CHAPTER 1
INTRODUCTION

1.1 Background of the Study

Bank is considered as the backbone in the development of the national economy. It is a financial institution, which act as a transaction of money by accepting various types of deposit, disbursing loans and rendering other financial services. So, among the various function to provide loan to the investors is the major function. Through the loan, there will be increase in the environment of the investment and the bank has the major role in creating such an environment.

Loans and advances means providing of the fund for the investors in the certain sectors taking risk in the hope of better return for the investors. Investments that take place or action done in the present and the result can be obtained in the future. So, the loan and advances are very risky assets because the result or effectiveness of it will be found at the future. Due to this, while providing loan, bank should be very careful because performing loan only can move towards the way of success and non- performing loan moves the bank towards the way of failure.

Loan and advances dominate the assets side of the bank. Similarly, earning from such loans and advances occupy the major space of the income statement of the bank. Lending can be said to be the raison d'être of the bank. However, it is very important to be reminded that most of the bank failures in the world due to the shrinkage in the value of the loan and advance. Hence loan is known as risky assets. Risk of non repayment of loan is known as credit risk or default risk. Performing loan has multiple benefits to the society while non performing loan erodes even existing capital.

Bank provides the excess amount of funds to fulfill the demand of the investors and better allocation of financial resources and to encourage economic growth in the economy. For this loan should be efficiently managed and controlled. If the loan is not efficiently managed, it can cause inflation or deflation, recession and unemployment in the economy. Misleading of loan management can lead to misallocation of the investible resources and the economic power concentrated on the certain person's and against the social objective. So, the non- performing loans not only creates the problem in the economy of the country but it can move the bank towards the liquidation.

Bank plays a vital role in the economic development of a country. In fact, in the modern industrialized and service oriented era, the availability of banks with competitive services is the measure of economic development of a country. While many people believe that banks play only a narrow role in the economy taking deposit and making loans the modern banking has had to adopt new roles in order to responsive to public needs. The principal role that a bank today play are:

The Intermediation role:

The saving received from different households and business firms from different accounts were transfer into investments in different sectors like construction, renovation, purchase of land and houses, commencement of new business and other capital assets.

The payment role:

Payment for goods and services on behalf of their customers such as by remitting money from one place to another, payment of bills(water, telephone, electricity and so on), issuing and clearing cheque, discounting the bill of exchange and dispersing currency and coins.

The Guarantor role:

To pay off the customers debt basically in international transactions when those customers are unable to pay such as by issuing letters of credit. Some of guarantees are bid bond, performance bond etc.

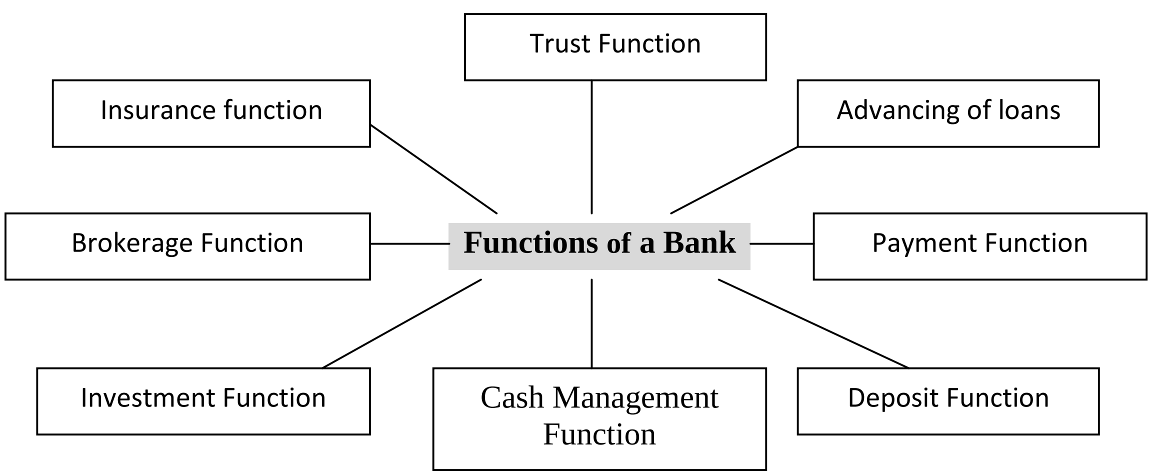
The Agency role

As the agent of customers, modern banking performs different types of functions such as periodic payments; periodic collections purchase and sell of securities, representative, trustee and so on.

The Policy Role

Serving as a conduct for government policy in attempting to regulate the growth of the economy and pursue social goal. Some of the vital functions performed by a full banking service institution today are summarized in the figure below.

Figure 1.1:Functions of a Bank



Sources: (Joshi Shyam 1998)

The evolution of banking industry had started a long time back, during ancient times. There was reference to the activities of moneychangers in the temple of Jerusalem in the New Testament. As a public enterprise, banking made its first beginning around the middle of the 12^{th} century in Italy and the bank of Venice, found in 1157 was the first public banking institution. The history of banking in Nepal starts right from the establishment of Nepal Bank Ltd. On 30^{th} Kartik 1994 B.S. before the inception of the traditional ways of banking was in existence. The operation of NBL brought out a landmark in the economic history of Nepal. The economic activities grow up gradually and the Central Bank of Nepal, Nepal Rastra Bank was instituted on 14^{th} Baisakh 2013 under NRB Act, 2012. Likewise, RBB was established on 10^{th} Magh 2022 under Banijya Bank Act, 2021. As the economic activity took a larger shape, two other financial organization, Nepal Agriculture Development Bank (2023) and Nepal Industrial Development Corporation (2016) was set up to modernize agriculture and establish various industries. Their role in the national economy is of great significance since they have been well capable of winning the approval of many people. They have sown seed of banking in Nepalese soil. Despite this soil strength, they had weakness as well. Our economic activities remind in shadow because of traditional and unscientific banking process.

There was urgency that newer banking modalities and advanced technologies to be practiced in the field of banking. Hence, Banks started to be established in Nepal. During that course, NB Bank Ltd. was established. With a short span of 11 years, banks have been established and some are willing to come to Nepal. These are the clear indications that the banking activities are tremendously increasing day by day. It is undoubtedly a good sign for the economy of our country. And on the other hand, banking is going to be more competitive in the days to come. They are efficient and effective monetary financial institutions in modern banking. Bank provides the excess amount of funds to fulfill the demand of the investors and better allocation of financial resource and to encourage economic growth in the economy. For this loan should be efficiently managed and controlled. If loan is not efficiently managed, it can cause inflation or deflation recession and unemployment in the economy. Misleading of loan management can lead to misallocation of the investible resources and the economic poor concentrated the certain persons and against the social objective.

The banks take almost care in analyzing the creditworthiness of the borrowing customer to ensure that the interest and the principal amount on loans are timely recovered without much trouble and legal process for the recovery. A sound lending policy is essential for the good performances of the bank are further to attain economic objectives directed towards acceleration of the development. Lending policy should be carefully analyzed and the banks should be careful while performing its credit creation effectively and to minimize the risk factor.

Due loan management is not satisfactory and its being a national issue and to contribute towards the topic through the study among the lot of topics, the loan management topic is selected. Thus study aims to focus on the comparative loan management of the joint venture banks namely, Everest Bank Limited and Himalayan Bank Limited.

1.2 A Brief Profile of the Banks

In the initial period capital of the both banks are shown in the table.

Table 1.2

Capital Structure of EBL and HBL

Capital	Everest Bank Limited	Himalayan Bank Limited
Authorized capital	Rs.2,00,00,00,000.00	Rs.300,00,00,000.00
Issued capital	Rs. 1,28,14,06,500.00	Rs.160,00,00,000.00
Paid-up-capital	Rs. 1,27,96,09,490.00	Rs.160,00,00,000.00
No. of share	11,19,609	160,00,000
Preference share capital	Rs. 16,00,00,000.00	-
Par value	Rs.100.00	Rs.100.00
Paid-up-value	-	Rs.100.00
Listed in Nepal stock Exchange	2052/12/25 (B.S.)	2052/09/09 (B.S.)

Source: AGM of EBL and HBL 2067/68.

1.2.1 Everest Bank Limited (EBL)

Everest Bank Limited was established under the company act 1964 in 19th November, 1993 (2049/09/03) and started banking transaction in 16th October 1994 (2051/07/01). This is the joint venture bank with Punjab national bank of India and Nepalese promoters. A team of professional departed by Punjab National Bank under the Technical Service Agreement manages it, and managing director is the executive director depute by PNB under this arrangement. Now the bank has 23 branches including main branch (i.e. head office) in Nepal. Currently, the bank is going to started new branches in different places like Chitwan, Lamjung and so on.

An authorized capital of the bank had been Rs.490 million with out 340 million preference capital issued capital of Rs.240 million and paid up capital of Rs.117.5645 million in the beginning of the year 2051/52.

It has the following share holding patterns.

i.	Punjab National Bank (India)	20%
ii.	Nepalese promoters	50%
iii.	General public	30%

Similarly, the present composition of Board of Directors (BOD) of the Bank comprise as gives below.

1	Chairman	-	Promoter	nominee
3	Director	-	Promoter	nominee
2	Director	-	PNB	nominee
2	Director	-	Elected by public shareholders	

The objectives of Everest Bank Limited are as follows:

- To play an important role in facilitating Indo-Nepal trade. This is growing with the support of large network of branches of Punjab National Bank in India.
- To provide a whole range of International Banking services o facilitate Nepal’s trade and tourism.

- To participate in the emerging industrial scenario in Nepal Punjab's age-old exposure, banking experience and expertise would come in hand.
- To provide the full range of quality banking service to both the business community and common man.

(Source: Brochure of EBL)

1.2.2 Himalayan Bank Limited(HBL)

Himalayan Bank was established in 1993 in joint venture with Habib Bank Limited of Pakistan. Despite the cut-throat competition in the Nepalese Banking sector, Himalayan Bank has been able to maintain a lead in the primary banking activities- Loans and Deposits.

Legacy of Himalayan lives on in an institution that's known throughout Nepal for its innovative approaches to merchandising and customer service. Products such as Premium Savings Account, HBL Proprietary Card and Millionaire Deposit Scheme besides services such as ATMs and Tele-banking were first introduced by HBL. Other financial institutions in the country have been following our lead by introducing similar products and services. Therefore, we stand for the innovations that we bring about in this country to help our Customers besides modernizing the banking sector. With the highest deposit base and loan portfolio amongst private sector banks and extending guarantees to correspondent banks covering exposure of other local banks under our credit standing with foreign correspondent banks, we believe we obviously lead the banking sector of Nepal. The most recent rating of HBL by Bankers' Almanac as country's number 1 Bank easily confirms our claim.

All Branches of HBL are integrated into Globus (developed by Temenos), the single Banking software where the Bank has made substantial investments. This has helped the Bank provide services like 'Any Branch Banking Facility', Internet

Banking and SMS Banking. Living up to the expectations and aspirations of the Customers and other stakeholders of being innovative, HBL very recently introduced several new products and services. Millionaire Deposit Scheme, Small Business Enterprises Loan, Pre-paid Visa Card, International Travel Quota Credit Card, Consumer Finance through Credit Card and online TOEFL, SAT, IELTS, etc. fee payment facility are some of the products and services. HBL also has a dedicated offsite 'Disaster Recovery Management System'. Looking at the number of Nepalese workers abroad and their need for formal money transfer channel; HBL has developed exclusive and proprietary online money transfer software-Himal Remit TM. By deputing our own staff with technical tie-ups with local exchange houses and banks, in the Middle East and Gulf region, HBL is the biggest inward remittance handling Bank in Nepal. All this only reflects that HBL has an outside-in rather than inside-out approach where Customers' needs and wants stand first.

An authorized capital of the bank had been Rs3000 million with, issued capital of Rs.1600 million and paid up capital of Rs.1600 million in 2067.

1	Chairman	-	Promoter
3	Director	-	Promoter
1	Director	-	Nominated from Employee Provident Fund
1	Director	-	Elected by Public Shareholders
1	1st Vice Chairman	-	
1	2nd Vice Chairman	-	Nominated by Habib Bank Ltd,Pakistan

1.3 Statement of the Problem

Loan management is the essence of commercial banking; consequently the formulation and implementation of second lending policies are among the most important responsibilities of directors and management. Well conceived lending policies and careful lending practices are essential if a bank is to perform its credit. Loan management effects on the company's profitability and liquidity so it is one of the crucial decisions for the commercial banks.

