impact of non-performing loan in the performance of commercial bank.

1.5 Significance of the study

The success and prosperity of bank depends upon the successful implementation of collected resources, which develops the economy of the country. Good lending of the bank has positive impact on economic development of the country and vice versa. Increasing non-performing loan is one of the challenges faced by commercial bank in the present context.

Several studies have been conducted regarding the financial performance of commercial bank of Nepal. Likewise, deposit and loan pattern of Nepalese bank has also been studied by various researchers. Further there is numerous thesis arguing the risk and return on investment in the share of commercial banks. But less research has been made regarding the performance of loan of commercial bank among them most research has been conducted before the introduction of new NRB directives, which is not useful in present scenario. Some research covers the study of two big governments owned bank, which makes the study a general. This research will be different from all those researches conducted earlier because it studies the non-performing loan in middle class private commercial banks of the country. This study will be helpful to give some of the present issue, latest analysis regarding non-performing loan of commercial bank. Not only that this study gives the real picture of current non-performing loan of Nepalese commercial banks to its stakeholders.

The study is mainly concerned with the analysis of NPL in total assets, total deposit and total lending of different Nepalese commercial banks. Therefore, it has significant to find the level of NPL of Nepalese commercial bank. It is also significant to find out whether the Nepalese commercial banks maintaining loan loss provision in accordance with the current NRB directives or not.

This study has tried to find out the trend of NPL on individual basis of Nabil bank limited, Global IME bank limited and Agriculture development bank limited. The result of this study is thought to be importance for the following groups:

1. Management of the bank: - After analyzing the cause and effect of NPL, it would be helpful to management. They can observe internal as well as external reasons for growing NPL in their organization.
2. Potential investors: - They can analyze themselves the condition of banks whether it is advisable or not by reviewing this research.
3. Government: - Government can think to make necessary policy or adjustment in current policy and guidelines by reviewing current study.
4. They can make base whether the commercial banks following their policy and guidelines or not.
5. Policy formulators: - They can review aspect of NPL related matters by going through research.
6. Academicians: - This study will be helpful to them for further research and for their syllables.

1.6 Limitations of the study

This study will be focus on sensitive part of the bank which resultants the management a little bit hesitation to come up with open view regarding the lending policy and provision method. Therefore, the study has been conducted on the basis of annual reports of selected banks, published and unpublished material, NRB publications, and my personal judgment. Therefore, the strength of findings will largely depend upon the correctness of input information. This research has following limitations; -

1. This study is a milestone in explanatory study in a searching the NPL problems and its solutions in Nepalese financial sector. Finding of the study might be very much useful for academicians as well as for practitioners. However, this study suffers from many limitations such as:
2. This study will be focus on only three commercial banks i.e. Nabil bank limited, Global IME bank and Agriculture development.
3. This study will be analysis mostly base on secondary data.
4. This study will not recover every part of NPL due to availability of limited information.
5. This study will be take only five years period of time.
6. The study is based on following variables:
    1. Non-performing loan of selected Nepalese commercial banks.
    2. Total assets of selected Nepalese commercial banks.
    3. Total deposit of selected Nepalese commercial banks.
    4. Total loan and advances of selected commercial banks.
    5. Total loan loss provision of selected commercial banks

1.7 Organization of the Study

This thesis is prepared in line with prescribed format and structured into five chapters; each devoted to some aspects of Non-performing loan of commercial banks. The titles of each of these chapters are summarized and the contents of each of these chapters of this study are briefly mentioned here.

Chapter-I: This chapter includes introduction & background of the thesis, which shows; significance, statement of problem, objective of the study, limitation of and organization of the study.

Chapter-II: This chapter containing: literature review, which shows; review of related studies.

Chapter-III: This chapter includes research methodology, which shows; research design, source of data, statistical tools used, data processing and analysis and definition of some of the major terms used in the study.

Chapter-IV: This chapter containing data presentation and analysis.

Chapter-V: This chapter includes summary, conclusion & implications.

CHAPTER II

REVIEW OF LITERATURE

2.1 Introduction

This part of the study deals with making the review of past studies made on non-performing loan. So, this chapter will encompass the Conceptual/theoretical review, Review of NRB directives, Review of articles/journals/newspapers/website, Review of thesis concerned.

2.2. Conceptual review

Under this heading Following issues are discussed under the Nepalese prospective.

a) Loan and advances

Commercial bank's main function is to create form it's borrowed fund. The bank doing so convert's it's liability into active asset. Loans and advances are the assets coming from such activities. Loans and advances dominate the assets side of the balance sheet of any bank and also constitute the primary source of income to the banks. Loans and advances may take different forms and are allowed against various types of securities. Loan, overdraft, discounting of bills of exchange etc are some of the forms of bank lending.

b) Pass due/overdue

An amount due under any credit facility is treated as past due or overdue when it has not been paid on the due date fixed by the bank. Any amount due to the bank under any credit facility is 'overdue' if it is not paid on the due date fixed by the bank.

c) Loan classification

Loan classification refers to the process banks use to review their loan portfolio and assign loans to categories of grades based on the perceived risk and other relevant characteristics of loans and as per guidelines of central banks. In the context of Nepal as per guidelines of NRB, loans are classified into four categories namely pass, substandard, doubtful and loss.

d) Performing loan

Performing loans are those loans that repay principal and interest timely to the bank form the cash flow it generates. In the context of Nepal, the loans classified as 'pass' category is termed as performing loan.

e) Non-performing loans/non-performing assets

These are the loans that do not repay principal and interest timely to the bank. A common feature of NPL appears to be that a payment if more than 90 days past due. In Nepal, if the loan is past due for over 3 months, it is NPL. Hence the loans falling under substandard, doubtful and loss categories are regarded as NPL.

f) Letter of credits and guarantee

In the event of conversion of contingent liabilities of the licensed institution e.g. letter of credit, un-matured guarantee and other contingencies, into the fund-based liabilities and required to make payment, such amount shall be classified as PASS loan up to 90 days from the date of conversion. Such credit facility shall be classified as LOSS loan if not realized within 90 days.

However, adopting a proper risk management in place some loans turns to be distressed in due course of time due to various unavoidable reasons. Such distressed loans whose due date exceeds 90 days are called NPL. These NPL should be managed very carefully and technically in order to avoid a huge loss for the institution.

It will be imperative to understand the terms NPA and NPL. NPA relates to net profit financial assets. In this sense, NPA are defined as debt instrument whose obligors are unable to discharge their liabilities as they become due. Therefore, NPAs comprises the wider area of assets portfolio where as the NPL is referred to distressed loans classified as per regulation of the central bank. Since the loan being the significant component on financial assets portfolio, NPL and NPA are used interchanging but if there are no other assets other than loans to denote, it will be better to say NPLs.

Nepalese financial system still has a high level of NPL s in the system. System's soundness cannot be restored without resolving the problem of NPL. The problem of high level of NPL needs to be addressed in time resolved as soon as possible. The sooner the problem is resolved, the quicker the crisis is removed from the system. In order to resolve the problem of NPL we should require initiating various measures in the system. Preventive measures will be helpful to control the growth and curative measure will be beneficial to lower down the level of NPL in the system. In order to resolve the problem the root cause of the problem needs to be identified; analyzed and properly addressed.

If the NPL'S are already at outstanding level, curative measures are required to lower down the level of NPL. If the level of NPL is at high level despite of having properties management, best credit practices and strong compliance mechanism in place, then the curative measures become significantly important. In such a situation, the authorities need to pay greater attention because the system might be falling adverse effect of external factors or shocks beyond the control of institutions. In such a circumstance, extra supportive measures are required to be introduced by the supervisory authorities and the government. (RBB Annual Report 2008)

If the NPL'S in the system in growing due to the lack of good credit culture corporate governance and risk management skills with in the institutions; prudential measure such as; issuance of prudential regulation, compliance of regulations and strengthening of internal risk management skill, formulating of percent and 100 percent provisioning should be made for pass, substandard, doubtful and loss loans respectively.

2.3 Review of relevant NRB directives

Nepal Rasta Bank issues various relating banking regulations and prudential norms. NRB has provided following directives for classification of loan and advances and it's loss provisioning for the purpose of minimizing possible risk in bank's lending by using the authority given by sub section 1 of section 23 of NRB acts 2012 (Revised) and section 19 (ka) of commercial bank act 2031 (Revised).

1. Classification of loan and advances on the basis of overdue again schedule. A bank is required to classify their loan on the basis of overdue.
2. Classification of loan and advance.

   Loan and advances is required to classify

Pass

This class includes the loan that principal overdue up to 3 months. It is also defined and classified as performing loan.

Watchlist

This is provision for loan that Principal overdue for 3 months and other conditions mentioned by NRB.

Substandard

Loan with principal overdue above 3 month and up to 6 months called substandard loan.

Doubtful

All loans and advances which are past due for a period 6 months to 1 year shall be included in this category.

Loss

Loan with principal overdue above 1 year called bad loan, which have least possibility of recover or considered unrecoverable and those having this possibility of even partial recovery in future. Loans and advances failing in the category of substandard, doubtful and loss are classified and defined as NPL.

2.4 Review of books

There is no adequate availability of books in this topic but some relevant books are available in the market. These books are categorized in the from international publications and Nepali publications as follows.

Book named "Banking Management" says that in banking sector or transaction, an unavoidable of loan management and its methodology is regarded very important. Under this management, many subject matters are considered and thought, For example, there are subject matters like the policy of loan flow, the documents of loan flow, loan administration, audit of loan, renewal of loan, the condition of loan flow, and the provision of security, the provision of the payment of capital and its interest and other such procedures. This management plays a great role in healthy competitive activities (Bhattrai D.R, 2016).

It is very important to be reminded that most of the bank failures in the world are due to shrinkage in the value of loan and advances. Hence, risk of non-payment of loan is known as credit risk or default risk (Dahal N., 1999).

Portfolio management helps to minimize or manage the credit risks by spreading over the risk to various portfolios. These methods of managing credit risk is guided by the saying do not put all the eggs in a single basket (Bhattrai S., 2016).

2.3.1 Review of books (Nepalese publications)

A book for beginners in banking b writer duo Mr. Bhuwan dahal and Mrs. Sarita Dahal namely 'a hand book to banking' has emphasized on various aspects of banking in brief that is required to exercise sound banking practices. It says "A bank is judged on the basis of capital, assets quality, management earning liability and sensibility to market risk. Almost all the government banks are running at loss while all the private sector banks are showing profits, it is very difficult to call them sound if appraised from CAMELS approach. Some banks have very low capital adequacy ratio while some banks have piled up NPL. Similarly banks do not have proper system in place for management of market risks.

Writer duo is more specific in this book while marking financial institutions in terms of standard form of yard sticks i.e. CAMELS. Nepalese banking sector as they mean, are yet to be streamlined and systematized. Due to this reason credit processing and calculation of market risks are given low priority while extending advances. There are the main causes of siphoning of funds and impairment of loans. As a result whole financial sector is heading towards a huge and accumulated NPL. Therefore, suggestion is given by the writer duo to NRB to control the system by implementing directives enforceable/actable in this regard.(Dahal B. And Dahal S., 2007:171)

2.3.2 Review of books (International Publication)

It seems that the problem of cumulating NPL s is also raising its head to neighboring country in India where banking system is considered to be more systematic advanced and up to the global standard. Therefore Reserve Bank of India (RBI), Central Bank of India has given paramount preferences to the mounting NPL in financial sectors of Indian economy.

The book on ‘Managerial Finance’ written by Weston and Brighman stresses on Risk- Return trade off as one of the major financial functions. They believe that the maximization of the value of the firm can be achieved through maximization of returns in one hand and minimization of risk in the other. The relationship between the expected future state of the economy and the performance of individual firms enables a relationship to be set forth between the state of the economy and the returns from investment in firms (Westom and Bringham; 1980: 93).

Describing about the new areas of finance, James C. Van Horne in his book ‘Financial Management and Policy’ stresses on two broad functions, viz:

- Investment in assets and new products;

- Determining the best mix of financing and dividends in relation to a company’s overall valuation.

According to him “Investment of funds in assets determines the size of the firm, its profits from the operations, its business risk and its liquidity. Obtaining the best mix of financing and dividends determines the firm’s financial charges and its financial risk; it also impacts its valuation” (Van Horne; 1997:758-776).

Khubchandani in his book" practices and law of banking "has mentioned about NPL and income recognition norms. He has quoted a high level committee headed by Shri M Narasingham appointed by the government of India that was formed in august, to examine all aspects relating to the structure, Organization, functions and procedures of financial system. (Khubchandani B.S. 1991:305)

The recommendations were to make the balance sheets more transparent with full disclosures. It also emphasizes on internationally accepted accounting system practices so far income recognition is concerned i.e. income recognition should be based on cash realization instead of accrual basis. Similarly, risky assets should be classified as per their NPL criterion. It also speaks of BASEL committee recommendation in regard to the capital adequacy ratio (CRR) of banks. It says "following these recommendations, the RBI issued a host of guidelines\instructions to banks in April 1992. Since the crux of the matter relates to definition of NPL based on which alone the income recognition, assets classification, provisioning and capital adequacy of banks and other financial institutions is determined, the RBI has issued the following guidelines the banks from time to time.

a) The definitions/criterion adopted for treating an account as NPL is that, for instance, if interest debited/installment due in an account prior to 31 march, 1991 say as on 31 March, 1991 is still not collected such interest/ installments should be deemed to have become due on 30, April 1991. Up to 30 April 1991, the facilities would be treated as "substandard" and from 1 may 1991, they would be treated as "doubtful". Thus for the treatment of credit as a NPL, the entire period for which interest/ installment remains uncollected should be reckoned.

b) All the accounts will be treated as non-performing. If in the case of :

i) Term loans: interest remains past due for a period of

- quarters, for the ending 31 march 1993.

- quarters, for the ending 31 march 1994.
- quarters, for the ending 31 march 1995 and onwards.

ii) Cash credits and overdrafts: the account remains out of order or the periods indicated as before.

iii) Bills purchased discounted: The bill (BP/BD) remains overdue/ unpaid for the period specified hereinbefore.

c) If a particular facility of a Brower on the above criterion/definition becomes NPL. And them all the facilities granted to the borrower should be treated as NPL. Thus, the treatment of NPL concept is borrower wise and not facility wise.

d) It was also clarified by the RBI that in cases where the outstanding balances in the principal operating account is less than the sanction limit/drawing limit, but there are no credits continuously for six months as on the date of the balance sheet or credits are not enough to cover the interest debited during the period, these accounts should be treated as out of order.

e) An account should be considered 'past due' if is not repaid within 30 days from the due date. Thus if interest is due on 31 March 1992, it becomes past due on 30, April 1992, if it is not paid/collected within 30 days grace period.

f) Both interest and installments, where ever applicable, should be taken in to account for assessing the NPA status of an account, after of course, allowing for 30 days, grace period in both cases.

2.5 Review of relevant articles, newsletters, journals

For Nepalese banking system and its amounting NPL s level, some of the think takes from the related sectors have commented and forwarded their views, suggestions through articles, journals, speeches, news letters etc.

These suggestions, recommendations and views are based on past track record and practices; some of financial menace. Therefore, the researcher has tried to drag in some of their related views to the research work.

Dhungana director bank and financial institution Regulation department, NRB in some years ago. In his article NPLS and its management" in Banking Prabradam 20 pg 7, he has expired an introduction of NPL and its problem in commercial banking sector. He has explained the main cause for high level of NPL in the Nepalese banking system and he has given instruction of how to solve the NPL problem? He has described the steps initiated by NRB to control the level of NPLS in the system.

He has described of main factor effect to increasing level of NPL. According to his own view on main causes for high level of NPA in the Nepalese banking system, "Nepalese banking system suffers from problem in credit management and also some obstacles beyond the area of credit management those are contributing to raise the level of NPL. For the purpose of this analysis, the factors contributing to have a high level of NPL have been classified into two groups. The first is internal factor which mainly comprise of weakness of the particular bank or financial institution in the credit management and over sight deficiencies in this regard. If preventive measures are applied at the institutional level, the banks themselves to some extent can resolve the problem of NPLS. Similarly, another aspect relates with the external factor beyond the control of the external factors beyond the control of the bank and financial institution. We can point out some of these components as follows:

Internal factors

a) Lack of loan write off policies.

b) Poor recovery efforts even the loan is categorized under bad.

c) Insider abuse and fraud in lending and recovery.

d) Limited supervision by the bank itself and weak internal controls in the bank. This comprise of weak supervision and monitoring, lack of reward and punishment system and poor management information system (MIS) to monitor, manage and control the risks with in the banks and financial institutions.

e) Management oversight deficiencies in policy level, along with rapid and aggressive growth strategies in some banks and lack of competencies in the BOD to monitor risk.

f) Risk management deficiencies within banks and financial institutions. This comprises of poor system, procedures and credit culture in credit management.

External factor

a) Poor legislative regime in the system specially governing financial issues.

b) Other systematic problems that are being faced by all the financial institutions equally.

c) Security and conflicts situation at present.

d) Poor regulative and supervisory capacity of the central bank in the past.

e) Deterioration in economic growth rates and activities since last few years.

f) Lack of supportive institutions helping to reduce the NPA, such as lack of effective and professional notary public office in order to eliminating problems associated with bills purchased and discounted, lack of secured transaction office to register moveable properties, lack of credit rating agencies facilitating to rate the risk grades, lack of asset management corporation assisting the financial institution to manage the distressed loans, lack of proper training center and academic institutions focused to enhance the skills on credit management, lack of debt recovery tribunal to deal with loan accounts.

2.6 Review of thesis

Researcher tried to find out research works done in this field through the concerned places and found some published/unpublished thesis in the related field. Therefore, review of the same is attempted.

Paudel. (2001**)** in his Thesis "A study on lending practices of joint venture commercial banks with reference to Nepal Bangaladesh Bank Ltd. (NBBL) and Himalayan Bank Ltd. (HBL)" has made comparative study of these two banks in different lending aspects and strategies.

In his findings, the liquidity position of NBBL is comparatively better than HBL. The liquidity ratio of HBL is more stable and consistent then NBBL that indicates the stable policy of HBL, NBBL is found slightly better to be maintaining between assets and liabilities. NBBL has high lone and advances to total assets ratio, loan and advances to total deposit ratio, but HBL has high investment to total loans and advances and investment and total investment to total deposit ratio. He has concluded that NBBL is able to manage its assets to complete in this competitive banking business than HBL. As per his findings its liquidity position of NBBL is better and hence HBL is recommended to its liquidity position. He has suggested both bank to strictly follow the NRB directives, which will help them to reduce credit risk arising from borrower's defaulter, lake of proper credit appraisal, defaulter by blacklisted borrowers and professional defaulter. Loan loss provision of both banks is in fluctuating trend. So both banks are suggested to adopt sound credit collection policy which wills helps to decrease loan loss provision.

The main objective of his Thesis lending practices of joint venture commercial banks with reference to NBBL and HBL is investment criteria and sector, loan distribution and advance practice of joint venture bank. The limitation of the thesis was base on secondary data given by responded, five year's data and non-ending year's data.

Ojha. (2002) in his dissertation about "lending practices" has written that the commercial banks have to expand their credit in the area if rural economy so as to compromise between the liquidity and credit need such economy. This helps in minimizing the idle find in business and at the same time contribute to the national economy. The banks should also increase the volume of credit in the sector of agriculture as the ratio of contribution made by the banks in this priority is decreasing. Research has found out that following the normal guidance of Nepal Rastra Bank and acting upon reduces many on the credit risk arising from borrower's defaulter, lack of proper credit appraisal, defaulter by blacklisted borrowers, and professional defaulter. The over confidence of commercial banks regarding credit appraisal efficiency and negligence taking information from Credit information bureau has caused many of the bad debts in these banks. He thinks that these banks have to follow the directives of NRB strictly and be more cautious and realistic while granting loans and advances.

The high volume of liquidity reveals that a degree of lending strength has been prevailing in all of the commercial banks. The lack of reliable lending opportunities and fear of losing the principal in rural sector has been keeping these banks less oriented towards the lending function. Hence, the government should take appropriate action to initiate these banks to attract to flow credit in rural economy. Posing the compulsions by directives does not create long-term healthy lending practices unless the commercial banks are not self-motivated to flow credit in this sector.

Joshi. (2003), In "A Comparative Study on Financial Performance of Standard Chartered Bank Nepal Limited and Everest Bank Ltd" states that the mean current ratio of EBL is slightly higher than that of the SCBNL and the variability of ratio of EBL is more consistence than SCBNL in comparison. The mean ratio of cash and bank balance to total deposit of SCBNL is lower in comparison to EBL. SCBNL has better liquidity position than EBL because of the high volume of liquidity indicated the inability of the bank to mobilize its current assets. Moreover SCBNL's ratios are homogeneous than EBL. The mean ratio of case and bank balance to current assets of SEBNL is lower in comparison to EBL. Similarly, SCBNL's ratios of the studyperiod are more consistent than EBL. The mean ratio of loan and advances to total deposit of EBL is higher than SCBNL. It can be said that EBL used to provoked grater loan and advance in comparison to its total deposit than SCBNL. Likewise, SCBNL's ratio seems to be variable than EBL. The mean ratio of investment on government securities to total working fund of SCBNL is higher than EBL. Consequently, it has consistency in maintaining the ratio than EBL. The mean ratio of return on loan and advances of SCBNL has found to be significantly greater than EBL with more consistency than that of EBL. The mean ratio of credit risk of SCBNL is lower than that of EBL's ratio are more consistent that of SEBNL. Growth ratio of deposit is more consistent than that of SCBNL is lower i.e. 19.28% in comparison to EBL i.e. 76.46%.

The main statement of the problem of his research is the investment decision is the major tool of financial institution. There are many finance companies and commercial banks operating in Nepal. The fast growth of such organizations has made pro-rata increment of in collecting deposits and their investment. They collected adequate amount from the mass, however they could not find or locate new investment sectors required to mobilizes their fund on the changing context of Nepal. Many banks or companies succumbed to liquidation although they had sustainable investment capacity. The increasing rate of liquidation has caused a downward trend in investment sectors. It has ensured bad impact on interest rate to the depositors, lower market value of shares etc. for the assessment of such adverse impact, this study has shown to contrast and analyses the investment policy of joint venture banks. Joint venture banks viz. standard chartered bank Nepal ltd and Everest banks limited. The main objectives are comparing investment policy of concern banks, find out the empirical relationship among total investment deposit, deposit utilization loan and advance, net profit and outside asset and compare of SCBNL and EBL.

Dhungana, (2006), had written an article on “Problem of NPL’s and need of financial Discipline in the Nepalese Banking System” has concluded that poor credit management and deteriation in the quality of loans gives birth to non-performing assets. The internal measures play significance role to control the growth of NPL. Best credit practices, culture and policies are required to strengthen the internal factor. The banks should have a proper system and competency on risk management and should ensure that risk are accurately identified, assessed and controlled properly. A proper risk management is undoubtedly an important tool for a good banking and NPL management.

Dhungana further states that it can be expected that the financial sector reforms will lower down the level of NPL from the existing level and strengthening the bank and financial institution internally to manage the credit portfolio efficiently and support will be continued to make a good credit culture in the banking system.