The need of financial resources in a developing country like Nepal is essential for the economic development of country. All the sectors from industrial and commercial to agriculture and infrastructure are in need of finding. Although the growth of industrial loans has not been encouraging in the recent years, there is sizable growth in the commercial and other short-term credits. Commercial banks are focusing loans on consumer loans like housing, vehicle, education loan etc. It is encouraging to explore new sector for loan management but it should also be considered that industrial loan should be gives prime importance as the economy largely depends on this sector.

Lending policies are not systematic and no clear cut vision of policy is available on lending aspect. In Nepal it has been found that on approval and lending decisions are made flexible to favour to personnel networks also. A new customer finds that loan providing process being very complicated and sometimes the documents submitted for loan sanctioning being fraudulent and for formality purpose only.

In this perspective following are some notes problematic aspect of the study.

i. How effectively is the lending policy of selected sample bank is being followed?

ii. Whether the trend of the deposit and loans of the commercial banks are satisfactory.
iii. How the bank measures the liquidity position and impact of deposit on liquidity?
iv. What is the portion of lending between consumer and industrial loan?
v. How the bank measures the lending performance in efficiency, and contribution of profitability.

1.4 Objective of the Study

The main objective of the study is to analyze the loan management adopted by EBL & HBL. The specific objectives can be set as follows:

i. To analyze the effectiveness of lending practices of EBL & HBL.
ii. To measure the performance in quality, efficiency and contribution of profitability.
iii. To examine the trend of deposit and loans of the banks.
iv. To study the liquidity position, the impact of deposit on liquidity and its effect on lending performance.
v. To provide suggestions and recommending to improve the loan management on the basis of findings of the study.

1.5 Significance and Focus of the Study

There are few research done in loan management of commercial banks. Loan management is one of most important aspect of a bank. The study on analysis of loan management of the chosen selected banks would be beneficial to the shareholders, banking professional, investors, teachers and students of banking management.

Commercial banks accept the deposit from the public and provide the necessary amount fro the investors as of their demand from which the bank earn the profit. But in concern the Nepalese commercial banks the lending policy is not effective and the portion of the huge amount of the non performing loan creates not risk towards the banks but also in the national economy's. The success of the any bank determines by the earning of the profit and the increase in the non performing loans reduces in the profit portion of the bank. Higher non- performing loans not only effect in the profit of the banks but also effect in the collection of deposit and image of the banks and finally, turns towards the liquidation of the bank. The previous study showed that the public banks have portion of the non performing loans around 62 percent with N B L and 52 percent RBB of the total loans. Due to the critical situation the foreign management was introduce in hope of recovering non performing loans.

In order to face with non performing loans the NRB made a loan loss provision as type of loans and the bank have to provision the loan loss according to the N R B direction. The study try the know the loan situation of selecting bank and maintaining loan loss provision as of NRB directives which effect in collection of the deposit and in the expectation of the stakeholders.

This study focuses in the qualitative measurement of the selected bank. Similarly, the finding of the study will equally important to other who is interested in knowing about this particular bank. Last but not least, it will provide relevant and pertinent literature for future research on the area of loan management of banks.

1.6 Limitation of the Study

Since, the study is focusing to fulfill the partial requirement course of M.B.S. of T.U. It will have some limitation. We have limited resources and it may be difficult to explore researcher to find out new aspect. Reliability of statistical tools used and lack of research experience are the major limitation and some other limitations can be enlisted as follows:

i. This research is limited to the lending aspect mainly with the loan and advances only.
ii. The secondary data are used to analyze for result interpretations, so the accuracy of the finding depends on the reliability of available information.
iii. In some extent, the data published on the website of related banks will be taken.
iv. Due to time and resource factor only two commercial banks are taken for the study.
v. The study covers the time period of 2005/06 to 2009/10 years of data will be taken into account due to time and cost constraint.

There could be many factors affecting loan management decision. However only those factors related with lending policy will be considered in this study.

1.7 Organization of the study

This study has been organized into five chapters, each devoted to some aspects of loan management of joint venture commercial bank. The titles of each chapter are summarized and the contents of each of these chapters of this study are briefly mentioned here:

First chapter i.e. introduction chapter discloses with the general background of the study, a brief profile of the banks, focus of the study, statement of the problem, objective of the study, significance and focus of study, limitations of the study and organization of the study. The second chapter is mainly focused with literature review that includes a discussion on the conceptual framework on loan management and review of major-studies relating with leading decision. Also some related articles in journals, newspaper, bulletins, are reviewed. The third chapter describes the research methodology used to conduct the present research. It deals with research design, sources of data, data processing procedures, population and sample, period of the study, method of analysis and financial and statistical tools. The fourth chapter is concerned with analytical framework. It includes the analysis of financial indicators, analysis of financial indicators, analysis of mean, correlation coefficient, regression analysis, trend analysis and financial analysis and the major findings. The fifth chapter includes conclusion of the study which deals about the main theme of study and comparison of lending policy of the banks with recommended for improvement of loan management of the selected banks. The bibliography and annexes are also incorporated at the end of the study.

CHAPTER 2
REVIEW OF LITERATURE

The main purpose of this chapter is to review the available literature on loan management of financial institutions. Thus authentic and honest attempt are being made to highlight the gist relating with the concerned topic from various book newspaper magazines research articles as well as past thesis. To ensure the précised lucid and concrete views about the state topic, the entire review work is portrayed in the point wise breakdown as given below.

2.1 Conceptual Review:

It encompasses the review of textbooks and other reference materials such as newspapers, magazines, research articles and journals besides past thesis.

2.1.1 Review of Books:

A bank is a government regulated, profit making business that operates in competition with other banks and financial institutions to serve the saving and credit needs of its customers. The primary business of banks is accepting deposit and leading money. Banks accepts deposit for customers who want the safety and convenience of deposit service and the opportunity to earn interest on their excess funds.

Bhattacharya in his book “banking strategy, credit appraisal and lending. Decision has put the recommendation of Tandon committee from the report submitted this committee. Has prepared this report in 1975; however these recommendation stills deserve great significance in the sector of credit appraisal, the system proposed by the committee enjoyed upon the system proposed by the committee enjoying upon the banker.

a. To assess the need based credit of the borrower on a rational basis.

b. To ensure proper and use of bank credit by keeping a closer watch on the borrower business and thus ensure safety of the banks funds.

c. To improve the financial discipline of the borrower and

d. To develop healthy banker borrower relationship

The committee examined the existing system of lending and recommended the following broad changes in lending system.

a) The credit needs of borrowers are assessed on the basis of their business plans.

b) Bank credit only be supplementary to the borrowers resources and not in replacement of them, i.e. banks not to finance one hundred percent of borrowers, requirement,

c) Borrowers be required to old inventory and receivables according to norms prescribed by the reserve bank of India from time to time.

d) Credit be made available in different components only, depending upon the nature of holding of various current's assets.

e) In order to facilitate a close watch on the operations of borrowers, they are required to summit, at regular intervals, data regarding their business and financial operations, both for the past and future period.

The committee including stores and other items uses in the manufacturing process.

a) Raw material including stores and other items uses in the manufacturing process.

b) Stock in process

c) Finished goods

d) Receivable

e) Spares (Bhattacharya, 1998: 309)

“Bank growth and profitability are the result of carefully forecasting funding needs, competitively attracting funds, efficiently borrowing funds and effectively investing, funds in safe but profitable earning assets. Depending on a bank’s size and location and on local and national economic conditions, a bank may have adequate, relatively stable sources of low cost funds, or it may have to compete regularly and aggressively for funds at high market prices for an increasing number of banks, the second situation is becoming the norm as more, the second situation is becoming the norm as more and more banks face increasing pressure to attract adequate funds at reasonable costs.

In the word of Singh and Singh, 1983 “credit policies of banks are condition to great extent by the national policy framework, every banker has to apply his own judgment for arriving at a credit decision, keeping of course, bankers and credit policy also in mind” (Singh and Singh, 1983).

Shrestha,2000 said that the commercial banks should not concentrated on the specific sector but should fulfill the credit need of various sector of the economy including agriculture, industry, commercial and social sector of the economy service sector. The commercial banks should very effective while providing loans. While providing loans, the banks should think on the maximizing the economic growth of the country as well as the profit from providing the loan for the operation of the country. (Shrestha, 2000)

Financial institutions occupy the paramount role in development of the country. These institutions not only mobilize saving but also promote investments in the different enterprises of the national economy that spontaneously assist alleviating poverty, uplifting employment opportunities and there by developing the society and country as whole. Thus, the development of financial institution commercial banks, Finance Company, Insurance Company) is regarded as one of the crucial yardstick for measuring the level of economic development of a nation. Nepal the one of the poorest countries in the world is in need of additional capital investment to propel the rate of economic growth. Domestic and foreign capital i.e. grants and loans) are two major chunks of capital available for investment and earlier is crux and stable source of capital to gear sustainable development of nation.

Likewise, in another book the concerned matters are being presented as: Loan administration involves the creation and management of risk assets. The process of lending takes into consideration of the people and system required for the evaluation and approval of loan requests, negotiation of terms; documentation, disbursement, administration of outstanding loans and workout, knowledge of the process and awareness of its strength and weaknesses are important in setting objective and goals for lending activities and for allocating available funds to various lending functions such as commercial, installment and mortgage portfolios. (N.P Subedi).

Let's bifurcate the term 'Loan Management into the two separate terms: Loan and management in order to deliver the meaningful sense about the topic. Oxford Advanced Learners' Dictionary dubbed the term Loan as "A thing that is lent, especially a sum of money". (Oxford Learner's Dictionary, 1997). Similarly, the term management is defined as "The control and making decisions in a business or similar organization: and -further says "the process of dealing with or controlling people or thing." (Oxford Learners Dictionary, 1997).

Activities of other Banking Institutions (OBIS) include activities of deposit taking financial institutions other than commercial banks viz. Development Banks, Rural Development Banks, Finance Companies- financial Cooperatives (FINCOOPS) and Financial Non-government organizations (FNGOS). Similarly, Non-Bank financial Institutions include all other financial institutions not directly involved in the financial system in mobilizing financial resources collected in different forms. (Economic Report, NRB: 2000/O1)

Yet another dubbed as: Loan and advances dominate the asset side of the 'Balance sheet' of any bank. Similarly earnings from such loans and advance-5 occupy a major space in income statement of the bank. Lending can be said to be the raison of bank. However, 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 nonpayment of loan is known as credit risk or default risk.

Book named "Banking Management" says that in Banking sector or transaction, an inviolableness of Loan management's methodology (working‘ method) 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. (Bhandari, 2003: 170).

After restoration of democracy, the government adopted liberal, independent and market oriented policy. It has changed role of control.' oriented into promote oriented and as consequences a series of fundamental reform in fiscal, monetary, industrial, commercial and labor policy have been done to create a captivating environment for investment and these efforts provided impetus for the incorporation of a lot of 'Joint-venture Banks' including 'Finance companies' since then. "At present the varieties of license 'Finance companies' have been reached up to 57." (NRB, Mid-July 2004:Vol.5).

As inference from all these above stated authors it can be said that Loan management refers to systematic identification of needy one or required party

(Loan taker), verifying their documents, pre and post site visit, disbursement of loan keeping collateral as cushion for giver and post-disbursement inspection cum sound recovery of granted loan as far as practicable.

2.1.1.1 Loan [Definition]

Webster's Dictionary define loan as: "Something lent; esp. a sum of money lent, often for a specified period and repayable with interest" (Michael Agnes, 2000:821). Financial institutions lend money out of deposits, they have received. They must increase money by advancing loan since them to pay interest on deposits. It is apt to provoke: Deposits are children of loans and loans are the children of deposits.