Garg, (2063), had written an article on "NPAs at Nepalese Financial Sector" has highlighted NPA problem in Nepalese financial sector. In this article says" The NPAs of three banks (NBL, RBB and NIDC) are highly discussed and published. If we analyze them, we can find that the NPA of these banks have also made the required loan loss provisioning over the same period, high and improbable figures of NPA are still often quoted. There are many companies, which suspended their business one or two decade ago, but the banks are still carrying their loan account as NPA in their books. They should have the guts to either foreclose on the collateral or write the loan off in such cases.

Neupane, (2008), had written an article on "Banks cut NPAs to Global Level" has thrown some views regard bad loans of banking sector. As mentioned by him there was various types of risk inherent in the credit. One, who managed risk, earns profit. Neupane further added that recent financial crisis in the banking sector is due to weak accounting procedures, defect in loan classification, lack of transparency, loss control etc.

This article opined that NPL is the indicator of financial crisis and the factor leading to NPLs to is economics low down, recessions, bad intention of the borrower, lack of credit policy, increase in interest rate etc. NPLs increases resource mobilization cost and reduce profit-earning capacity of the bank. Neupane has also mentioned that the international standards of acceptable NPA is 40% but here is about 26% NPL in Nepalese banking sector, which is due to high level of NPL of two nationalized banks. As stated by the writer, major implication of NPL are banks cannot return depositors money on demand and it limits lending capacity of the banks. The author suggested internal and external measures for reducing NPL and its effect.

Internal measures comprise classification of loan and advances and providing provision for probable loss and external measures comprise to help from Credit Information Bureau (CIB), appointment of Assets Management Company (AMC), and Debt Recovery Tribunal (DRT). Neupane concludes, banks must give priority for reducing NPA. Neupane also mentioned that many countries are adopting various measures for reducing loan loss. Recently the president of

Philippines has announced tax rebate system for reducing NPA. Now it is high time improved bad debts of banking sector with firm determination.

Mishra.S, (2007), had written an article on "Management of NPA" on management of NPA made it clear that the traditional approaches to bank regulation are conductive for management of NPA. These approaches emphasized the view that the existence of capital adequacy regulation plays a crucial role in the long-term financing and solvency position of banks, especially in helping the bank to avoid bankruptcies and their negative externalities on the financial system. In general, capital or net worth serves as a buffer against losses and hence failure. Rather than accommodating measures to combat the NPA issues, the traditional measures tried to protect the interest of deposits trough maintaining adequate capital in liquid form. This had affected the availability of funds for productive purpose since banks were not able to lend it, rather forced to keep as reserves. Strengthening financial system has been one of the central issues facing emerging markets and developing economics. This is because sound financial system serves as an important channel for achieving economics growth through the mobilization of financial savings, putting them to productive use and transforming various risk. In this article emphasized that the essential components of sound NPA management are quick identification of NPAs, their containment at a minimum level and ensuring minimum impact of NPA on the financials.

The major objectives were:

a) To analyses the level of non-performing loans of Nabil Bank Ltd.
b) To make an assessment of loan loss provision made against the NPL by Nabil Bank Ltd.
c) To examine the relationship between the NPL and profitability, assets and business turnover of the bank.

The major findings were:

a) The loans and advances to total deposit ratio is also in the fluctuation trend. The mean is 74.00% which indicates the average efficiency of the bank in utilization of its deposits. The S.D. is 4.00% and C.V. is 0.00%. It signifies less deviation and more consistency in advancing loans out of deposits.

b) The average mean ratio of non-performing loans to total advances is 1.50%, which is considered to be a strong side of the bank in managing NPLs. The S.D. is 0.70% and C.V. is 0.00%. It can be said that the bank controlling its NPLs efficiently.

c) The ratio of provision held to total non-performing loans is sufficiently high. The average mean is 96.60%. The S.d. is 78.10% and C.V. 15.90%. It indicates that the bank has sufficiently provisioned against non-performing loans. The higher the ratio of NPL provisioned against loans, the better the cushion against the risk of actual loan loss.

d) The ratio of net income to total loan and advances shows how efficiently bank has through its lending activities. The average ratio is 0.90%. The S.D. of the ratio is 49.00% and C.V. is 9.70% respectively. The lower S.D. and higher the C.V. indicates greater the stability in income generation.

e) The correlation between deposits and loans and advances is positive and significant. The coefficient and correlation between loans and deposits is 0.9925. the coefficient of determination is 0.9851. The correlation is significant because the correlation coefficient is greater than the relative value of 6 P.E.(r).

Arora and Ostwal, (2014), conducted an article on "*Unearthing the Epidemic of Non-Performing Assets: A Study of Public and Private Sector Banks"* which deals with the concept of non-performing assets and analyze the classification of loan assets of public and private sector bank. It also explores the comparison of loan assets of public sector and private sector banks. The study concluded that private sector improving due to decline in NPAs ratio compare to public sector banks due to recovery management done in NPAs and suggest that there is need to check the NPAs of public sector banks so that Indian banking system becomes efficient.

Peter. S, (1999), had written an article on "Empirical Study on Non-performing assets of Bank." evaluate the non-performing assets of Punjab National bank and its impact on profitability and to see the relation between total advances, net profit and gross and net NPA. The study uses the annual reports of Punjab National Bank for the period of six years from 2008-09 to 2014-15. These papers conclude that there is a positive relation between Net profit and NPA of PNB. It is because of the mismanagement system of the bank.

Shakya, (2015), had conducted a thesis entitled on "A Study on the Credit Risk Management of Neplease Commercial Banks (with Reference to Kumari Bank Ltd. and Machhapuchre Bank Ltd.)"

The major objectives were:

a) To examine the credit risk position of the selected commercial banks in Nepal.

b) To analyze the credit risk management system and practices of KBL and MBL.

c) to evaluate the organization structure of KBL and MBL to manage the credit risk.

The major finding were:

a) The concentration risk is the main source of credit risk for both KBL and MBL. Similarly, lack of of systematic and through credit processing is also the major sources of credit risk in these banks.

b) The problem in credit processing includes lack of thorough credit assessment, absence of testing and validation of new lending techniques, subjective decision-making by senior management, lack of effective credit review process, failure to monitor borrower or collateral values, and failure of bank to take sufficient accounts of business cycle effects etc.

c) The market-sensitive and liquidity-sensitive exposures also increase the credit risk of these bank. Similarly, it is found that both banks have their own rating system of the credit client and the sectors.

Bhattrai, (2016), published an article on "Determinants of Non-performing Loan: Perception of Nepali Bankers." Argues that energy crisis; lack of timely budgetary expenditure by the government and instable political environment increases the non-performing loan. Similarly bankers also perceive that borrowers honestly in disclosing the information, better monitoring and evaluation of the loan, have significant negative impact on non-performing loan. However, the banker's perception shows that the macroeconomic variables like unemployment rate, inflation rate, exchange rate and interest rate are not much important variables to influence non-performing loan of the commercial banks of Nepal. The bankers also perceive that increase in GDP growth rate decrease the non-performing loan of commercial banks in Nepal.

Basnet, (2016), had conducted a thesis entitled on "Non-Performing assets of Nepalese Commercial Banks."

The major objectives were:

a) To analyze the non-performing assets of commercial banks.

b) To examine the level of NPAs in total assets, total deposits and lending of commercial banks.

c) To examine whether the Nepalese commercial banks are following the NRB directives regarding non-performing assets or not.

The major finding were:

a) The level of NPA of Nepal Bangladesh Bank Limited seemed greater than all of the others banks under the study. Similarly, Nepal SBI Bank and Bank of Kathmandu stands at second and third position respectively.

b) The position of NABIL Bank Limited seemed to be quite satisfactory because the bank has been reducing it NPA every year and NPA of Nepal Investment Bank has been reducing it at minimum than that of all the other banks and it is found that none of banks have been following the directives of NRB regarding the loan loss provision.

Mr. Jaya Lal Neupane has carried out study on 'Non Performing Loan and Loan Loss Provisioning of Commercial Banks' with reference to Nepal Bank Limited, Rastriya Banijya Bank and Nabil Bank Limited. His objectives is to find out and analyze the guidelines and provisions pertaining to loan classification and loan loss provision and level of NPL in commercial bank, and to find out the impact of loan loss provision on the profitability of the commercial banks. In his study, he concluded the ineffective credit policy, political pressure to lend non- viable projects, overvaluation of collateral and even without collateral disbursement are the major causes of mounting non- performing assets in government owned banks. He further adds lending factors of accumulating NPAs are poor credit appraisal system, ineffective credit monitoring and supervision system, poor security system and recession, willful defaulter etc.

Mr. Hiraman Niraula in his thesis 'A Study of Loan Classification and Non- Performing Assets Management of Rastriya Banijya Bank' has pointed out the Non- Performing loan as a major problem of Nepalese commercial banks. In his study he discloses the factor that the RBB holds the largest portion of Non- Performing loans of the banking sector.

He concludes that the ineffective credit policies, overvaluation of collateral are the major causes of mounting non-performing assets. He realizes the needs to resolve the problems of NPAs by changing the policy and gaining the confidence of borrower to settle loan by way of understanding. Bhattarai S.(2009). In her thesis 'Implementation of Directives issued by Nepal Rastra Bank' with reference to the Nepal SBI bank and Nepal Bangladesh bank limited has focused to the legal implementations of non-performing loan of commercial banks. She concluded the impact of new directives issued by NRB has a negative impact to the commercial banks. She writes the new directive compels the bank to provide additional loan loss provision for outstanding loans, which ultimately reduces the operating profits of banks. However, it strengthens the position of banks and increases the quality assets of banks.

Ms. Niva Shrestha has conducted a study named 'A study of non-performing loan and loan loss provisioning of commercial banks' with reference to the Nabil Bank Limited, Standard Chartered Bank and Nepal Bank Limited. Her objectives are to find out the portion of no performing loan, relationship between loan loss provision and loan and advances and profitability. She has pointed out the problems of the commercial banks as lack of smooth functioning of economy, different policies and guidelines of NRB, political instability, security problem, poor information system, over liquidity caused by the lack of good lending opportunities, increasing non-performing assets etc.

Research Gap

Research gap refers to the gap between previous research and this research. The purpose of the research work is quite different from the studies made by the above person (related to commercial banks). This study focus in analysis of non-performing loans and profitability Nabil Bank Limited, Global IME Bank Limited and Agriculture Development Bank Limited. Different financial and statistical tools have been used in the study. Among them, ratio analysis, regression analysis are the strong financial tools. This study is a little bit different than previous studies. It may be one of them research study of non-performing loan and profitability of few research work to Nabil Bank Limited, Global IME Bank Limited and Agriculture Development Bank Limited. This study tries to indicate the effectiveness of credit policy of concerned banks through analysis of non-performing loans.

CHAPTER III

RESEARCH METHODOLOGY

This study aims to explore the NPL and it's impact of NABIL Bank Limited, Global IME Bank Limited and Agriculture Development Bank Limited. It also intends to examine whether there is any direct relationship between the growing instability of all kinds and NPLs. and to fulfill the objective of the study a systematic methodology has been followed. To reach the findings of any study we have to use right methodology. Methodology is a design or framing of whole study. This study has used mostly descriptive research methods. By this methodology researcher tries to find out the real scenario of NPLs of selected commercial banks and it's comparative relation to banking healthy. This study only based on secondary data, as a data analysis tools, researcher has used the statistical and financial analysis tools to show the relations.

3.1 Research Design

Research design is the specification of methods and procedures for acquiring the information needed. It is the plan, structure and strategy of investigation conceived so as to obtain answer to research question and to control variance. This research is aimed at studying the NPL of NABIL Bank, Global IME Bank limited and Agriculture Development Bank Limited. For this purpose, the present study is based on descriptive type of research design.

3.2 Natures and Source of Data

This study has included only secondary data, Sources of information. Secondary data will be obtained from all the published books, booklets, articles, bulleting, annual reports and other related materials including international rules and regulation. The data collected will be both qualitative and quantitative.

Basically, the data and information required for this purpose is to be obtained from selected Nepalese commercial banks. Therefore, all the data collected are secondary.

Following are the secondary data collection sources:

Annual reports, Newsletter, broacher etc of selected Nepalese commercial banks.

a. Laws, guidelines and directive regarding the subject matter.
b. Related articles published in newspapers, journals, magazines, and other publications.
c. Unpublished thesis and dissertation.

d. Various reports published by NRB. Quarterly report of financial statistics, banking and financial statistics no.46, Nepal Rastra Bank Samachar etc.
e. Various related websites www.nrb.org.np, http://internet/newsn events.php, www.nepalnews.com.np, www.sebonp.com.np etc.
f. Beside above any kind of other sources, such as assertions, interviews, remarks/opinion by the experts that provides valuable data and conclusion regarding the subject mater has been considered in this study.

3.3 Population and Sample

Population refers to the entire group people, events or things of interest that a researcher wishes to investigate. Since this study is about NPL and its impact of commercial banks, the population for this study comprised all the licensed commercial banks of the country.

There are altogether 28 commercial banks in Nepal. Out of the total population NABIL Bank Limited, Global IME Bank Limited and Agriculture Development Bank Limited are selected as sample for this study by using judgmental sampling method and time period is 2069/70 to 2073/74. Cause of selecting these commercial banks are more effecting by NPL and it's impact on various sector (like Net profit, loan lending procedure, deposit repayment capacity, loan loss provisioning etc.) of these commercial banks. So this study could represent true picture of NPL and it's effect on commercial banks.

The population is selected as convenience sampling:

- One as joint venture
- Second as government bank
- Third as private bank.

Among the 28 Commercial Banks, the researcher chosen three banks (Nabil bank limited, Global IME limited and Agriculture development bank). Total number of commercial banks in Nepal (p)= 28. Sample of Nepalese commercial banks chosen by the researcher (s)=3. Percentage of sample of Nepalese commercial banks=10.71%.

3.4 Data Analysis and Method

The available information is grouped as per the need of the research work in order to meet research objectives. The collected data are presented in appropriate forms of in tabulation and charts. The collected data are organized and analysis is done using all the appropriate statistical, financial and simple mathematics tools.

3.5 Financial Tools

While adopting financial tools, ratio analysis is used as a benchmark for evaluating the financial position and performance of any firm. According to LM. Pandey, "Financial analysis is the process of identifying the financial strength and weakness of the balance sheet and profit and loss account." According to John wild, K.R, Subramanyan, report Halsey, "Financial analysis is the use of financial statements to analyze a company's financial position and performance and to assess future financial performance."

3.6 Ratio analysis

Ratio analysis is the widely used tool of financial analysis. Financial ratio is the mathematical relationship between two accounting figures. Ratio is simply one number expressed in terms of another and as such it expresses the numerical or quantitative relationship between two reprisals. Ratio analysis reflects the relative strengths and weakness of any organization and also indicates the operating and financial growth of the organization.

According to I.M. Pandey, "ratios help to summarize large quantities of financial data and to make quantitative judgment about the firm's financial performance. The relationship between two accounting figures expressed mathematically is known as financial ratio." Even though there are many ratios, only those ratios have been calculated which are related to the subject matter. Following ratios have been computed and analyzed in this study:

a) NPL to total deposits

This ratio tells the volume of NPL compared to ascertain the repayment capacity of the banks to it's depositors; this ratio is calculated as follows; NPL to total deposit

$$\text{Ratio} = \frac{\text{NPL}}{\text{Total deposits}}$$

b) NPL to total loans and advance ratio

This ratio determines the proportion of non- performing loans in the total loan portfolio. It is used to know the situation of NPL of Nepal bank limited. Knowing % of NPL to total loans and advances, we may be aware what are the possibilities of roll over of the funds exposed to risk assets? Higher ratio implies the bad quality of asset of banks in form of loans and advances.

Hence lower NPL to total loan and advances ratio in preferred as per international standard only 5% NPL is allowed but in the context of Nepal 10% NPL is accept Table This ratio is calculated as follows:

$$\text{NPL to total loan and advance} = \frac{\text{NPL}}{\text{Total loan and advances}}$$

3.7 Statistical Tools

Some important statistical tools are used to achieve the objective of this study. In this study, statistical tools such as correlation coefficient analysis, standard deviation, coefficient or variance, least square linear trend and hypothesis testing have been used. The basis analysis is written in point below:

1. Coefficient of correlation between different variables.
2. Trend analysis of important variable.

Correlation and Regression

Correlation may be defined as the degree of linear relationship existing between two or more variables. Tow variables are said to be correlated when the change in the value of one variable is accompanied by the change of another variable. For example in the study area, change in the value of loan and advances are associated with the change in NPL. Similarly, changes in value of LLP are accompanied by change in NPL.

Karl person's correlation coefficient: Karl person's correlation coefficient denoted by r measures the intensity or magnitude or degree of relationship between the two variables.

3.8 Trend Analysis

Trend analysis is one of the statistical tools, which is used to determine the improvement or deterioration of it's financial situation. Trend analysis informs about the excepted future values of various variables. The least square method has been adopted to measure the trend behaviors of these selected banks. This method is widely used in practices.

Diagrammatic and Graphical Representation

Diagrammatic and graphs are visual aids that give a bird eye view of a given set of numerical data. They represent the data in simple and readily comprehensive form. Hence various bar diagrams, pie chart and graph have been used for presentation and analysis of data. This representation has been conducted on the various factors related to NPL.

a) Trend line analysis of NPL.

b) Trend line analysis of Profit

c) Trend line comparison of profit and NPL

d) Bar diagram of trend of deposit

CHAPTER IV

DATA PRESENTATION AND ANALYSIS

This chapter is devoted to the presentation, analysis, interpretation and scoring the empirical finding out of the study through definite course of research methodology. To achieve the stated of the study and also to make the reader easier to understand the findings qualitative data and information has been analyze. Different types of ratios have been calculated to reach in the conclusion of this study.

4.1 Ratio analysis

4.1.1 Loan and advances to total assets

Loan and advances is the major portion of the assets of any balance sheet of commercial banks. Loan and advances directly generates incomes to the bank therefore it is essential to analysis the ratio of the loan and advances to total assets. The more the portion of loan and advances in the assets the more the effective utilization of assets of the bank.

Granting loan is the risky decision because each loan carries certain level of risk therefore loan and advances are also known as risky assets. Therefore if loan and advances to total assets ratio is low it indicated low risk to management and low profitability and vice versa.

Total Loan and Advances of listed commercial banks can be seen in the Table 1.1 below.

Table 4.1

Loan and advances to total assets

(In million Rs)

	ADBL			GBIME			NABIL		
FY	**L&A**	**TA**	**RATIO**	**L&A**	**TA**	**RATIO**	**L&A**	**TA**	**RATIO**
69/70	4968	7710	64%	2621	3902	67%	4537	7334	61%
70/71	5719	8852	64%	4177	6054	68%	5468	9029	60%
71/72	6858	10081	68%	4894	6919	70%	6550	11869	55%
72/73	7949	11179	71%	5922	8770	67%	7610	12762	59%
73/74	8821	12687	69%	7896	11659	67%	8988	14033	64%
MEAN	**67%**			**68%**			**60%**		
S.D.	**4**			**3**			**4**		
C.V.	**6%**			**4%**			**7%**		

Source: Annual report 2069-2074

Fig 4.1 Percentage of loan & advances to total Assets

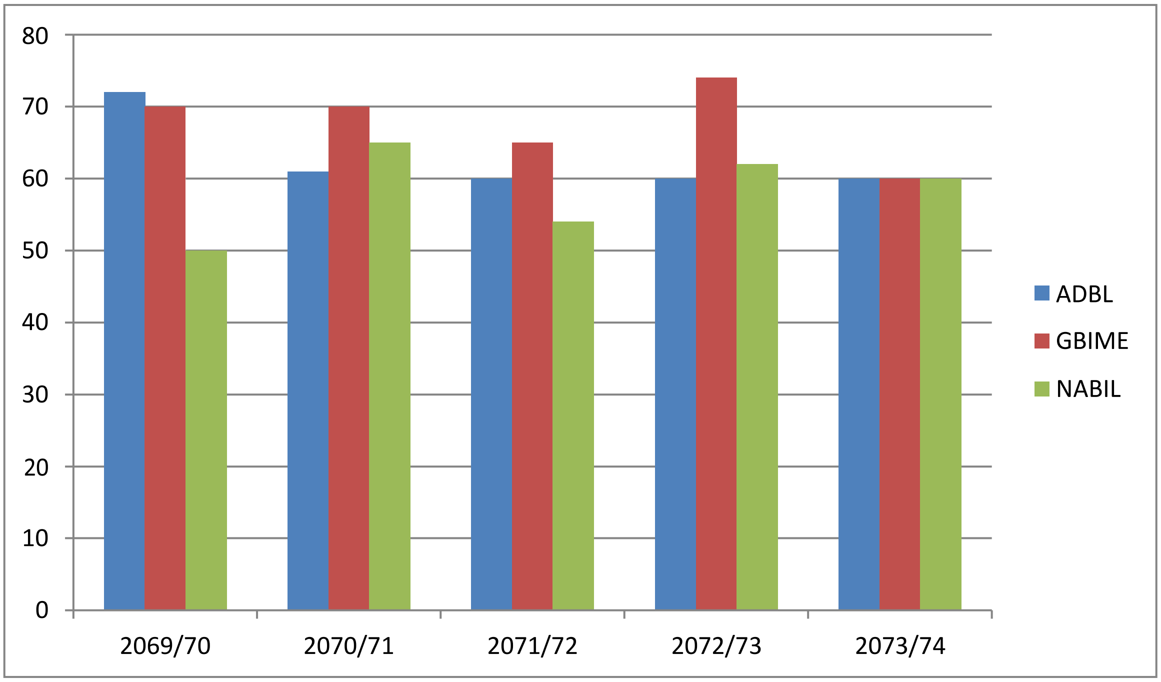

Table number 4.1 shows that total loan and advances to total assets of all the sample banks i.e., ADBL,GBIME & NABIL.

The table depicts that total loan and advances to total assets of ADBL, GBIME & NABIL is in between 60-68% whereas this ratio of NABIL has comparatively low risky assets in their portfolio. Higher portion of Loan and advances of ADBL and GBIME provides the opportunity to generate higher interest income with low liquidity whereas lower portion of loan and advances of NABIL indicates comparatively high level of liquidity but relatively is the opportunity for income generation.

Regarding the standard deviation (S.D.) and coefficient of Variation (C.V.) of the ratio as calculated and displayed in the above table we find that the NABIL & ADBL has the highest SD and CV of 6% and 7% respectively. This means NABIL has the highest variability in the portion of Loan and advances in total Assets. Whereas ADBL has same SD and CV of 6% and 4 % which is moderate among the banks under study.

In total we can say that GBIME and ADBL shows the managed trend of loan and advances in total assets which mean it disburse loan according the size of growth of assets. Likewise ADBL has the most scattered trend of flowing loan. Going through its results we can say that it does not have any policy regarding proportion of loan and advances in total assets. Other banks seem to have moderate consistency.