Banks do not keep cent percent reserve against deposit for meeting the demands of depositors. As all depositors do not need money at the same time, banks with a Small reserve satisfy their demand whenever and wherever demonstrated and grant loan from excess reserve than depositors 'need to needy feasible subscriber. Loan is financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for an obligation repay on specified date or demand. Loan usually comprises.

i. Consumer installment, overdraft and credit card loan.

ii. Residential mortgages.

iii. Non-personal loans, such as commercial loans to business, financial institution, government and their agencies.

iv. Direct finance leasing.

v. Other financial arrangement that are in substance loans

As gist it is apt to quote, "Performing loans have multiple benefits to the society while non-performing loan erodes even existing capital." (Dahal et. al., 2002: 114.)

2.1.1.2 Types of Loan:

Types of loan are also know as disbursement procedures and falls under lending conditions and disbursement procedures. Johnson & Johnson et. al. has depicted the types of loan as:

i) Commercial loan

ii) Consumer loan

iii) Mortgage loan

Whereas KAFAL provides the following varieties of loan:

i) Term loan

ii) Housing loan (Real estate loan)

iii) Miscellaneous loan (fixed deposit receipts and provident fund loans)

iv) Bridge Loan

v) Hire purchase loan

vi) Share loan.

As there is no uniform standard among intellectual and organization for classifying loan sincere and authentic effort is being made for categorizing and dealing about loan.

i. Term loan

It refers to money lent in lump sum to the borrowers: It is principal forms of medium term debt financing having maturities of 1 to 8 years. It term loans are usually repaid in level amounts, over the period of the loan, either a large final 'Balloon payment' or just a single 'Bullet payment' at maturity. Banks can accommodate repayment patterns to the anticipated cash flows of the borrowing firms. The rate of interest on it is sometimes fixed not only for the life of loan but also as per prime rate. The conditions of a term loan are likely those of most unsecured bonds.

Barely, Richard and Steward Myers urge that the banks loans with maturities exceeding 1 year are called term loans. The firm agrees to pay interest based on the bank's prime rate and to repay principal in the regular installments. Special patterns of principal payments over time can be negotiated to meet the firm's special needs. (Brealey 1996:80). It is made to support equipment purchases and more permanent funding needs. In recent timid loans occupy the apex past of the banks loan portfolio: but traditionally short-term loan were emphasized.

ii. Overdraft

Overdraft connotes the excess amount withdrawn over their deposits. The situation of overdraft evolves when bank honors the cheques to an agreed limit. It is a kind of working` capital (i.e. fulfillment of short-term needs of businessmen) loan and allowed only in current account. Hence, it is an agreement by which the bank allows the customer to draw over and above the current account balance. The account balance fluctuates frequently since withdrawn and repayment of money took place. Interest on overdraft is charged on debit balance on daily basis.

iii. Cash credit

It is the commonest form of lending done by the firm, (Bank). The loan is not given directly in cash but deposit account is being opened on the name of loan taker and tine amount credited to that account. In this wav, every bank loan creates deposit. It may be operated within the stipulated limit and required time by the borrower. It is provided against the pledge or hypothecation of stock in trade, land building, goods and machinery.

iv. Working Capital Loan

Working capital denotes the difference between current Assets and current liabilities. It is granted to the customers to meet their working capital gap for supporting production process. A natural process develops wherein funds moving through the cycle are generated to repay a working capital loan. Working capital can be categorized into fixed (permanent) working capital and variable (Temporary) working capital. Short term loan meets the fixed working capital needs where as overdraft fulfils the variable working capital demands.

v. Loan against Fixed Deposit Receipts

The depositors keep fixed deposits for a specified period. The depositor can let loan against the collateral of such deposits if he needs money before the maturity date. In general financial institutions allow up 90% of the fixed deposits as leans. "Loan up to 90% of the FDR face value can be taken against pledge of original FDR for a period not exceeding FDR maturity" (KAFAL'S Loan Policy 2060) is written in KAFL's loan policy.

vi. Project Loan

Project loan is granted to the customers as per project viability. The borrowers have to invest certain proportion to the project from their equity and the rest will be financed as project loan. The so-called "Debt-Equity Ratio" of the project is 60:40.

"Construction loans are short-term loans made to developers for the purpose of completing proposed projects. Maturities on construction loans range from 12 months 'to as long as 4 to 5 years, depending on the size of the specific project". The basic guiding principle involved in disbursement policy is to advance funds corresponding to the completion stage of the project.

Hence, what percent of the loan will be disbursed at which stage of completion must he spelled in disbursement policy. Term loan and working- capital loan needed for project fall under it.

vii. Priority or Deprived Sector Loan

Commercial Banks are required to extend advances to the priority and deprived sector.l2% of the total loan must be flown towards priority sector including deprived sector. Rs. 2 million for agriculture cum service sector and Rs. 2.5 million for single borrowers are limit sanctioned to priority sector. Institutional support to 'Agriculture Development bank' and 'Rural Development Bank' are also considered under this category. Deprived sector lending includes.

- Advance to poor/downtrodden/weak/deprived people up to Rs. 330.000.00 in generating income or employment.

- Institutional credit to 'Rural Development Bank'.

- Loan to NGOs those are permitted to carry out banking transaction for lending up to Rs. 30000.

xi. Consortium Loan

No single financial institution grant loan to the project due to single borrower limit or other reason and two or more such institutions may consent to Loan credit facility to the project among them. Financiers have equal (or likely) charge on the projects' assets.

xii. Bill purchase and Discount

Purchasing of bill of exchange of customers to which favor limit is prescribed, is known as purchasing of bills. Such bills may be either documentary bills of which contains documents of little to the goods (like airway receipt, airway bill, bill of landing, truck receipts) or clean bills of which do not have any documents concerning with title of goods. Indeed, it is form of advance granted by discounting the bill keeping the bill as security. The holders of bill of exchange can come to

This is why, it is urged that a good bank manager knows the difference between a bill and mortgage. The banks also purchase cheques of approved customers. It is deemed as being liquid investment as it posse's certainly to get back fund invested on it as maturity over.

xiii. Single Payment Loan

Occasionally retail customers need to borrow larger amounts of funds for a short term and then repaid in a single payment. As it is a special purpose loan, it requires special handling than typical retail loan. Commercial loan department processes this type of loan many banks.

The differentiating features of it are that the funds are needed for a short period of time and a source of funds will be available to retire the loan. Loan made against the certificates of deposit is its example. It is usually not a major component of a bank's consumer loan portfolio.

xiv. Credit cards and Revolving Lines of Credit

Banks are increasingly utilizing charge cards and revolving lines of credit to make unsecured consumer loan. Revolving line lowers the cost of making loan since operating and processing cost art reduced. Due to standardization, centralized department processes revolving credits resulting reduction on administrative cost. Continued borrowing arrangement enhances cost advantages. "Once the credit line is established, the customer can borrow and repay according to his needs and the bank can provide the fund to the customer at lower cost."

Charge cards and credit lines tied to demand deposit accounts are the two most common revolving credit agreements. It can be further divided into credit cards, automatic overdraft lines and large credit lines.

xv. Off-Balance Sheet Transaction

In fact, banks guarantee and letter of credit to 'off balance sheet' transactions of financial institution. It is also known as contingent' liability. Contingent liability pinpoints the liability, which may or may not arise during the happening of certain event. Footnotes are kept as reference to them instead of recording in the books of accounts.

It is non-funded based remunerative facilities but more risky than the funded until adequate collateral are taken. Lets its two varieties be described separately.

Bank Guarantee:

It is used for the sake of the customers in favor of the other party [j] (beneficiary) up to the approved limit. Generally a certain percent amount is taken as margin from the customer and the customer's margin account is credited

Letter of credit (L/C)

It is issued on behalf of the customers (buyer/importer) in favor of the exporter (seller) for the import of goods and services stating to pay certain sum of money on the submission of certain documents complying the stipulated terms and conditions as per the agreement of L/C.

It is also known as importers letter of credit since the bank of importer opens it. However, the same import L/C is known as exporter L C to exporter's bank and exporter himself. This clarifies the fact that exporters and importer do not open separate L/C for the trade of same commodities.

2.1.1.3 Objectives of the sound Loan (Credit) Policy

The purposes of a written loan policy are (i) to; assure compliance by lending personnel with the bank's policies and objectives regarding the portfolio of loans and (ii) to provide personnel with a framework of standards within which they can operates.

Senior loan administrator getting supports from subordinates and associates should write loan policy. For establishing this policy, it is necessary to get approval about this from board of directors after discussion. Performing loans extend multiple benefits to the society where as non-performing loan (i.e. given to unviable project) erodes even existing scare capital.

i. To have performing Assets:

Performing assets repays principal and interest to the bank from its generated cash flow. The objective of sound loan policy is to keep financial health of the bank meeting interest of depositors and shareholder as well.

ii. To contribute economic development

Sound loan policy says that loans are granted to productive sector (or viable project) of which provides multiple benefit to the society such as: direct and indirect employment generation, capital creation, tax paid to the government and uplift of living standard.

iii. To provide Guidance to Lending officials

There, should be not discrimination while dealing with -borrower by one officer of another and one branch or another. Individual loan officers make inconsistent judgment from each other and also with organizational goal in the absence of credit Policy.

iv. To set a Yardstick for Control:

Periodic follow-up is essential for proper implementation of any credit policy. A sound credit policy aids in identifying the deviation between actual and standard performance along with corrective actions to be taken.

2.1.1.4 Criteria for Providing Loan

Set-up of well established criteria for disbursing advances and loan is the most essential to survive, thrive and enlargement of the banks. Loan should not be allowed to all demanding parties haphazardly. Actions and inactions taken in haunch to flow loan and advances without systematic, scientific and through study cum analysis may lead to ditch. Ergo, well defined and setup criteria to grant loan must be Visible to the personnel. These are positively demonstrated below:

i. Personal Character

Intensive analysis of loan demander is essential to determine loan disbursement policy. Persons' character must be studied to know the intention to pay the loan. Their practice to repay loan, creditworthiness, habit to use acquired fund, past trend regarding the receipt and payment of loan are to be reviewed. Dubious person's proposal should not be accepted.

ii. Capacity or Competency

Whether the person is capable in making contract according to 'Contract Act, 2056' or not should be checked out at first. Considering the potent and expertise of persons (borrowers) in concerned field, decision about the flow of loan is to be taken.

iii. Capital

Examination of loan demander is apt to match his demand with his status-quo and business. This ultimately helps to know the amount of money he needs as investment. Indeed, his financial feasibility should be stronger than his demand to get the faith of the lenders.

iv. Security

Priority should be given to readily marketable and handy collateral. Decision about the flow of loan is made considering nature of business and types of securities; proposed. Accept loans having securities above and near about and denies the loan proposal containing inferior quality security.

v. Credit Information:

It is appropriate to get the information relating with loan proponent from the persons or businessmen working together in the concerned sectors. Credit information denotes knowing whether he is black listed or not, his capacity and his demand etc. If information obtained is satisfactory, the proposal will be accepted and will be rejected in reverse plight.

vi. External Environment

External environment of industry of business shown by loan proponent needs to be evaluated on the eve of providing loan to know the facts about use and salability of right business. It is pivotal to evaluate external environment of business where business origins, thrives and survives since modification of external environment is almost impossible in accordance with own motto and plight. This aids in understanding forth coming prospects and retrospect's of business as well as gives guidance for decision making.

2.1.1.5 Loan Approval Process

Disbursement procedures work after the operation of loan approval process under lending conditions and disbursement procedures.

Loan approving authority approves loan only after being convinced that the loan will be recovered along with interest. There may not be the same procedure for all kinds of loan. The process of accepting loan to industry or merchant differs with each other. Similarly, the approving process of loan concerning to primary sector and bigger project is also not similar. Approval of wrong loan proposal on haunch the makes lending institution death-knell. It entails the following sequences.

i. **Application:**

Every loan process gets momentum after submission of loan request. It encompasses project proposal, historical financial statements and documents about incorporation cum legal existence.

ii. **Conducting the Interview**

Loan officer may conduct oral interview with the applicant to gauge authenticity at the bank premise. It should be done in a friendly and positive manner. Here is the threat that interviewer may be extremely negative due to risk of undesirable loan. It clarifies about:

- **Loan purpose**: **-** Uniformity between the need of borrower and lender.
- **Repayment source**: **-** Every loan posses primary as well as secondary repayment source. Hence, repayment plan should be realistic.
- **History of business**: **-** Past and present of firm in regard to management, principal and their age, experiences as well as product and service position along with heightened competition.
- **Banking relationship**: **-** Accounts kept in different banks and loan taken from them and reason to change financial institution is to be mentioned. Lastly separate credit file is to be allotted for each applicant though loan is not allowed. This facilitates the possibility of future business with the applicant.

iii. **Credit Analysis:**

"Analyzing a credit request includes analysis of the character, capacity and capital position of the potential borrower and evaluation of those features in terms of the current economy and the economic conditions predicted over the loan period." (Johnson et al., 1940:174). He further says the basic questions the loan officer attempts to answer in the credit analysis include:

- What is the character and managerial ability of the borrower?
- What is the borrower's capacity to repay the loan as requested?
- What is the capital position of the borrower in case the borrower experiences difficulties?
- How will current and predicted economic conditions affect the ability of the borrower to repay the loan?