4.1.2 Loan and advances to total deposit

Loan and advances to total deposit ratio indicates the proportion of deposit utilized as lending. This ratio is also called CD ratio. CD ratio is the most important to analyze the banks utilization of their deposits and to know the liquidity position of the bank. The core banking function is to take deposit and channel the funds in the form of loan. For every deposits bank has to pay interest and failing to utilize the deposit may hamper the profitability of the bank. Therefore, Higher CD ratio implies higher utilization of the deposit and low fund available to service the depositors when they come for withdrawal and vice versa. 75%of CD ratio is assumed to be optimal in banking sector however up to 80% limit is permissible by NRB.

Table 4.2

Loan and advances to total deposit

(In Million Rs)

FY	ADBL			GBIME			NABIL		
	L&A	**TD**	**RATIO**	**L&A**	**TD**	**RATIO**	**L&A**	**TD**	**RATIO**
69/70	4968	5448	91%	2621	3412	76%	4537	6361	71%
70/71	5719	7703	74%	4177	5231	79%	5468	7539	72%
71/72	6888	8739	78%	4894	6018	81%	6550	10424	62%
72/73	7949	12830	61%	5922	7468	79%	7610	11027	69%
73/74	8821	13542	65%	7896	10192	77%	8988	12184	73%
MEAN			**74%**	**78%**			**69%**		
S.D.			**11.77**	**1.95**			**4.39**		
C.V.			**8%**	**10%**			**8%**		
Correlation			**0.98**	**0.99**			**0.99**		

Source: Annual report 2069-2074

Fig:4.2 loans & advances to total deposit

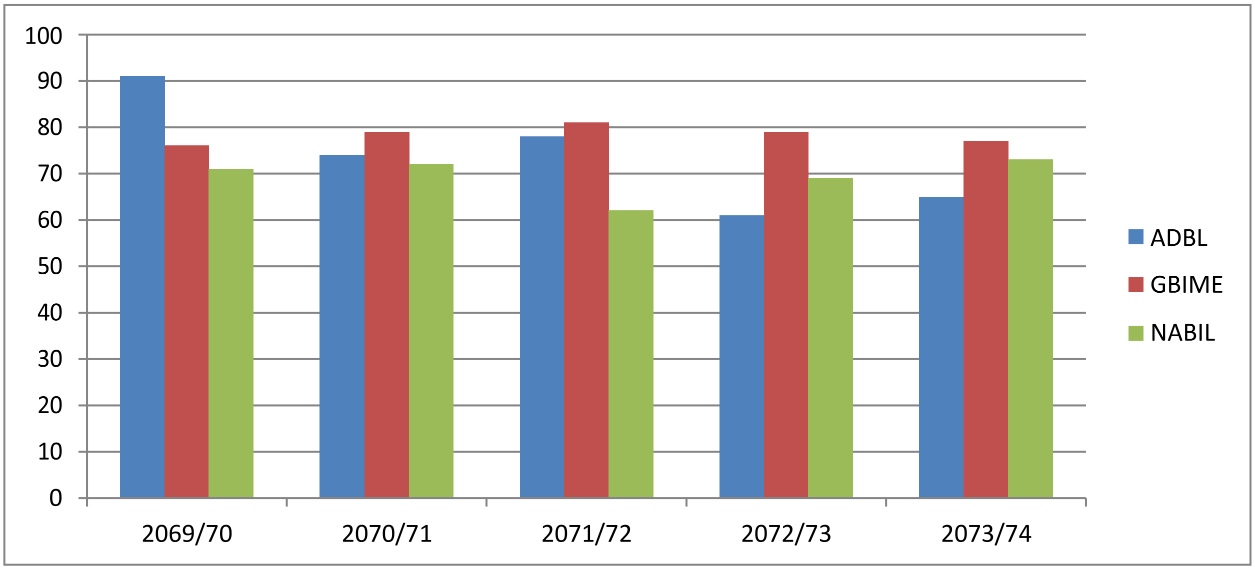

Table number 4.2 exhibits the ratio of loan and advances to total deposit of selected commercial banks for the period of five years. From the above table it is clear that GBIME is in the top in utilizing depositor's money. It has highest CD of 78 % which is high among three banks. Likewise ADBL also 74 % of CD ratio which is slightly lower than the standard assumed. If we see the CD ratio of NABIL is 69% which indicates enough liquidity available with these banks.

Standard deviation ADBL,GBIME & NABIL are 6, 8, 5 respectively. Likewise CV is 8, 10, 8, respectively. This indicates that GBIME has highest variability is CD ratio and NABIL has the lowest one. ADBL has moderate variability in its CD ratios. In total we can say that GBIME utilizes its depositor money optimally and also maintains the liquidity position of the bank. NABIL has not been able to utilize its deposits optimally.69%CD ratio implies that either it has ideal money in the form of cash and bank balance or it has invested high amount in low yield investment portfolio. Likewise other banks can be considered as moderate in utilization of deposit and moderate in liquidity aspect.

4.1.3 Loan loss Provision to loan and advances

Loan loss provision to loan and advances shows % of loan is covered against the possible future loss due to non-payment of loan. Since there is risk inherent in the loan and advances, NRB has directed commercial banks to classify its loan and advances into different category and accordingly to make provision for possible losses. Loan loss provision signifies the cushion against the future contingencies crease by the default of borrower in the payment of loan and ensures the continuous solvency of the bank. Since high provision has to be made for non-performing loan, higher provision for loan loss reflects increasing non-performing loan in the volume of total loan.

The low ratio signifies the good quality of assets in the volume of total loan. It indicates how efficiently it manages loan and advances and makes efforts to cope with portable loan losses. Higher ratio implies higher portion of NPL in the total loan Portfolio. The ratio is calculated as follows.

Table 4.3

Loan loss provision to loan and advances

(In million Rs)

Source: Annual report 2069-2074

	ADBL			GBIME			NABIL		
	LLP	L&A	RATIO	LLP	L&A	RATIO	LLP	L&A	RATIO
69/70	127	4968	2%	47	2621	1%	101	4537	2%
70/71	87	5719	1%	44	4177	1%	125	5468	2%
71/72	244	6888	3%	55	4894	1%	122	6550	1%
72/73	145	7949	1%	61	5922	1%	88	7610	1%
73/74	177	8821	2%	36	7896	0.4%	72	8988	0.8%
MEAN			**2%**	**1%**			**1%**		
S.D.			**1**	**1**			**1**		
C.V.			**27%**	**31%**			**40%**		
Correlation			**(0.46)**	**0.96**			**0.94**		

Table number 4.3 shows the ratio of loan loss provision in total loan and advances of selected banks from 2069/70- 2073/74. It is clear to see that ADBL have higher average ratio of loan loss provision in total loan and advances making 2%. Likewise GBIME & NABIL have moderate LLP in total Loan and Advances making 1%each. GBIME & NABIL have decreased trend of loan loss provision in total loan which indicates that these banks have been able to flow quality loan in recent years.

If we go through the SD and CV of these ratios it can be seen that all banks have SD of 1. CV of ADBL,GBIME & NABIL are 27, 31, 40 respectively. This indicates NABIL has more variability in provision because of the higher growth of Loan flow in this bank. There is a positive correlation between loan loss provision and loan and advances. In every increment of loan and advances loan loss provision automatically increases. The table shows how wonderfully NABIL has done the management of loan and advances. In the one hand it has increased the volume of loan and in the other hand it has decreased the level of provisioning from 1%to 0.8 %s implying its well managed portfolio with good loan in respect to other banks under study.

4.1.4 Non-performing loan to total loan and advances

NRB has directed the commercial banks to classify their loan into two categories i.e. performing loan and non-performing loan. Non-performing loan to total loan and advances ratio determines the proportion of nonperforming loan in the total loan portfolio. Higher ratio implies the bad quality of the assets of the bank in the form of loan and lower return from the loan portfolio and lower ratio implies good quality of loan. Hence lower NPL to total credit ratio is preferred. The ratio is calculated as follows:

Table 4.4

Non-performing loan to total loan and advances

(In million Rs)

	ADBL			GBIME			NABIL		
	NPL	**L&A**	**RATIO**	**NPL**	**L&A**	**RATIO**	**NPL**	**L&A**	**RATIO**
69/70	321	4968	6%	61	2621	2%	20	4537	0.4%
70/71	340	5719	5%	109	4177	2%	24	5468	0.4%
71/72	386	6888	5%	112	4894	2%	17	6550	0.2%
72/73	363	7949	4%	115	5922	1%	18	7610	0.2%
73/74	426	8821	4%	129	7896	1%	19	8988	0.2%
MEAN	**5%**			**2%**			**0.3%**		
S.D.	**1%**			**0.40%**			**0.1%**		

Source: Annual report 2069-2074

Fig:4.3 % of Non-Performing loan to loans & advances

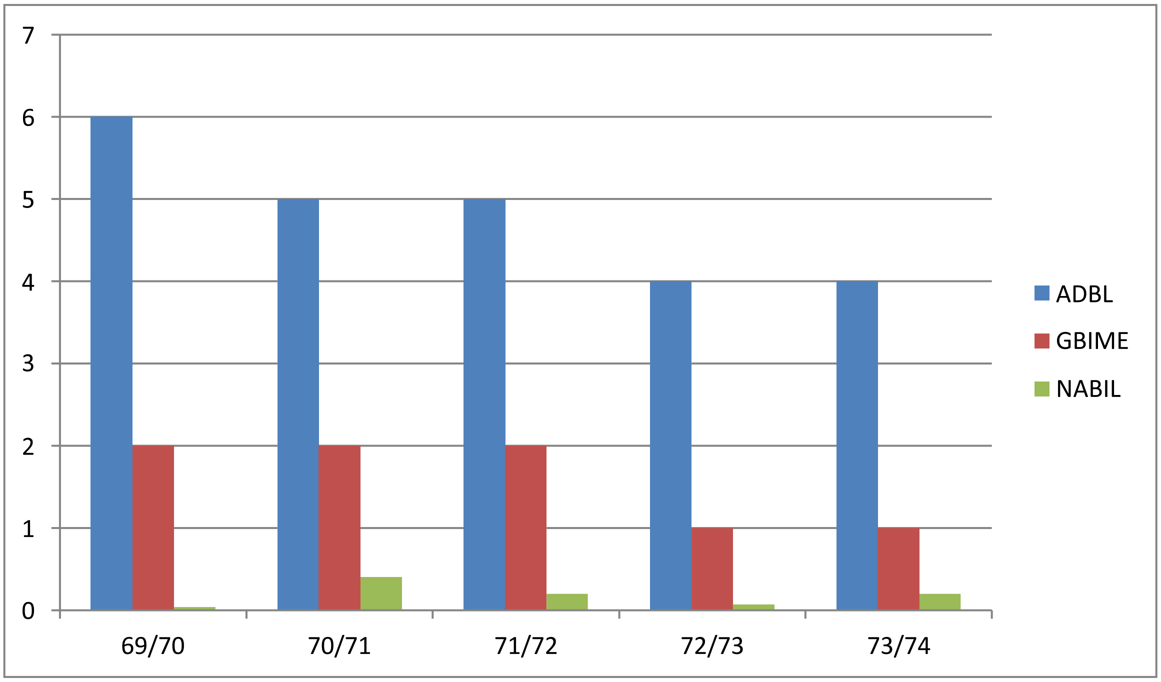

Table number 4.4 exhibits the ratio of non-performing loan to total loan and advances of the selected commercial banks for the period of five year from 2069/70 to 2073/74. From the above table it is clear that NPL of all commercial banks has been decreasing. ADBL started from 6%of NPL in total loan and advances and is able to successfully decrease its NPL to 4 % in the year2073/74 but still its NPL to Total loan and Advance is high in comparison to other banks.

GBIME is able maintain its NPL level very low making 2% which indicates that this banks have been making contentious effort to maintain its NPL level low. If we compare the NPL with other banks we see that when other banks had above 4% of NPL these banks were able to maintain the NPL at 1 % which is considerably significant.