Johnson and Johnson have presented 'Credit Analysis' 'under the following eight steps:

- Acquiring basic information about the borrowers.
- Acquiring basic information about loans.
- Making preliminary review of risk.
- Acquiring more complete information.
- Varying the critical information.
- Making a refined analysis of the risk.
- Making an overall decision.
- Structuring the loan.

Following paces are formed in evaluating loan application:

Historical Analysis

It denotes ex-post analysis. It deals about past financial statement and business risk, which is quantitative analysis by nature. Further, it depicts the financial performance of management and business risk analysis supports to measure such as: supply, demand, production, collection etc. realized in the past and how management settled them. It discloses the borrower's likely success or failure in repaying the debt in future.

Financial institutions have practiced analysis of **5C'**s of credit.

Character

It covers borrowers' personal traits like norms values, ethic and honesty by which lending decisions get shape. Character is composition of fact full answers to queries, reliable purpose, responsibility and sincerity to repay loan on time on the assumption of lending officials. Only good rated borrower gets priority from lending officials.

Capacity

Capacity represents two-folded sense. One tells about the legal capacity to borrow money where as another pinpoint ability to generate ample income to repay loan or through liquidation of assets. The first sense observes the borrowers legal power to borrow money but second sense gives preference to assess quality of management not character. Deferent ratios are to be examined for so.

Conditions:

It indicates the general economic condition beyond the control ' of the borrower which affects the borrower's business. Condition refers to security, political and other social condition that requires for creating conducive of business. Loan is granted to only those whose general condition look favorable.

Collateral

If borrower can repay loan from cash flow generated from operating activities, loan is given to him. Bank wants certainty about the payment of loan even in default case. Land' building, machinery, working capital like account receivable and inventories can be fixed as collateral.

Capital

Capital represents borrower's net worth. This falls under leverage ratio. Leverage ratio will be high if the borrower has high capital. If leverage ratio is acceptable, bank gives loan

iv. Forecast and Risk Rating System

The analyst has to forecast impending major risk based on the finding of historical analysis on the present considering the present and foreseeable environment. The analyst has to disclose the extent to which inherent risks will be mitigated and how unmitigated risk can be covered. Credit Analysis tells about:

- Releasable loan and non-releasable loan.
- Ranking of the released loans from the standpoint of risky ness (low to high risk)

Aforesaid clues determine the rate of interest to be charged and value of securities to be obtained. Two types rating system have been evolved for forecasting and rating risk.

Objective Type Loan Rating System

It quantifies certain financial statement statistics, collateral, documentation and financial statement quality. Financial statement quality refers to the bank's confidence in the level of the statements provided by the customer such as certified financial statements with unqualified or qualified opinions. Depending on the numerical values of each category, a composite numerical rating is derived for classifying each loan. Under it, numerical values or weights on each item of information considered vital in judging the risk of a potential loan. Each vital factor: Liquidity, leverage, management ability, collateral etc is allotted a value from 1 to 5, with 1 being best and 5 being worst.

Subjective Type Loan Rating-System

It relies on the judgment of the loan reviewer to place a loan in one of a several defined classes without allotting numerical values to specific data such as financial statement ratios. The classification within it may differentiate examiner-classified loans and loans classified on the basis of internal loan-review evaluations. The internal review evaluations may include classes for loans that correspond to examiner classes but mostly internal-review classes are assigned to loans that probably be classified by the examiner in next review:

Return

Income received on investment plus any change in market price, usually expressed . as a percent of the beginning market price of the investment. Total return (i.e. interest, fee and commission) should be calculated through analysis and compare either it meets bank's standard or not.

vi. Liquidation

The bank may decide to bring liquidation in order to satisfy creditors if the possibility of the borrower's long-range survival is minimal. This is mostly persisting by the borrowers. Once the liquidation decision is taken and then a plan of action that includes the method of liquidation and settlement of debt obligation should be adopted.

Sale of the company as a going concern and either a bulk sale of certain assets or' piecemeal distribution liquidations may be adopted. Bank gains control of the assets to ensure the use proceeds in retiring debt. Additional security is to be asked if inadequate security reveals on liquidation analysis.

vii. Creditworthiness and Debt Structure

Structuring of debt facility to be released is essential if the analysts find the credit worthiness of borrower and determines to grant loan.

viii. Preparation of Credit Report

Prepare the structured credit report containing the loan approval process in a precise order. It entails the answers to the vital questions during initial interview as well as consequences of checking various sources of credit information and the results of financial statement analysis. Sometimes a one layer higher than analyst may be approving authority but ultimately works as this authority.

Approving authority decides the approval (rejection) decision of loan facility after analyzing the contents of appraisal form. In this way, loan approval process comes to an end. Some writers have divided the entire process into five points as:

- Evaluation of Loan Proposal
- The Types of Loan
- Determination of Necessary Documentation Loan Acceptance Charge

2.1.1.6 Pricing of Loan

Pricing commercial loan is a vague process that needs estimating the return the bank should earn on a particular loan and then forming a loan agreement that will generate the desired return.

The yield on loan covers not only the interest rated charged for borrowed funds but also the charges a bank makes for commitments and compensating balance. It certain cases, service fee income also fall under total return.

The interest rates can either be fixed or variable (floating) rate terms to check elevation in the general level of interest that increases bank's cost of fund. Loan will be made on fixed rate if there is no possibility of rises in interest rate. Major pricing terms are:

a. Fixed Rate

Fixed interest rate is agreed at organization until maturity if there is no chance of incline in rate of interest.

b. Variable Rate

Depending on the base rate varying interest rate is installed. It is classified as:

- Prime base: Highest graded customer obtains it.
- Prime plus: Prime rate plus a fixed percentage is charged under it.
- Prime times: Under it the rate will mount (or dismount) by the multiple and prime rate time a fixed multiple.
- Other base rate: Beside the base, it is identical to prime rate.
- Caps and floor: The highest and lowest limit up to which loan can be released on variable rates are caps and floors respectively.

iii. Commitment Fees

It is levied by bank to customer for agreement to availed fund. It is charged on used and unused & portion of a credit line.

iv. Compensating Balances

It is deposit balance to be k%-,-t as per the deed of lender until the over of loan period. It is to be kept on average rather than at a strict minimum.

2.1.1.7 Structuring the Loan

"Structuring the loan is not separate from 'Credit Analysis'- it is the final stage of the overall analysis. The loan officer uses the information gained in the credit analysis to construct to make it a bank-able".Credit Analysis discloses the element of risk, needed fund for applicant and likely timing of borrowing. Lending officer puts above stated with loan proposal and this helps in deciding the types of loan complying with applicant and banker's needs as well. Repayment schedule and protective covenant need to be prepared.

i. Loan Agreement and Protective Covenants

"Once the decision has been made on whether the loan is to be secured of unsecured, the next steps in the construction of a loan agreement. A written loan agreement details all of the expectations of the bank concerning performance on the loan. Loan agreement comprises the followings:

- Description of the loan
- Representative and warranties by borrowers
- Protective covenants
- Condition of lending
- Remedies

Protective covenants are pivot factor of loan agreement officer sets conditions to protect bank against potential loan losses or risk. The covenants must be realistic and should be designed to meet the elements of the loan.

ii. Loan Participation

"Participation involves two or more banks jointly providing to a single borrower" (Ibid: 183). It is used since it reduces risk. Bank meets excess than lending limit to fulfill the customer's request. Loan participation can either be upstream or down stream. Loan originates in a large bank and small bank gives fund for a portion of the loan under"Down stream participation a small bank creates the loan and sells a portion of the loan to the large bank in 'upstream participation'. Participation in loans requires analysis of i.e. loan and analysis of the originating bank. The lead banks philosophy, lending record and overall performance must be evaluated to determine the risk of participation.

It creates special management problem though it provides opportunity funds profitably reducing risk through diversification. Care of the lead bank is necessary to limit risks.

2.1.1.8 Management and Control of Potential Loan Losses

A poorly administered loan portfolio germinates negative outcomes on earning and capital. Hence, control of loan losses is a crucial task of a bank. Greater provision for loan losses in the 'income statement' is essential to coup the larger loan losses than anticipated situation. It comprises:

i. Loan Review

Its main aim is to appraise the value of loan. It can be carried out as internally and externally (i.e. regulatory agencies). The quality and liquidity of each loan is being evaluated herein after studying about collaterals and credit files. The examiner grades loan as substandard, doubtful, loss or other specially mentioned loans.It further goes as pre loan review, past loan review and exception review. It should be submitted to the board of directors or senior loan manager.

ii. Identifying Problem Loan

Early traces out of a problem loan increase the possibility of recovery' of loan. But with the passes of time such type of hope ceases. Loan officer should be aware about the signs of existed or forth coming problem concerning to loan concerning to loan. These signs are:

- Customer's failure to provide current financial statement as per Loss of borrower rapport (agreement) A recession economy
- Miscellaneous:
- Illness or death of a principal
- Marital problem of a principal especially divorce
- Irresponsible behavior of a principal
- Unexpected loan renewal Overdraft
- Strike or hostile relating with labor

iii. Handling Problem Loan

Once problem loans are identified, search the causes of the customers' difficulties. Wait and see rule operates if customers are co-operative. Otherwise, more aggressive actions should be taken. This may involve ceiling the loan which results either rehabilitation or liquidation of the company. - Rehabilitation:

It converts the weak company into the strong company with loan performance. The bank has to hire management expert or consultant if it likes to provide loan to sound customer properly as possible. It can be done as:

- Eliminate or reduce every possible expense.
- Reduce inventory and review account receivable.
- Dispose of idle or unessential equipment or plant.
- Analyze debt structure and manage cash flow to service debt.
- Seek additional equity capital.
- Prune unprofitable operating division.

Liquidation

Bank orders liquidation to satisfy creditors viewing the minimal possibility of long term survival of the borrower. Most of the borrowers extremely resist it. It includes method of liquidation and settlement of debt obligations.

2.1.2 Loan Administration

Loan administration refers to planning, organizing, and controlling of lending activities. Here, planning denotes consideration of risk and return to meet profit object along with division of loan assets among consumer Commercial and mortgage. Organization refers to putting goals and objectives into action through definition and processes with support functions. Controlling entails making and monitoring loan as per deadlines supported by corrective actions to be taken in granting loans if necessary.

Loan department carries out all acts relating to loan from initial stage if providing loan to the loan recovery stage. It does such work getting supports from other departments. Excess flow of loan than demand of needy party results failure to the bank. It pertinent two parts:

i. The Management for Providing Loan: (Disbursement Management)

The following are inevitable for loan:

a. Proposal for Loan

Printed loan proposal stating essential things should be kept ready and any in coming old or new customer should be given it. Necessary thing in it are: name, occupation, address, kind of loan, amount of loan and securities. After filling aforesaid, it should be given to loan department where it' is to be reviewed carefully to know correctness.

b. Deed of the Loan

Loan department prepares it and includes name, address of the loan taker and year of loan taken, quality of loan, interest rate, loan recovery, date and date of loan agreement (deed) etc. Such deed has to be registered from related office.

c. Securities

It is dealt in 1.1.4 under element to be dealt in loan policy. Any reliable securities such as movable or immovable should be kept as security to provide cushion for loan besides cash generated.

d. Granting Loan Based on Guarantee

Bank grants loan taking movable or immovable properties of third person if the debtor's security is less than needed or unacceptable or do not meet bank's limit. But all legal process related to it should be fulfilled

e. Commitment Deed

After approval of proponent's proposal, loan department prepares separate commitment deed to be signed by the debtor. It portrays loan condition and the rules of bank abiding the borrowers. '

f. Contract of Indemnity

Contract deed of indemnity needs to be prepared by the game department. The loan proponent signs in it and puts his thumbs over it. Such contract abides the debtor to pay debt and any breach of rule makes him liable for payment to bank.

j. Invoice

The debtor must submit all bills, vouchers, and documents relating to business on time as per demand of the bank.

ii. The Management for Loan Recovery (Recovery Management)

Bank desires the proper utilization of loan by the debtors. Indeed, recovery of loan denotes sequences lay down to get back loan amount with all due interest including remedial and punitive actions to be taken if necessary.

Audit of Credit

Credit audit refers to keeping eyes on the granted loan to decide how properly this is utilized. It is done until the loan is recovered. It is done until the loan is recovered. It is done from time to time to know plight of debtor, proper use of the loan and profit-loss position. It comprises:

- Verification of loan documents
- Field visit
- Forms of credit to be prepared
- It may be of different forms such as:
- Internal credit audit
- External credit audit
- Credit audit by control bank

a. Recovery of Interest on Loan

The borrower should pay interest and principal on time as per the deed of the loan and time assigned by the bank. Otherwise, bank adds interest according to rule of bank. It charges the interest on interest if borrower does not pay the interest and loan in fixed time.

b. Loan Recovery Process

Bank recovers the granted loan as per the terms arid conditions stated deed of the loan. Loan should be repaid either on installment basis or lump-sum basis as per the deed of loan. Loan recovery period can be extended making new agreement if borrower's situation goes beyond his control.

c. Handover of Securities

Bank needs to return movable or immovable properties taken as securities from borrower or security received from third persons as guarantee.

d. Process of Recovering - Date-expired Loan

The bank recovers principal and interest of not recovered loan as per Commercial Bank Act 2031 (1934). After recovering the loan accordingly the remaining cash from sale ' of property (security) be returned to the borrower. Good, acceptable, low qualities, doubtable and bad are the classification of loan by NRB.

Maintenance of Data

A report must be prepared containing clear cut information about loan from release date to recovery data. This works as guideline to current and future management.

2.1.1.9 Renewal of Loan

Whether to renew a loan or not depends under discretionary right of a bank. There holds relationship between the bank and debtor once the loan is extended. Renewal of loan is possible if there is proper adoption of rule and deed including timely payment of debt and interest.

Borrower has to apply inn the bank for the renewal of loan and needs to fill the printed form for that if available. Other«6se, borrower has to write application. Banks studies that and makes field visit to provide loan if necessary.

The following should be analyzed before giving green signal for the renewal of loan.

- Is application for renewal of loan complying with loan or not?
- Is it against the deadlines given by central bank?
- Does the company's own memorandum, articles of association, policy and regulation permits that?
- Is there liquidity remains in banks for renewing the loan of the debtor?
- Whether any problem exists there to renew the loan or not.
- Bank renews the loan if there is no problem.
- Does the use of debt accord with the proposal of loan taking?
- Is payment of debt and interest is made on time?
- Is debtor been benefited from loan taken?
- Do any losses arise after renewal of the loan?

- Whether the debtor is submitting real picture of his business or not.
- Do any extra collateral require in renewing the loan?

2.1.10 Payment of Debt and Interest

As per varieties of loan, the payment procedure of debt and interest differs. In case of long-term loan;-payment is received in the foam of installment and same is applied to hire purchase loan while interest is paid at the stated frequency and principal at maturity in case of overdraft. All these are as follows:

i. Discount

Interest is collected at the commencement deducting from loan amount and debt at the maturity. E.g. If debt for Rs. 100000/- has sanctioned @ l5% p.a., the borrower gets only Rs. 85000/- as Rs. 15000/- is deducted at the source. He pays Rs. 100000/at maturity.

ii. Collects

Interest is collected periodically or in arrears on the basis of period the loan is outstanding. It may be as:

a. Bullet Payment Method

Under it, interest is paid periodically where as principal is paid at the maturity. Principal along with interest for that period is paid at final date.

b. Balloon Payment Method

It is also known as lump-sum payment method since principal and interest are recovered at maturity or any date when debtor comes to pay loan. It is simple and matches with tradition of rural society.

c. **Installment Method (Amortization Method)**

Repayment of loan is made in various installments. Bank may fix installment of principal and interest or only of principal and interest is calculated and collected separately. It is applicable to hire purchase, term loan, priority sectors of which are flown taking movable and immovable property as security.

2.1.1.11 Review of KAFL's Loan Policy

"This policy is revised on the basis of past experience to administrate the lending activities more effectively and efficiently. The policy supersedes the previous policy and will come in force with effect from Shrawan l, 2060. (KAFL's Policy 060). The policy prefers healthy clients for sound purpose considering all legal cum practical aspect and after appraising honesty to optimist returns to company investing- funds in the safest way adhering the interest of depositors and shareholders.

It comprises all together 12 heads. It allows eight types of loans which are as follows:

- Housing (real state) loan
- Business Loan
- Documents loan
- Agricultural Loan
- Hire purchase Loan
- Educational Loan
- Foreign Employment Loan
- Other Loan

Clause 7 deals about collateral required. As per this head Land, Land and Building or other assets such as Plant & Machinery, Equipments and Vehicles or any other collateral having ownership of borrower accepted by the Company shall be accepted as collateral.

In case of unavailability of collateral having ownership of borrower, authorized assets by third party in accordance with prevailing law can be accepted as collateral. Likewise, financial guarantee issued by other bank and finance company against the Company or Fixed Deposit Receipt or authorization of the same issued by the Company or other Bank and Finance Company can be accepted as collateral. But this credit policy of KAFL is silent about insurance provision of the collaterally accepted assets.

Clause 4 deals about Lending Process. As per this section, borrowers have to contact at Loan Department of the Company along with filled u2 'can form and the following documents:

- Photocopy of the citizenship certificate of the borrower
- Photocopy of the Firm Registration Certificate Photocopy of the Income Tax Registration or PAN card
- Recent photocopy of Land Measurement Map
- Photocopy of property title document (Dhanipurja or Lalpurja)
- Photocopy of approved documents issued by concerned office for construction of building (for Housing Loan)
- 'Bato Khuleko Char Killa Kagajpatra' issued by DC or Ward Office
- Paid receipt of the land and building tax
- Approved Income Statement and loan repayment plan
- Board minute and authorized document of appointment of the person for dealing loan for Limited Company
- Quotation of the assets for Hire Purchase loan

- Partnership Deed for partnership firm
- Any other documents demanded by "the Company as deemed necessary.

After getting the loan form along with aforesaid documents. valuation and inspection of the collateral will be done by independent valuator or employee of the company. In case of loan more than Rs.15 Lacs, valuation of the collateral should be done by independent valuator after valuation done by employee of the company. Assets acquired under hire purchase loan should be registered under the name of the Company.

This head deals also about the `Registration and Rokka' of the collateral. All documents about the collateral should be registered to concerned office before releasing the loan.

Clause 8 deals about the interest rate and installment of the loan. Interest rate and service charge are fixed by Board of Director in time to time. Notice about interest rate charged by the company will be published in National Daily Newspaper.

Penalty interest will be charged @ 2% on due installment if borrower default to pay agreed installment in pre-determined time. Generally, Mid-term loan is for 1 to 4 years and Housing Loan is for 2 years. For housing loan 1 year is assumed as construction period and remaining 1 year is treated as loan repayment period. If the borrower feels to extend the loan period, it can be extended up to 2 years more if borrower has repaid minimum 10% of the loan amount at the time of extension date. Clause 6 deals about the sanction authority of loan. Loan amount up to Rs. 1 lack can be sanctioned by loan-manager by following the required lending process. CEO or deputy CEO in case of authority assigned to him by CEO can sanction loan amount up to Rs.2 lacks: Loan sub-committee has authority for sanction of loan up to 30 lacks and loan amount more than 30 lacks should be sanctioned by BOD. Clause 5 deals about preparation of required documents for lending. The company releases the loan only after the preparation of the following documents relating to loan:

- Promissory Note
- Loan deed
- Property title document. (Lalpurja or Dhanipurja)
- Confirmation of `Property Rokka' received from concerned office.

Clause 9 deals about financial guarantee issued by the company. Company shall issue guarantee or financial guarantee under the directives of the Nepal Rastra Bank.

- Company can issue guarantee up to 50% to 65% of collateral for fund-based guarantee.
- For non-fund based guarantee, company can issue up to 75% of the collateral value.
- 10% margin is required for every guarantee.
- Rate of service charge, commission and interest of guarantee are fixed by BOD.

Clause 11 deals about investment provision of the company. Company can invest in securities of the listed public company or primary shares as per decision of the BOD. Except that, company can invest its fund anywhere within limit of Finance Company Act, 2042, Nepal Rastra Bank Act 2058 and NRB Directives.

Clause 12 deals about the miscellaneous provision about loan management like function loan sub-committee, members of the loan sub-committee their membership period.

2.2 Review of NRB Directives:

The latest directives to finance company from NRB are divided into 21 directives (heads) having further division under each. These are as follows:

1. Provisions Relating to Capital Adequacy
2. Provisions Relating to Classification of Loans/advances and Loan Losses
3. Provisions Relating to Single Borrower and Limitation of the Sectoral Credit and Facilities
4. Provisions Relating to Accounting Policies and Format of Financial Statements
5. Provisions Relating to Mitigation of Risks in Transactions of Licensed Institutions
6. Provisions Relating to Good Corporate Governance
7. Provisions Relating to Timeframe for Implementation of Regulatory Directives Issued in connection with Inspection and Supervision
8. Provisions Relating to Investment
9. Provisions Relating to Filing of Statistical Returns by Licenced Institutions to Nepal Rastra Bank
10. Provisions Relating to Transfer or Sale of Promoters Shares of licensed institutions
11. Provisions Relating to Consortium Financing
12. Provisions Relating to Credit Information and Blacklisting

13. Provisions Relating to Compulsory Reserve/Statutory Liquidity

14. Provisions Relating to Opening of Branch/Offices

15. Provisions Relating to Interest Rates

16. Provisions Relating to Collection of Financial Resources

17. Provisions Relating to Lending to Deprived Sector

18. Provisions Relating to Amalgamation, Merger and Upgrading

19. Provisions Relating to Know Your Customers

20. Provisions Relating to Subsidiary Companies

21. Miscellaneous Provisions

Directive No. 2/067

Provisions Relating to Classification of Loans/advances and Loan Losses

Having exercised the powers conferred by Section 79 of the Nepal Rastra Bank Act, 2002,the following Directives have been issued with regard to classification of credit/advances and provisions to be made for its possible loss by the institutions obtaining licenses from this Bank to carry out financial transactions.

1. Classification of loans/advances:

Entire loans and advances extended by a licensed institution have to be classified as follows based on expiry of the deadline of repayment of the principal and interest of such loans/advances:-

(a) Pass: Loans/advances which have not overdue and which are overdue by a period up to three months.

(b) Sub-standard: Loans/advances which are overdue by a period from three months to a maximum period of six moths.

(c) Doubtful: Loans/advances which are overdue by a period from six-months to a maximum period of one year.

(d) Loss: Loans/advances which are overdue by a period of more than one year. The loans which are in pass class and which have been rescheduled/restructured are called as "the performing loan, and the sub-standard, doubtful and loss categories are called non-performing loans.

Note: Loans/advances also include bills purchased and discounted.

2. Additional provisions relating to pass loans:

(1) The following loans may be included in the pass loan:-

(a) Loans/advances extended against the collateral of gold and silver;

(b) Loans/advances of fixed receipts 46

(c) Loans/advances of Government of Nepal securities and loans/advances made against the collateral of Nepal Rastra Bank bonds; Provided that the cases of the loans/advances against the fixed receipts or Government of Nepal securities or Nepal Rastra Bank bond as the additional collateral, such loans and advances shall also have to be classified in accordance with the directive referred to into Point No. 1 above.

(2) The working capital loan having the deadline of up to one year for repayment may be included in the pass loan class. In case the interest to be received from the loans of working capital nature is not regular, such loans have to be classified on the basis of the duration of interest to be due.