NABIL is able maintain its NPL level very low making 0.2% which indicates that this bank have been making contentious effort to maintain its NPL level low. If we compare the NPL with other banks we see that this bank is very efficient in comparison to other banks.

4.1.5 Total provision to non-performing loan

This ratio determines provision held to non-performing loan. NRB had directed all commercial bank to provide provision for all types of loan and advances. This ratio measures up to what extend of risk inherit in NPL is covered by the total loan loss provision. More than 100 percent ratio signifies that the bank is insured against future contingencies that may create due to bad loans, whereas lower than 100 percent may create huge provision in coming future due to requirement of high provision to substandard loan and advances.

Table 4.5

Total provision to non-performing loan

(In million Rs)

FY	ADBL			GBIME			NABIL		
	LLP	**NPL**	**RATIO**	**LLP**	**NPL**	**RATIO**	**LLP**	**NPL**	**RATIO**
69/70	127	321	39%	47	61	77%	4537	20	500%
70/71	87	340	25%	44	109	40%	5468	24	520%
71/72	244	386	63%	55	112	49%	6550	17	717%
72/73	145	363	39%	61	115	53%	7610	18	488%
73/74	177	426	41%	36	129	27%	8988	19	378%
MEAN			**42%**	**50%**			**522%**		

Source: Annual report 2069-2074

Table number 4.5 shows the ratio of provision to NPL of selected commercial bank for five year starting from2069/70 to 2073/74. From the above table it can be seen that the total provision of all banks are increasing and about almost all commercial banks are safe against the future contingencies that may be created due to nonpayment of loan.

NABIL have highest average total provision of 522% and GBIME & ADBL have comparatively low average total provision of 42 and 50, which indicates NABIL bank is prepared against the future possible loss and latter two banks need to increase.

4.1.6 Return on loan and advances

Return on loan and advances ratio indicates how efficiently the bank has employed its resources in the form of loan and advances. Net profit of a bank largely depends upon interest earn from loan and advances and there is positive correlation between effective utilization of loan and advances and net profit. This ratio measures the bank's profitability with respect to loan and advances. Higher the ratios better the performance of the bank.

Table 4.6

Return on loan and advances

(In million Rs)

FY	ADBL			GBIME			NABIL		
	NP	L&A	RATIO	NP	L&A	RATIO	NP	L&A	RATIO
69/70	321	4968	6%	61	2621	2%	57	4537	1%
70/71	340	5719	5%	109	4177	2%	117	5468	2%
71/72	386	6888	5%	112	4894	2%	153	6550	2%
72/73	363	7949	4%	115	5922	1%	232	7610	3%
73/74	426	8821	4%	129	7896	1%	351	8988	3%
MEAN	**5%**			**2%**			**3%**		

Source: Annual report 2069-2074

Fig:4.4 Return on loan and Advances

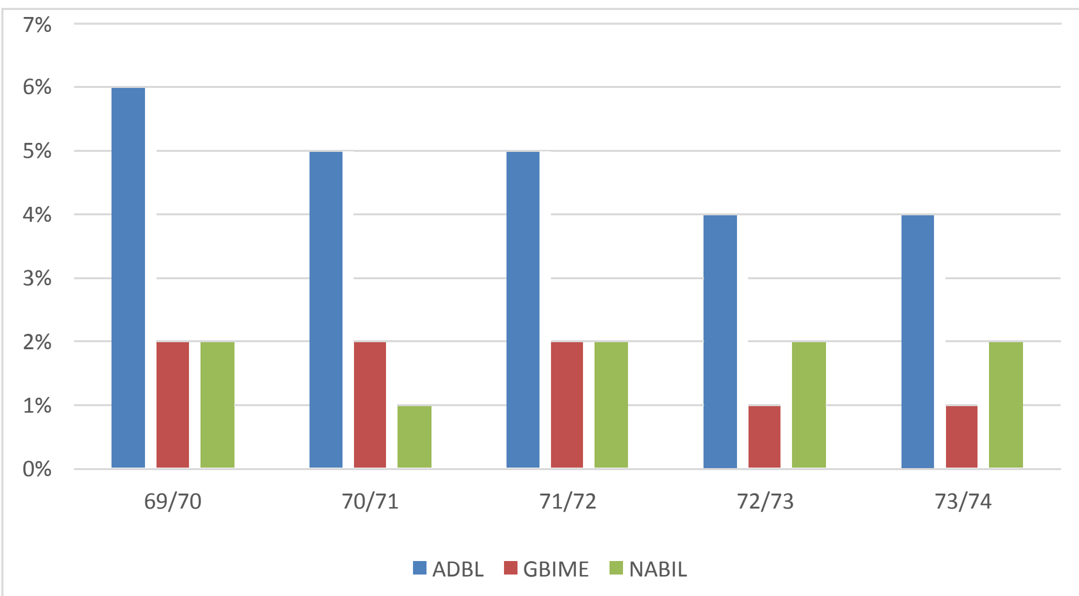

Table number 4.6 shows the ratio of Return on loan and Advances of selected commercial bank for five year starting from2069/70 to 2073/74. From the above table it can be seen that the Net profit of all the banks are either constant or decreasing and the % of net profit in respect of loan is also decreasing except of NABIL.ADBL & GBIME have a fluctuating trend in return on loan and advances. They started from 6% and reached to 1 % and showed growth in return on loan and advances resulting 6% of ADBL which shows decreased efficiency of ADBL to utilize its resources which further indicates that in the early year they invested high portion of their assets in loan in advances but due to lower quality of loan they switched their portfolio from loan and advances to other less risky investment like treasury bills and government bank.

NABIL show the most consistent trend of return on loan and advances. It has been able to manage its return at 3% throughout the year. This indicates that these banks are very much efficient to manage their loan portfolio.

4.2 Correlation analysis

Correlation is a statistical tool that can be used to describe the degree of linear relationship of one variable to other variables. Correlation analysis is another important tool of statistics. It describes the relationship between variables and degree of dependency of one variable with another variable. Two variables are said to be correlated when the change in one variable results the change in another variables. Different model for correlation analysis has been formulated and we have used Karl Pearson Coefficient of correlation to determine the relationship between variables studied.

4.2.1Correlation between loan loss provision and loan and advances

This relationship shows the likely pattern of loan loss provision if loan changes. In other words, correlation of loan loss provision and loan and advances indicates the degree of linear relationship between these two variables, which helps us to take decision regarding loan and advances.

Following table no.4.7 exhibits the correlation between Loan Loss Provision to Loan and Advances.

Table.4.7

Correlation between loan loss provision and loan and advances

Banks	Correlation coefficient	Probable Error (P.E.)	σ*(P.E.)
ADBL	(0.45850)	0.23823	1.42936
GBIME	0.96190	0.02254	0.13521
NABIL	0.91680	0.48100	0.28863

Fig 4.5

Correlation Between Loan Loss Provision & Loan & Advances

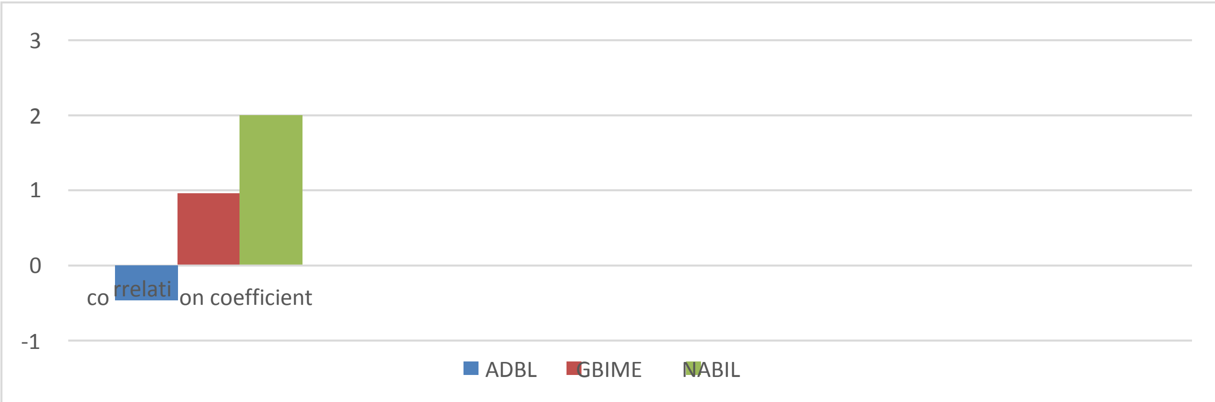

Table number 4.7 shows the relationship between LLP and Loan and advances for the selected commercial Banks. It is clear to see that almost all banks have perfect positive correlation between loan loss provision and loan and advances except ADBL.ADBL has a negative correlation of 0.4585, which indicates that the provision amount does not follow the trend of loan and advances. The cause of negative correlation is that the bank has write off its huge amount of bad loan during 2070/71 which has decreased the loan loss provision amount but loan is still increasing which results negative correlation between loan loss provision. It has 6 P.E. of 1.42936, which shows the correlation is insignificant. GBIME & NABIL have perfect positive correlation of 0.9619,0.9168 respectively which indicates that loan loss provision follows the pattern of loan and advances which means if loan and advances increases loan loss provision also increases in the same ratio and vice versa. Likewise correlations of these banks are higher than the six times of its P.E., which proves the above claim.

4.2.2 Correlation between loan loss provision and non-performing loan

This relationship shows the degree of linear relationship between these Non-performing loan and Loan Loss Provision. Following table no. 2.2 exhibits the correlation between Loan Loss Provision and Non-performing loan.

Above table 2.2 shows the relationship between LLP and NPL for selected commercial Banks. It is clear to see that almost all banks have perfect positive correlation between loan loss provision and non-performing loan except ADBL.

GBIME & NABIL have perfect positive correlation of 0.7687, 0.8746 respectively which indicates that loan loss provision is perfectly correlated with the non-performing loan level which means if non-performing loan increases, loan loss provision also increases in same ratio and vice versa. In other words, it can be said that if these banks will to decrease the level of their Loan loss provision, they have to focus to increase quality loan portfolio and reduce the level of non-performing loan. Likewise, correlations of these banks are higher than the six times of its P.E. which proves the above claim.

ADBL has a negative correlation of 0.4457, which indicates that the loan loss provision of ADBL is not affected, by the non-performing loan level. The reason for negative correlation between LLP and NPL is loan loss provision is increasing even non-performing loan level is decreasing. It has 1.45034 of P.E. this shows the correlation is insignificant.

4.2.3 Correlation between loan and advances to deposit

Accepting deposit and granting loan are the major function of commercial banks. The relationship of deposit and loan and advances should always be perfect positive.

Table 4.8

Correlation between deposit and loan and advances

Banks	Correlation coefficient	Probable Error(P.E.)	σ *(P.E.)
ADBL	0.97780	0.01324	0.07943
GBIME	0.98650	0.00808	0.04847
NABIL	0.99130	0.00520	0.03120

Table number 4.8 shows the relationship between Total Deposit and Loan and Advances for five commercial banks. It is clear to see that all banks have perfect positive correlation between Deposit and Loan and Advances for review period.

Perfect positive correlation between Deposit and Loan indicates that loan and advances largely depends on deposit volume of these banks which means if one want to increase loan and advances, it has to accept the additional deposit. Likewise, correlations of these banks are higher than the six times of its P.E. that proves that the correlation calculated above are highly significant and reliable. ADBL has a negative correlation of 0.4457, which indicates that the loan loss provision of NICB is not affected by the non-performing loan level. The reason for negative correlation between LLP and NPL is loan loss provision is increasing even non-performing loan level is decreasing. It has 1.45034 of P.E. This shows the correlation is insignificant.