3. Additional Provisions Relating to Loss Loans

In case there seems any of the following discrepancies in any of the following loans, whether or not the deadline for repayment of which is expired, such loans and advances has to be categorized as the loss loan:

(a) The market price of the collateral cannot secure the loans;

(b) The debtor is bankrupt or has been declared to be bankrupt;

(c) The debtor disappears or is not identified;

(d) In case non-fund based facilities such as purchased or discounted bills and L/C and guarantee which have been converted into fund-based loan, are not recovered within ninety days from the date of their conversion into loan;

(e) Loan is misused;

(f) Expiry of six months of the date of auction process after the loan could not be recovered or a case is pending at a count under the recovery process;

(g) Providing loan to a debtor who has been enlisted in the black-list of Credit Information Bureau Ltd;

(h) The Project/business is not in a condition to be operated or project or business is not in operation

(i) The credit card loan is not written off within 90 days from the date of expiry of the deadline; 47

(j) While converting the L/C, guarantee and other possible liabilities into a fund based loan under the regular process, if the said loan is not recovered within 90 days; and

(k) In case of expiry of the deadline of a trust-receipt loan.

Note: For the purpose of clause No. 3(e) of these Directives, "misuse" means non-use of the amount of the loan for the purpose for which it has is taken; the project is not in operation; the amount accrued from the concerned project or business is not used in repayment of the loan but in other activities; and the word also includes the loan which is proved to have been misused by a supervisor in the course of inspection or supervision or by an auditor in the course of auditing.

4. Additional Provisions Relating to Term-Loan

In cases of the term loans extended in installments, if the deadline of installment of the principal amount expires, remaining entire loan amount has to be classified based on

expiry of the deadline of the installment amount.Provided that in cases of the installment of the term loan given by licensed institution not having the facility of engaging in overdraft transaction, entire loan amount has to be categorized as loss loan only if the installment amount has crossed the deadline by a period of more than one year. In case the installment amount has crossed the deadline by a period of less than one year, only such installment amount has to be classified in the loss loan with a provision of loan loss. However, this clause shall not be deemed to have hindered if the licensed institution wants to classify the entire loan amount as the loss loan.

Note: For the purpose of this clause "term loan" means a credit/advances made available having fixed the repayment period of more than one year.

5. Additional Provisions Relating to Gold/Silver Loan

The licensed Banks and financial institution of classes "A", "B" and "C" may provide loan having mortgages gold/silver subject to the following conditions:-

(a) The provisions of providing loan by mortgaging gold and silver has to be stated in the credit policy/byelaws of the institution;48

(b) Prior to carry out transaction of gold/silver loan, provisions relating to necessary security, evaluation of the collateral, vault insurance and checkers have to be made;

(c) Annual studies have to be conducted whether or not the gold/silver loan is useful and profitable to the financial institution and annual monitoring has to be conducted from the Board of Directors.

6. Principal and Interest not allowed to be recovered crossing the overdraft limit:

Principal and interests of a loan shall not be allowed to be recovered having overdrawn the current account of a customer so that the overdraft limit is crossed. Provided that this provision shall not be deemed to prohibit to recover the principal and interest having debited the balance in an account of the customer. In case the account is not settled by a period of one month after overdrawn of the account while recovering principal and interest by debiting the account of the customer, the amount overdrawn shall also be included in the loans not recovered and such loans have to be classified in one class lower than the class to which such loans belongs. While debiting the account, overdraft shall not be allowed by crossing the limit provided to the customer.

7. Provisions Relating to Grace Period

Licensed institution shall not normally be allowed to make available term loans with grace period of more than one year. In case longer grace period has to be provided, the reasons for and bases on which such longer period has to be granted, such details shall have to be disclosed and it shall have to be approved by the Board of Directors at the time of approval of the loan .

8. Provisions Relating to Rescheduling and Restructuring of Loans

(1) In case a licensed institution is convinced on the following bases stated in the written action plan submitted by the debtor, it may rescheduled or retract the loan:-

(a) Evidence showing that documents relating to loans and security are adequate;

(b) Bases on which the licensed institution is convinced of the possibility that the rescheduled or restructured loans would be recovered; 49

(c) In addition to submission of written plan of actions for rescheduling and restructuring loans at least 25 percent of the interest due to be paid until the date of rescheduling or restructuring of such a loan has been paid;

(2) While rescheduling or restructuring the loans to the industries which have been recommended by the Sick Industries Preliminary Inquiry and Recommendation Committee formed under Government of Nepal, a minimum of 12 percent of interest has to be paid, other procedures need to be fulfilled and rescheduling and restructuring shall have to be carried out making a provision for twenty-five percent loan loss.Provided that in the event where the loan has been rescheduled and restructured based on payment of less than 12 percent of interests, provision for loan loss has to be made based on the duration upon expiry of the deadline according to the prevailing provisions.

(3) Description of the loans classified pursuant to classes (1) and (2) has to be separately prepared.

Note: For this purpose, "Rescheduling" means the process of extending the timelimit of repayment of the loan availed by the customer. "Restructuring" means *the process of changing the nature or terms and conditions of altering the restrictions on or changing the time limit of the credit facilities.*

9. Provision to be maintained for loan loss

(1) For the loans and bills purchase classified according to these Directives, the following loan loss provision shall be maintained based on the remaining amount of principal:Loan classification Minimum Provision for loan loss

(a) Pass 1 percent

(b) Sub-standard 25 percent

(c) Doubtful 50 percent

(d) Loss loan/the loan extended to blacklisted persons, firms, company or corporate body 100 percent Provided that in case of the insured loans, it would be required to make provision of only 25 percent of the provision referred to in sub-clause (1) 50

(2) In cases of the loans rescheduled and restructured, the following loan loss provision shall be made:-

(a) The loans classified in the pass class at the time of rescheduling and restructuring shall, while rescheduling and restructuring, provision of at least 12.5 percent has to be made as loan loss, while rescheduling and restructuring the loans classified as substandard, doubtful and loss, no adjustment shall be allowed in the then loan loss provision except in the cases referred to in clause 10(c). In cases of the loans made available on an equal monthly installment, no loan loss provision shall have to be made in case of rescheduling and restructuring of the following of such loans if the principal and interest is regular:

(i) In case amount of installment and number of installment is decreased because of prepayment of installment.

(ii) Due to change in the rate of interest having regard to the market situation, the duration of the loan and installment amount has been changed. In this context, if the rate of interest is increased and thereby by the duration and installment amount is increased, the installment amount determined at the time of sanctioning the loan is not allowed to be decreased. Similarly, if the rate of interest is decreased and thereby the duration and number of installment are decreased, the installment amount determined at the time of sanctioning the loan is not allowed to be decreased.

(b) In case the installment of principal of the rescheduled and restructured loan and interest of two years, such loans may be converted into pass loans.

(c) No loans extended having pledged shares shall be rescheduled and restructured.

(3) In the event of deprive sector lending made by licensed institution Bank and financial institution to deprived communities according to Directives of this Bank; if such loans have been secured through Deposit Insurance and Credit Guarant 51 Corporation or if other loans have also been insured an exemption of 75 percent has been made and provision for remaining 25 percent shall be required.

(4) Banks and financial institution shall not provide any type of loan on the security of the memo (*adhakatti*) of an application to be submitted for share purchase at the time of initial public offering. In case of providing loan in such a way, the concerned bank or financial institution shall have to make cent percent loan loss provision.

(5) While providing loan on personal/institutional guarantee, description of property equal in value to the amount of the personal guarantee and in sole ownership of the debtor and free of any claim of any one else shall compulsorily be obtained. Even the loans given only on the basis of personal/institutional guarantee shall also be classified as stated above in pass, substandard and doubtful as may be required and loan loss provision shall be made 20 percent more in addition to the percentage prescribed for that class. Even in the cases where personal guarantee has been taken for the collateral of physical property alone could not secure the loan, the provision for additional loan and stated above has to be made. Classifications of such loan has to be made separately. Provided that in cases of loans and advances made to the institutions referred to in sub-clause (b) of clause 4 of the Directives No. 3, Nepal Oil Limited and Nepal Food Corporation, no additional loan loss provision of 20 percent shall be required to be made.

(6) No additional loan loss provision of 20 percent shall be required to be made in the loan loss provision referred to in sub-clause (3) above in cases of education loan and loans extended to micro-credit financial institutions and cooperative financial institution under the deprived sector lending by banks and financial institution on personal guarantee.

(7) There is no restriction to classify loans and advances of higher class to lower class in case licensed institution so wishes. For an example, substandard loan may be classified as doubtful or loss loan and doubtful loan may be classified as loss loan.

(8) Loans/advances also includes bills purchase and discounts. 52 *Note: Loan loss provision made for performing loan shall be treated as general loan loss provision and that for non-performing loans shall be treated as specific loan loss provision.*

10. Conditions for Adjustment in loan loss provision

No loan loss provision shall be allowed for adjustment except in the following conditions:-

(a) In case the loan is written off;

(b) In the event where repayment of loan is in installment or in partial basis, the loan loss provision made to the extent of the loan so repaid may be written back and adjusted while maintaining loan loss provision according to loan classification; and

(c) In the event of the loan is reclassified after loan rescheduling and restructuring, if the repayment of the principal and interest of the loan so rescheduled and restructured is regular for a consecutive period of two years. Details of such loans shall be separately prepared.

11. Loss Provisions and Auction of Non-banking assets

(1) In case of the non-banking assets accepted by the licensed institution, cent percent loss provisions shall be made from the date of the acceptance.

(2) In case of sale of the non-banking assets, necessary adjustment in the accounts of loss provision maintained for such property shall immediately be made.

(3) While accepting collateral security as non-banking assets by licensed institution, the following provisions shall be applicable while selling the non-banking assets so accepted:

(a) While accepting the collateral property of a customer as non-banking assets whose outstanding loan amount is more than 2.5 million, the concerned party shall compulsorily be black-listed.

(b) Prior to auctioning the non-banking assets in the name of the institution, it shall have to be evaluated by an independent evaluator. No excessive/less evaluation shall be allowed.

(c) Transparent and clear provisions shall be made with regard to auction sale of collateral security/non-banking assets in Financial Administration Byelaws and sales shall have to be carried out in such a manner to serve interest of the bank or financial institution.

(d) While accepting the non-banking assets in such a manner, entire property mortgaged as collateral that could not be sold by auction shall have to be accepted and it may not be accepted in part.

(e) The property so accepted shall have to be sold at the earliest to the extent possible. In case it is necessary for own purpose of the licensed institution, the same shall have to be approved by the Board of Directors and information thereof shall be made available to this Bank as well.

2.3 Review of Journals and Articles

Among the various review of journals and articles pertaining to the study, the major mostly contributing to the study has been outlined below.

Problems loans and cost efficiency in commercial Bank

Berger & Young (1997)

The author suggests that what is largely missing from the research literature related to the field of financial institutions is an analysis of the relationships between problem loans and cost efficiency. Recent empirical literature suggests at least three significant links between these two topics.

First, a number of researchers have found that failing banks tend to be very cost inefficient, that is located far from the best practice frontiers. Cost inefficient banks may tend to have loan performance problems for a number of reasons, for examples, banks with poor senior management may have problems in monitoring both their cost and their loan customers, with the losses of capital generated by both these phenomena potentially leading to failure. The author refers to this as the "bad management" hypothesis. Alternatively, loan quality problem may be caused by an event exogenous to the banks, such as unanticipated regional economic downturns. The expenses associated with the non-performing loans that results could crate the appearance, if not the reality of low cost efficiency. The author refers to this as the "bad luck" hypothesis.

The second empirical link between problem loans and productive efficiency appears in studies that use supervisory examination data. A relationship between assets quality and cost in consistent with the failed bank data, and suggests that the negative relationship between problem loans and cost efficiency holds for the population of the banks as a hole as well as for failing banks.

Third, some recent studies of the bank efficiency have directly included measure of nonperforming loans in cost or production relationships. Whether this procedure improves or hinders the estimation of cost efficiency depends upon the underlying reasons for the relationship between costs and non performing loans.

Thus important policy and research issues rest on identifying the underlying relationship between problems loans and measured cost efficiency.

The primary cause of the problem loans and banks failures determining the most important supervisory focus for promoting safety and soundness at banks deciding how to estimate the cost efficiency of financial institutions.

The authors test four hypothesis bad luck, bad management, skimping and moral hazard using Granger- causality analysis. The bad luck hypothesis persists that exogenous events can cause non- performing loans to increase and that after time passes the extra expenses associated with these loans will be reflected in lower measured cost efficiency. The bad management hypothesis posits that poorly run banks do bad jobs at both cost control and at loan underwriting and monitoring and that after time passes this slacks leads to increase in problems loans as borrowers fall behind on their loan repayments. The skimping hypothesis posits that banks might achieve low costs by under-spending on loan underwriting and monitoring in the short run, and after time passes this slacks results in increase in the problem loans. The authors tests the moral hazards hypothesis by tasting whether equity capital negatively Granger- cause non-performing loans.

The author result suggests that the inter-temporal relationships between loan quality and cost efficiency run in both directions. Increases in non-performing loans tend to be followed by decreases in measured cost efficiency, suggesting that problems loans cause banks to increase spending on monitoring, working out, or selling off problems loans. The data favor the bad management hypothesis over the skimping hypothesis decreases in measured cost efficiency are generally followed by increase in non performing loans, evidence that bad management practices are manifested not only in excess expenditure, but also in subpart underwriting and monitoring practices that eventually lead to non-performing loans. For a sub set of banks that are consistently efficient, however, increase in measured cost efficiency precede increases in non-performing loans, consistent with the skimping hypothesis that banks trade short run expenses reductions in loan quality. Finally decrease in bank capitals ratios precede increased in non-performing loans for banks with low capital ratios, evidence that thinly capitalized banks may respond to moral hazards incentives by taking increased portfolio.

The authors suggested that if these results can be confirmed by future research, their findings have research and policy implications. The inter-temporal relationships revealed by Granger-causality techniques are indicative of which among the alternative hypothesis are consistent with the data. Future research might use other statistically techniques to reveal the inter-temporal relationships between loan quality and productive efficiency in financial institutions; attempt to decompose the determinants of loan quality into interval versus exogenous factors; or focus on the empirical consequences of controlling for loan quality when estimates efficiency. (Berger and young, 1997)

“The banking sector is severally affected by the Non-performing loans problem. It is estimated that the NPL of the Nepalese Baking system is around 16 percent. Therefore, there is not doubt that it has a serious implication on economic performance of the country.” (Dhungana, 2058: 127)

NRB register me thousand five hundred and thirty eight borrowers, who have not repaid the loan they received fro the fifteen major commercial banks of the country, in ‘Black list’.

The black listed number of borrowers and the amount of different commercial banks are reported as follows.

Table 2.2

Bank wise Black listed Borrowers and the account due from them

Banks	No. of Black listed borrowers	Amount due from them (in million)
RBB	546	5526.66
NBL	673	3904.47
HBL	57	383.04
NBBL	45	317.23
NABIL	32	229.30
BOK	17	116.45
NSBIBL	26	102.96
NIBL	17	56.06
EBL	9	33.89
NCCBL	19	32.38
SCBNL	4	19.13
NICBL	2	7.19
LBL	2	0.64

Source: NRB Report.

The principal loan amount due from these one thousand five hundred and thirty eight borrowers in different banks is totaling Rs.5731 million 609 thousand. The interest due is total Rs.5, 717 million 8 hundred thousand. (Bhatta, 2002)

Morris, (1990) in the discussion paper has concluded that “most of the banks concentrated on compliance with central bank rules on reserve requirements, credit allocation and interest rate. While analyzing loan portfolio quality, operating efficiency and soundness of bank investment management has largely been overlooked. The huge loosed now found in the banks portfolio in many developing countries are testimony to the poor quality of this oversight investment function.

He further adds that mismanagement in financial institutions has involved inadequate and over optimistic loan appraisal, tax loan recovery, high risk diversification of landing and investment high risk concentration, concocted and insider landing, loans mismatching. This has led many banks for developing countries to failure in 1980s" (Morris, 1990: 81).

Shrestha, **(1997)** article "lending operation of commercial banks of nepal and its impact on GDP" has presented with the objective to make analysis of commercial banks lending to the Gross Domestic product (GDP) of Nepal. She has set hypothesis that there has been positive impact of landing of the commercial banks to the GDP. In research methodology she has considered GDP as the dependent variable and various sectors of lending dependent variable and various sectors of lending viz. agriculture, industrial, commercial service and social sectors as independent variables. A multiple regression techniques have been applied to analyze the contribution.

The multiple analyzes have shown that all the variables except service sector lending has positive impact on GDP. Thus in conclusion, she has accepted the hypothesis i.e. there has been positive impact by the lending of commercial in various sectors of economy, expect service sector investment. (Shrestha, 1997)

"A study on deposit and credit of commercial banks in Nepal concluded that the credit deposit ratio would to 51.30%, other things remaining the same. In Nepal that was the lowest under the period of review. Therefore, he had strongly recommended that the joint venture banks should to give more credit entering new fields as far as possible; otherwise, they might not be able to absorb even the total expenses. (Shrestha, 1998: 15)

In the same way, **Kishi**,(**1996)** his article states. “The changing face of the banking sector and the HMG/N recent budgetary policy”concludes the following an introduction of the reform in the banking sector as an integrate part of the liberal economic policy, more banks and fiancé companies have come up as a welcome measure of completion.

However because of poor investment policies and lack of internal control the two government controlled banks, Nepal Bank Ltd and Rastriya Banijya Bank’s non-performing assets have increased substantially. Now, Nepal Rastra Bank has awarded the management contact to foreign companies to improve the condition of non performing assets. The policy of giving management is professional consultant is a part of the financial sector reform policy of NRB. (Kishi, 1996: 27-32)

Karki,(2000) has summarizes some of the challenge through his article“The financial sector is facing major challenges of high NPL of the banking sector, which comes around 18% of the total loan but it the loan classification is made according to least international practice, it is assumed to exceed 30% credit demand is being met largely by non-institutional source i.e. private money lender, merchant trade, individual and land lord at very high rate of interest, which is 2-3 times higher then of institutional source, this shows that the unorganized financial sector is playing a major role in Nepalese economy. The liquidity has played a major role in Nepalese economy. The liquidity position of the banking sector is rated as high as 24%, but the productive sector of the economy is starved by credit crunch. This has created a paradoxical situation in banking sector.

He has given some suggestions to improve the Nepalese financial sector:

The financial institutions especially CBs have to identity new area of investment to increase loans and advances in reducing the liquidity position.

With the rapid growth in the number of banks and financial institution, deposit insurance scheme is a must. The principle reasons for introducing such deposit insurance should be one of the social justice rather than economic justification in order to protect the interest of the small depositors. In this condition, this scheme should be expedited to implement. (Karki, 2000: 26-30)

2.4 Review of Thesis

Past thesis relating to loan of which are considered as relevant to this study is reviewed here in.

Mainaly (1999) has studied on “An Evaluation of Loan Distribution and Collection of Agriculture Development Bank”. His research objectives are as follows:

- To analyze the target of loan disbursement and collection.
- To examine the achievement of purpose wise, term wise and development region wise loan disbursement, outstanding and collection.
- To analyze the relationship between targeted and achievement of loan recovery.
- To provide suggestion to ADB/N on the basis findings.

The adopted research methodologies under his thesis are as follows:

- This study is merely concerned with the primary and secondary data and is based on published and presented data for the loan disbursement and collection of ADB/N.
- Descriptive analysis and statistical tools analysis are research designed used by him. He defines descriptive analysis as, “it is difficult to study the principle causes arising from borrowers side and quantify them in relation to the weak repayment performance of ADB/N’s loans disbursement so that

some of the causes are studied in help of descriptive analysis.(Mainaly, 1999)

- Collected data are arranged and tabulated thereafter descriptive studies are made in case of primary data and stastical tools analysis like T-test, F-test, and Karl Pearson's coefficient of correlation is used for secondary data.

His major findings are:

1. Though targeted loan disbursement and collection are increasing, targeted loan collection of the bank is increasing at decline rate.
2. There is significant relationship between the achievement of loan disbursement and collection.
3. Finding from purpose wise actual loan disbursement, outstanding and collection are increasing and their correlation are significant incase of cereal and cash crop purpose, livestock purpose.
4. Actual disbursement, outstanding and collection reveals the fact that short term and midterm loan flow, outstanding and collection are increasing where as long term loan has mixed trend about that.
5. No significant difference between the mean ratios of targeted loan disbursement and actual disbursement. Likewise there is no significant difference between the mean ratio of targeted loan collection and actual loan collection.

Mrs. Bhattrai (1978) in her thesis paper "Lending practice of commercial banks in Nepal" has examined the lending practice of the commercial banks. The researcher found the result that utilization of resources is more important than the collection of the deposits. So, she recommended the banks to give more attention on the efficient utilization of the resources which helps in the economic development of the country.

She has concluded that efficient utilization of resource is more important than the collection of the same. Lower investment means lower capital formation that hampers economic development of the people and the country. So, she recommended that banks should give emphasis on efficient utilization of resources. (Bhattrai, 1978)

Shrestha (2003) in his study concludes that the proportion of loan outstanding has also increased significantly due to increase in long term loan disbursement by the bank and partly by the increase in outstanding loan. It is felt that the bank should be conscious to strengthen its field to the effective collection effort. It is observed positively that repayments of loan by the individual borrowers are marginal farmers with income below the subsistence level. Although the bank finance has increase the productivity, almost of income diverted to meet their consumption needs and that loans remains unpaid. Over and above the post loan supervision of the bank is poorly organized and that in many cases loan are mis-utilised. Most of the field offices rarely conduct post loan supervision and the bank approaches the borrowers only when installment matures. His major recommendations are as follows:

- Bank should grant rebate to the borrowers on timely repayment and charge penalty for over due. The borrowers should be granted the additional loans unless full or partial repayments of the debt are made.
- Sufficient credit should be provided to farmers to induce them to operate their farm under improved technology. The bank should give more priority in providing credit to irrigated farm in the Hill as well as Terai.
- Administration of strict rules and regulation of reward and punishment and post loan supervision should be enforced and those should be punished who neglect rules.

A study conducted by **Mr. Shrestha** (2003) regarding the investment practices of joint venture banks in Nepal with special reference to NABIL Bank Limited, Standard Chartered Bank Nepal limited and Nepal SBI Bank limited has figured out the problem conclusion and recommendation as follows.

“Commercial Banks are more emphasized to be making loans on short term basis against movable merchandise. Commercial Banks have a lot of deposit but very little investment opportunity. They are even discouraging people by offering very low interest rate and minimum threshold balances”.

Commercial Banks invests their funds in limited areas to achieve higher amount of profit. This regarded as a very risky step, which may lead to lose in profit as well as principle. The credit extends by commercial Bank to agriculture and industrial sector is not satisfactory to meet the growing need of the present situation.

He has concluded that the liquidity position of NABIL and SCBNL have not found satisfactory, it is therefore, suggested them to improve cash and bank balance to meet current obligations. SCBNL’s loan and advance to total deposit ratio is lower at all, it is recommended to follow liberal lending policy for enhancement of fund mobilization. It is recommended to NSBIBL that is has to invest its fund in share and debentures of other companies. It is suggested to enhance off balance sheet transactions, diversifying their investments, own new branches, play merchant banking role and invest their risky assets and shareholders fund to gain higher risky assets and shareholder fund to gain higher profit margin. NABIL and SCBIL are recommending to increase cash and balance to meet current obligations and loan demand.

This above study shows that Mr. Shrestha has concluded some conflicting statements which are obviously not matching with his statement of problem. His recommendation ignores the industry average and also failed to figure out what is right in the industry like banking along the excess of investment or loans and advances. And he thinks liberal lending policies solve the problem to increase the level of loans and Advances.

But some where in his recommendation, he has warned commercial Banks to increase the level of loans and Advances and suggested them to increase the level of investment in government securities or in other safe instrument just to avoid the risk arising from lending. Form this, it can be concluded that Mr. Shrestha has made his entire conclusion absolutely and has not made any relative analysis of the pros and cons of the entire factor affecting his study.