4.3 Trend analysis

Trend analysis is an analysis of financial ratio over time used to determine the patterns of growth. Trend analysis informs about the future expected values of studied variables. It gives a glimpse of future expected value if the same growth rate level is achieved. This information is crucial for management to make decision regarding future. This method is widely used in practice. The least square method has been used to measure the trend behavior of these selected banks.

4.3.1 Trend analysis of loan and advances

Trend analysis of loan and advances show the pattern of loan growth. It may be positive of Negative. Trend helps the management to estimate the future volume of their loan and if required volume of loan is high then the trend then management can either increase their marketing efforts to achieve the required loan volume or review their target. Therefore, it is most commonly used statistical tools of management. Following table no3.1 shows the pattern of loan and advances of listed commercial banks.

Table 4.9

Trend analysis of loan and advances

Banks	Forecasted loan and advances				
	2069/70	2070/71	2071/72	2072/73	2073/74
ADBL	4968	5719	6888	7949	8821
GBIME	2621	4177	4894	5922	7896
NABIL	4637	5468	6550	7610	8988

Source: Annual report 2069-2074

FIG 4.6: Trend of Loan and Advance

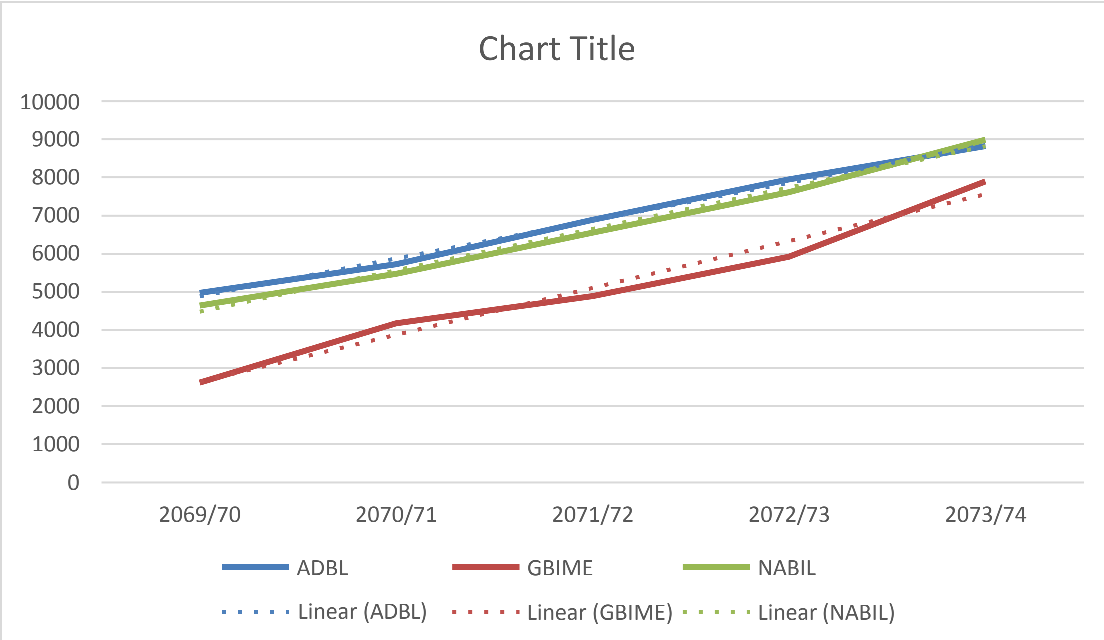

Table number 4.9 shows the trend of loan and advances of selected commercial banks of coming five years. It is clear that all the banks have increasing trend of loan and advances.

ADBL & NABIL show the highest increasing trend of loan and advances. If it continues the same trend of increment in the loan and advances it will become around two times greater than the current average loan. Increasing loan and advances in one hand increases the net interest income of banks but in the other hand there is high chance of flowing bad loan in the race of increasing loan and advances. Therefore, management should be sure about the quality than the quantity of loan.

Similarly, GBIME shows the lowest growth of loan and advances however it is growing at good pace growth in their loan and advances and if they continue the same trend their loan portfolio will become slightly more than double of their current position. The trend of loan and advances has been presented to have bird eye on future trend.

4.3.2 Trend analysis of loan loss provision

Trend analysis of loan loss provision helps the management to estimate the future volume of loan loss provision. Following table no3.2 illustrate the pattern of loan and advances of listed commercial banks.

Table 4.10

Trend analysis of loan loss provision

Banks	Forecasted loan Loss Provision				
	2069/70	**2070/71**	**2071/72**	**2072/73**	**2073/74**
ADBL	127	87	244	145	177
GBIME	47	44	55	61	36
NABIL	101	125	122	88	72

Source: Annual report 2069-2074

Fig 4.7 Analysis of loan loss provision

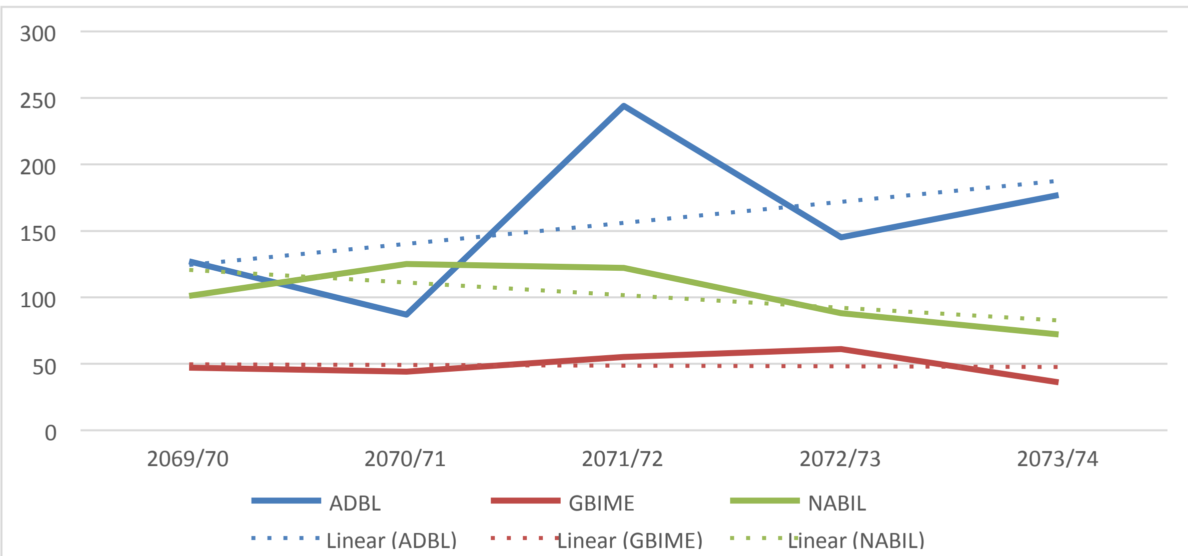

Table number 4.10 shows the trend of loan loss provision of selected commercial banks for the coming five years. Table clears that loan loss provision of all the banks except ADBL is decreasing. GBIME has been able to decrease the level of provision throughout the year which is good sign. NABIL have reducing trend of loan loss provision. Among them ADBL has shown the highest growth rate in LLP which indicates future pressure on profit and loss account of this bank due to additional loan loss provision. If ADBL fails to switch their loan portfolio with good loan it may create future losses. Likewise other banks have growing trend in their provision which increases the loan loss provision by almost double of all the banks. Therefore, these banks also need to manage their loan portfolio. The trend of loan Loss Provision has been presented to have bird eye view on future.

4.3.3 Trend analysis non-performing loan

Trend analysis of Non- performing Loan helps the management to control the level of Non-performing Loan in their future portfolio. Following table no3.3 illustrate the pattern of Non-performing Loan of listed commercial banks.

Table 4.11 Trend analysis of non-performing loan

Banks	FORECASTED NON PERFORMING LOAN				
	2069/70	2070/71	2071/72	2072/73	2073/74
ADBL	321	340	386	363	426
GBIME	61	109	112	115	129
NABIL	20	24	17	18	19

Source: Annual report 2069-2074

Fig 4.8

Trend Analysis of Non-performing loan

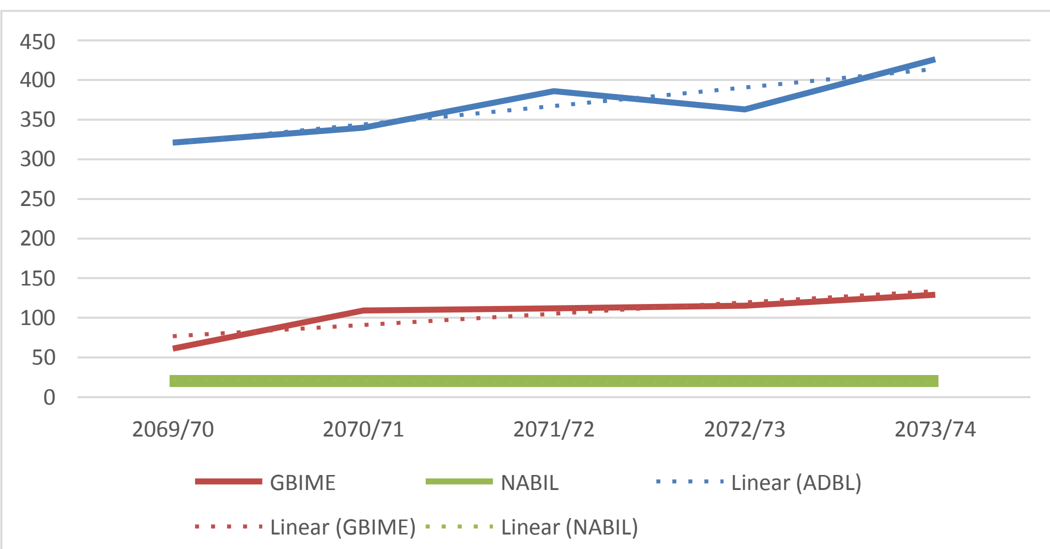

Table number 4.11 shows the trend of Non- performing Loan of selected commercial banks for the coming 5 years. It is clear to see that Non- performing Loan of ADBL & GBIME is increasing and that of NABIL is decreasing. NABIL have been doing well in respect of quality Loan. We can see that NABIL have been very liberal regarding flowing loan which in the one hand they utilize their loan growth but in the other hand it has enable them to maintain a better portfolio and made them able to decrease the level of provision. ADBL & GBIME have increasing level of NPL. These banks have reported higher growth in loan and advances and due to positive correlation between loan and advances and NPL, the NPL of these banks are also increasing.

4.4 Regression Analysis

4.4.1 Regression Analysis ADBL

Here, Independent Variable(x)= Non-Performing Loan
Dependent Variable(y)= Net Profit
Regression equation Y=a+bX
Where a= y-intercept
b = slope of the line

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.498026561
R Square	0.248030456
Adjusted R Square	-0.002626059
Standard Error	74.57456822
Observations	5

ANOVA

	Df	*SS*	*MS*	*F*	*Significance F*
Regression	1	5503.101325	5503.101	0.989523276	0.393179676
Residual	3	16684.09868	5561.366		
Total	4	22187.2			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*
Intercept	-84.11953214	336.1348497	-0.25026	0.81854913	-1153.850643	985.6115783
X Variable 1	0.906098944	0.910883042	0.994748	0.393179676	-1.992737429	3.804935316

we can observe that NPL will have moderate impact upon Net Profit i.e Net profit is explained around 50 % by Non-Performing loan of ADBL. Standard error is 74.57. The significance F is 0.39 which shows that significance is 39% for given regression of ADBL.

4.4.2 Regression Analysis GBIME

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.862786081
R Square	0.744399822
Adjusted R Square	0.659199763
Standard Error	33.66650306
Observations	5

ANOVA

	Df	*SS*	*MS*	*F*	*Significance F*
Regression	1	9902.899716	9902.899716	8.737081042	0.059742615
Residual	3	3400.300284	1133.433428		
Total	4	13303.2			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*
Intercept	-86.94336521	70.09127557	-1.240430631	0.30298683	-310.0050862
X Variable 1	1.923416019	0.650713844	2.955855382	0.059742615	-0.14744585

we can observe that NPL will have adeuate impact upon Net Profit i.e Net profit is explained around 74% by Non-Performing loan of GBIME. Standard error is 33.66. The significance F is 0.59 which shows that significance is 59% for given regression of GBIME.

4.4.3 Regression Analysis NABIL

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.150187488
R Square	0.022556281
Adjusted R Square	-0.303258291
Standard Error	49.51453825
Observations	5

ANOVA

	Df	*SS*	*MS*	*F*	*Significance F*
Regression	1	169.7315068	169.7315	0.069230425	0.80949669
Residual	3	7355.068493	2451.689		
Total	4	7524.8			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*
Intercept	299.0547945	180.9562598	1.652636	0.196974677	-276.8287858
X Variable 1	-2.410958904	9.163076399	-0.26312	0.80949669	-31.57195754

we can observe that NPL will have no impact upon Net Profit i.e Net profit is explained around 2% by Non-Performing loan of NABIL. Standard error is 49.51.

Hence analyzing all three-regression analysis we came to know that three different banks have different impact of Non-Performing loan on Net Profit hence there exist no proper relationship between Net-Profit & Non-Performing loan.

4.5 Major findings

4.5.1 Major findings of Trend Analysis

In this segment we have used least square method to find out the growth patterns and predicted the future expected values. All the banks have increasing trend of loan and advances. ADBL & NABIL show the higher growth rate of Loan and advances. Similarly, GBIME shows the lower growth rate of loan and advances. However, every bank are growing their loan and advances and if they continue the same trend their loan portfolio will be slightly more than double of current average loan. Loan Loss Provision of commercial banks has in increasing trend except NABIL which is somehow constant. GBIME has been able to decrease the provision throughout the year. Among them ADBL has shown the highest growth rate in LLP. Likewise other banks have growing trend in their provision which increases the loan loss provision by almost double of all the banks. Therefore, these banks also need to manage their loan portfolio. Non- performing Loan of ADBL, is increasing and that of GBIME & NABIL is decreasing. Both NABIL & GBIME are able to resource efficiently which has made them able to flow quality loan and decrease the level of provision. As we analyzed various ratios and Loan and Advances to total assets, we found that more than 60 % of total assets of all the banks are in the form of loan and advances and they have less deviation throughout the period and lesser CV in ratio.

4.5.2 Major Findings of Ratio Analysis

Likewise the analysis of ratio of loan and advances to total deposits has cleared that NABIL is in the top in utilization of depositor's money. It has the highest average CD ratio of 85% Likewise GBIME have 77% of average CD ratio which is slightly high than recommended of 75% which shows NABIL is able to utilize its resources very effectively compared to that of other banks.CD ratio of ADBL is comparatively low which indicates enough liquidity available with this bank, this ensures low risks for banks regarding liquidity related problems .Other analyses of loan loss provision in total loan and advances clarifies that ADBL & GBIME have higher ratio of loan loss provision in total loan and advances making 5% and 4% respectively but they are in decreasing trend, further NABIL have low loan loss provision 0.5% . Non-performing loan to total loan and advances of all commercial banks have been decreasing. ADBL & GBIME both have reduced the level of heir NPL from 8% to 3% but still their NPL level is high among other banks. NABIL have maintained their NPL level very low making 1% which indicates that this bank has been making continuous efforts to maintain their NPL level very low. Ratio of provision to Non-performing loan of bank shows that the level of provision of all banks are increasing and almost all commercial banks have created provision greater than the amount of non-performing loan which shows that all banks are safe against the future contingencies that may be created due to non-payment of loan. Return of loan and advances of bank shows that NABIL have most consistent return throughout the period where as the ratio of GBIME & ADBL is growing likewise return on loan and advances of all banks are in decreasing trend.

4.5.3 Major findings of Regression analysis

After analyzing regression of each bank regarding the impact of Non-Performing loan on Net-Profit we observed that each bank have different impact of non-performing loan on Net-Profit and that relation shows that there exist no consistent relationship between non-Performing loan & Net-Profit.

CHAPTER V
SUMMARY, CONCLUSION AND IMPLICATIONS

This segment includes the major findings and conclusion of the study. This chapter deals about the main themes of the study and gives recommendations for improvement non-performing loan.

5.1 Summary

Banking sector runs on public money and hence its security and proper utilization is very important aspect for banks. Non-Performing loan is that category of loan which principals and interest is due for more than three months from its payment date. Higher Non-performing loan suggests inefficiency and higher risk for banks hence this factor is analyzed with reference to profitability and we found there exist no direct relationship between Net Profit & Non-Performing loan .This was because with increase in loans and advances chances of increasing NPL also increases hence ratio between NPL & Loans and advances is more important to measure efficiency and risk factor. The major objective of this research is to understand the relationship between Non-performing loan & Profitability of the bank. For this research descriptive method is used and secondary data from Annual report of bank is used to identify relationship between Non-Performing loan & Profitability.

Loan and advances reflected in assets side of balance sheet of commercial banks. Loan and advances is direct contributor to banks income. Loan can be divided into two categories namely performing loan and non-performing loan. Performing loan are those loan and advances which service the banks on time. Which means the loan which pays its installment and interest within the time is known as performing loan. Performing loan is the contributor of bank's growth and prosperity. Non-performing loan is such loan which fails to pay its interest to bank within stipulated time. Non-performing loan is the major concern of management because non-performing loan needs to make provision and it hampers the profitability of bank.

This study mainly focuses on analyzing the non-performing loan issue of Nepalese commercial banks. Among total banks, five banks have been selected as sample. Required data have been collected either from the annual report of the bank or from the website of Nepal Rastra Bank. From the study following conclusion have been drawn.

1) Loan and advances are the major determinant of earning of commercial banks and major portion of their earning assets. The study of loan and advances to total assets has sighted that most of the banks have maintained sixty percent of their total assets in the form of loan and advances which obviously indicate high attention of management towards of loan and advances.

   Loan and advances largely depends upon the level of deposit. The banks having more deposit have higher portion of loan and advances and vice versa. The study has revealed that most of the banks has maintained CD ratio around 78 percent. Among them GBIME has highest CD ratio of 78 percent which indicates high liquidity risk in GBIME in comparison with the other banks studied. Likewise, NABIL has also 77 percent of average CD ratio which is slightly high than ideal CD ratio of 75 percent. ADBL is comparatively low risky regarding liquidity.

2) Loan loss provision is a safeguard against future contingencies which NRB has made mandatory to all type of loan and advances. Higher portion of LLP indicates high portion of NPL in total loan Portfolio and bad conditions of banks too. Our analysis of loan loss provision in total loan and advances has cleared that ADBL is the banks which have high loan loss provision of around percent in respect of total loan but they are in decreasing trend. Likewise, GBIME & NABIL have moderate LLP 2%-1% percent respectively. NABIL has the lowest portion of LLP of 0.5% percent only. This indicated that NABIL is doing well in respect of quality loan management whereas GBIME is better compared to ADBL whereas ADBL was poor in loan management but now they are managing their loan perfectly.

3) NRB has directed to divide the total loan onto two parts- performing loan and non-performing loan. Non-performing loan are those loans which fails to service in time and it is bad for financial health of any bank therefore, we have analyzed the portion of non-performing loan in total loan and advances which reveals that non-performing loan of commercial banks have been decreasing. Due to strict NRB regulations regarding loan loss provision, all banks have been focusing on quality loan which has resultant lower non-performing loan ratio. Among them NABIL have maintained their NPL level very low making 1 percent and 2 percent respectively which indicates that these banks have been making continuous effort to maintain their NPL level low.

5.2 Conclusions

The study concludes that:

1. Provision to non-performing loan of bank shows that the level of provision of all banks are increasing and almost all commercial banks have created provision greater than the amount of non-performing loan which shows that all banks are safe against the future contingencies that may be created due to nonpayment of loan.
2. Correlation between total deposit and total loan and advances indicates perfect positive which shows with increase in total deposit loan & advances increases as well. NABIL and ADBL shows the higher growth rate of loan and advances. Other bank i.e. GBIME have a moderate growth in their loan and advances and if they continue same trend, their portfolio will become slightly more than the double of current average loan.
3. Non-performing loan of ADBL is in increasing trend and that of GBIME has decreasing trend whereas NABIL has low and is not growing which is good for the bank.
4. All banks extending credit rapidly which loan loss provision and Non-performing loan is also increasing however NABIL is able to increase credit and reduce loan loss provision and non-performing loan as well. Their better managerial ability of flowing quality loan has helped decrease the level of provision.
5. There exists no significance relationship between Non-performing loan and Profitability as in case of NABIL & GBIME there was positive relationship whereas in case of ADBL there exist inverse relationship.

5.3 Implications

Based on the findings of the study and taking into consideration, the relevant issues, the appropriate recommendations are made as far as possible to make the study useful.

1) Commercial banks should follow a policy regarding loan disbursement. Loan and advances are risky assets. In the one hand, it generates high return to banks. On the other hand, it may become the cause of bank collapse. Therefore, a tread off between risk and return should be maintained and the portion of loan in total assets should be monitored closely.

2) The major job of bank is to collect deposit and invest that money in profit making projects. For every rupee, banks have to pay interest. Therefore, banks should be conscious to utilize the depositor’s money. Banks should be ready to pay depositor’s money on demand. This increases the creditability of banks. Therefore, banks should not invest it’s all money in loan and

advances. Banks should maintain certain level of CD ratio. Some banks have been found to have very high CD ratio and some have very low. High CD ratio generated more earning and less liquidity available with bank and vice versa. Therefore, banks have to utilize the depositor's money optimally.

3) Non-performing loan of all banks have been found to have decreased. It is good symptom. Banks should focus on quality loan in coming days and maintain their loan portfolio more productive.
4) Most of the banks have been maintaining the level of loan loss provision above the level of non-performing. Still some banks are not maintaining loan loss provision for their entire non-performing loan. Uncovered non-performing loan may create future loss to banks and certainly hampers the profitability of banks. Therefore, banks having uncovered non-performing loan should make adequate provision. In other word the ratio of provision to non-performing loan should be higher than 100 percent.

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APPENDIX-I

Loans & Advances

Year/Million	ADBL	GBIME	NABIL
2069/70	4968	2621	4637
2070/01	5719	4177	5468
2071/72	6858	4894	6550
2072/73	7949	5922	7610
2073/74	8821	7896	8988

Source :Annual Report 2069-2074

Total Assets

Year/Million	ADBL	GBIME	NABIL
2069/70	7710	3920	7334
2070/01	8852	6054	9029
2071/72	10081	6919	11869
2072/73	11179	8770	12762
2073/74	12687	11659	14033

Source :Annual Report 2069-2074

Loan Loss Provision

Year/Million	ADBL	GBIME	NABIL
2069/70	127	47	101
2070/01	87	44	125
2071/72	244	55	122
2072/73	145	61	88
2073/74	177	36	72

Source :Annual Report 2069-2074

Non-Performing Loan

Year/Million	ADBL	GBIME	NABIL
2069/70	321	61	20
2070/01	340	109	24
2071/72	386	112	17
2072/73	363	115	18
2073/74	426	129	19

Source :Annual Report 2069-2074

Total Assets