Kafle (2005) has concluded his study entitled “Non-performing loans of Nepalese commercial banks.” The researchers mean objective of the study was to know the problems of the non-performing loans and its effect in the ROA and ROE of the Nepalese commercial banks and to find out whether the Nepalese commercial banks are following the NRB directives regarding loan loss provision for non-performing loan or hot.

Through the research Mr. Kafle has found that the no banks have been following NRB’s directives regarding the loan loss provision. He also conclude that the return on assets (ROA) and return on equity (ROE) of the bank deposed upon the NPLs. The high degree of negative correlation between NPL and ROA and the NPL and ROE clearly indicates that there is inverse relation between them. He has recommended that for the smooth operation of the commercial banks, the NPLs should be controlled for this bank should provide necessary training regarding loan management to the manpower’s. In order to remove, the NPLs, banks should take enough collateral so that banks can recover its loan amount. For the loan loss provision as per the NRB directive and to reduce the NPL, the bank management should be effective and the NRB’s monitoring and regulation is necessary. (Kafle, 2005)

A thesis conducted by **Subedi (2002)** on “A Comparative Study of Financial Performance between Himalayan Bank limited and Everest Bank Limited and Everest bank limited” of the period from 1996 to 2000 has outlined his major finding and conclusion as follow:

“The mean and total loans and Advances to total saving deposit ratio of EBL is greater than that of HBL and the coefficient of variation between the ratios of HBL is less than EBL. It means that the ratio of HBL is less than EBL is more uniform than EBL. According to analysis, it found that EBL is more employing its saving deposit in term of loans and advances than that of HBL. So, loans and advances to total saving deposit ratio appear better in EBL than HBL.

The mean total investment to total deposit ratio of EBL is significantly greater than that of HBL but the coefficient of variation between the ratio of HBL but the EBL. It means that the variability of the ratios of HBL is more consistent than that of EBL. According to analysis, it if found that EBL is more successful in utilizing its resources an investment.

However, he failed to give his overall conclusion regarding the superiority of the financial performance of these two banks during the period of the study (1996-2000). He has also put several recommendations out of which few important recommendation are outlined here.

A thesis study conducted by **Lila Prasad Ojha (2002)** on “lending practices: A study on NABIL Bank Limited, standard chartered bank limited and Himalayan Bank Limited” has find found out that the measurement of lending strength in relative term has revealed that the total assets to total liability of SCBNL has the highest ratio. However the performance of other two banks has not deviated for from the mean ratio of SCBNL and the combined average. SCBNL tendency to invest in government securities have resulted with the lowest ratio of loans and advances to total assets ratio. The steady and high volume of loans and advances throughout the years has resulted NABIL ratio to be the highest. The ratio of loans and advances and investment to deposit ratio has measured the portion of total deposit that is used to increase the income of the banks irrespective of the profiles of its application. NABIL has deployed the highest proportion of its total deposit in earning activities and this ratio is significantly above the ratio of other two banks. The combined ratio is highly deviated from the mean ratio of NABIL and SCBNL. This is the indicative of that in fund mobilizing activities NABIL is significantly better than SCBNL.

Similarly the absolute measures of lending strength have revealed that the mean volume of net assets and deposit is highest in SCBNL with moderate variation. The volume of net assets of HBL is the least due to the low share capital, reserve and surplus in its capital mix. But the volume contributed by NABIL in the greatest in the study period. NABIL has the best contribution in productive as well as industrial sector in economy.

He has further concluded that the overall liquidity strength of SCBNL can be considered the best among the banks. However the liquidity risk arising from interest rate in SCNNL is the most likely. Since the market is highly sensitive towards the interest rate an SCBNL has generally been offering low interest rate as compare to other banks. The analysis of lending strength of HBL in loans and advances in the best however loans and advances, investments to deposit ratio have upgraded the performance of NABIL. If HBL strength succeeded in collecting the less chapter source of strength fund of HBL would push the performance of NABIL and SCBNL for behind in the coming future. Also the contribution made by HBL in the productive sector of economy is highly appreciable and the best among these the commercial banks. The highest growth rate, proportionately high volume of loans and advances and the best contribution in agriculture and priority sector and the high level of deposit mobilization of HBL has put his level of deposit mobilization of HBL has put this bask in the top positive in the lending function as demand by national priority, national development. However the better activity ratio of SCBNL has proved this bank then best in managing the lending portfolio according to the demand of profit-oriented business. The high volume of lending activities and high volume of productive sector loan of NABIL has put this bank then but in ratio of SCBNL has pored this bank then best in managing the lending portfolio according to the demand of profit-oriented business. The high volume of lending activities and high volume of productive sector loan of NABIL has put this bank in the top position in absolute term.

On basis of the findings and conclusion he has recommended for the banks as the liquidity position of all these three banks is found to be high he has recommended the banks to look upon new area of lending and investment. The rural economy has always been realizing the credit needs and the dominance of non-organized moneylender in this area has been prevailing. To compromise between the liquidity and credit need of rural economy these banks are highly recommended to expand their credit in this area. SCBNL's contribution in loans and advances is the lowest and this has low degree of variation and low growth rate as compare to NABIL and HBL, SCBNL is recommended to give extra priority on productive and priority sector loan. The increasing provision as loan loss and high volume of non-performing assets in NABIL and HBL certainly attract the high attraction of any person interested with these banks. The high volume of NL non-performing assets may have caused due to the failure of industrial and agricultural sector. NABIL's increased non-performing, asset may have caused due to the accumulated bad debts that is kept behind the certain to show the efficiency of management.

He has used different statistical tools like standard deviation, correlation, trend analysis and financial tools for the data analysis and presentation. In his study he has also taken sector wise loan- priority sector, productive sector etc. the different sector wise loan classification are presented and analyzed only secondary data has been used for the study, the overview of theoretical aspect of the lending practices of the banks has not been analyzed. He has taken five years data from 1997 to 2001 for study of lending practices of NABIL, SCBNL and HBL. (Ojha, 2002)

2.5 Research Gap

The review of above relevant literature has contributed to enhance the fundamental understanding and knowledge, which is required to make study meaningful and purposive. There have been lots of articles, published related to investment policy loans and advances of commercial banks. There are various researches conducted on investment analysis and policy of commercial banks, impact and implementation of NRB guideline in commercial banks but there few research conducted on lending aspect of commercial banks. However, no one has done a study on “Loan Management” with Everest Bank Limited and Nepal Bangladesh Bank Limited. Therefore the research attempts to study in this area. To know the loan management of these two banks will probably be the first study of these banks in the subject matter.

So, this study will be fruitful to those interested person parties scholars, professors, researchers, stakeholders, students, businessman and government for academically as well as policy perspective.

CHAPTER 3
RESEARCH METHODOLOGY

A systematic methodology is required to pick out an actual result for any special study. So, research methodology refers to various sequential steps to be adopted by a researcher in studying a problem with a certain objective in view. Thus, the chapter is to stress on the different method and conditions, which are used while conducting this study.

Research methodology depends on the various aspects of the research project. The size of the project, the objective of the project, impact, importance of the project, time frame of the project, impact of the project in various aspects of the human life etc. are the project in various that determine the research methodology of the particular project. However, the following steps provide a useful procedural guidance so far as research methodology is concerned:

This chapter includes the research design, population and selected sample, source of the data and the data gathering procedures and research variables and the statistical procedures.

3.1 Research Design

The research covers the two joint venture commercial banks in Nepal particular in their loan management practices. The research has its basic objective to figure out the problem therein and provide them with some recommendation. The literature has been reviewed specially from the post thesis conducted and the same aspects of the commercial banks specially this study follows more analytical and less descriptive research design.

3.2 Population & Sample Selection

There are 23 commercial banks operating in the country. Due to the time limitation, to study all the banks will take a long time. In our study, two joint venture banks are taken as sample.

All the commercial banks in Nepal are the population of the study. The commercial banks are as follows.

Table 3.1

Lists of Commercial Banks in Nepal

S.No.	Commercial Banks	Established Date(B.S)
1	Rastriya Banijya Bank Ltd.	2022/10/10 B.S.
2	Nepal Bank Ltd.	1997/07/30 B.S.
3	NABIL Bank Ltd.	2041/03/29 B.S.
4	Nepal Investment Bank Ltd.	2042/11/16 B.S.
5	Standard Chartered Bank Ltd.	2043/10/16 B.S.
6	Himalayan Bank Ltd.	2049/10/05 B.S.
7	Nepal SBI Bank Ltd.	2050/03/23 B.S.
8	NB Bank Ltd.	2050/02/23 B.S.
9	Everest Bank Ltd.	2051/07/01 B.S.
10	Bank of Kathmandu Ltd.	2051/11/28 B.S.
11	NCC Bank Ltd.	2053/06/28 B.S.
12	Lumbini Bank Ltd.	2055/04/01 B.S.
13	NIC Bank Ltd.	2055/04/05 B.S.
14	Kumari bank Ltd.	2056/08/24 B.S.
15	Machapuchhre Bank Ltd.	2057/06/01 B.S.
16	Laxmi Bank Ltd.	2058/06/11 B.S.
17	Siddhartha Bank Ltd.	2058/06/12 B.S.
18	Agriculture Development Bank Ltd.	2024/09/18 B.S.
19	Global Bank Ltd.	2063/02/15 B.S.
20	Citizens Bank Ltd.	2064/01/07 B.S.
21	Prime Commercial Bank Ltd.	2064/06/07 B.S.
22	Bank of Asia-Nepal Ltd.	2064/06/25 B.S.
23	Sunrise Bank Ltd.	2064/06/20 B.S.

24	Dev. Credit Bank Ltd.	2057/10/10 B.S.
25	NMB Bank Ltd.	2053/08/11 B.S.
26	Kist Bank Ltd.	2059/10/29 B.S.
27	Janata Bank Ltd.	2066/12/23 B.S.
28	Mega Bank Ltd.	2067/04/07 B.S.
29	Commerz and Trust Bank	2067/06/04 B.S.
30	Civil Bank Ltd.	2067/08/10 B.S.
31	Century Commercial Bank Ltd.	2067/11/23 B.S.

(Source: NRB website)

The sample taken from the commercial banks are follows

Total population	Sample taken
23 commercial banks	Everest Bank Ltd Himalayan Bank Ltd.

3.3Sources of Data

This study is based on both secondary and primary data.

3.3.1 Secondary Sources

The secondary data have been collected through annual reports of the concerned banks are the major sources of the data for the study. However, besides the annual reports of the subjected banks the following source of data shall also be used in the respective corner of the study.

1. NRB reports
2. Various publications dealing in the subject matter of the study
3. Various articles published in the News papers
4. Annual financial reports of the banks

Besides the above, any kind of other sources such as assertions, interviews, remarked by the specialist of those are capable improvising valuable data and conclusion, shall be considered in the study.

3.3.2Primary Sources

The primary data have been collected through unstructured interview and the observation of researcher. Different types of questions are asked to the respondents in order to examine the loan management of the banks. The respondents include borrowers and bankers. The primary data are the outcomes of the researchers own view. So the reliability of primary data depends on the observation of the researcher.

3.4 Data Collection Procedures

The Annual Report of concern bank was obtained from web sits of banks and field visiting of these banks especially from their corporate office. NRB publication, such as Quarterly, Economic Bulletin, Banking and financial statistics, Economic Report, annual Report of NRB etc. has been collected from the personal visit of concerned department of NRB at Baluwatar. The data on some aspect of these banks was obtained from the website www.nepalstock.com.np. of Nepal stock exchange. The primary data were collected through questionnaire, interview and so on and these data would be presented in required form.

3.5 Method of Data Analysis

For the analysis of the data the financial and statistical tools relevant to the topic are used. They are as follows.

3.5.1 Financial Tools

Ratio Analysis

A ratio analysis is simply one number expressed in terms of another and as such it express the quantitative relationship between any two numbers. Ratio can be expressed in terms of percentage, proportion and as coefficient. The technique of ratio analysis is a part of the whole process of analysis of financial statements of any business of industrial concern especially to take output and credit decision. Through this technique, a comparative study can be made between different statistics concerning varied facts of a business different statistics concerning varied facts of business units. Just as the blood pressure, pulse and temperatures are the measures of the health of an individual. So, ratio analysis measures the economic financial health of a business concern. Thus, the technique of ratio analysis is of a considerable significance in studying the financial stability, liquidity profitability and the quality of the business and industrial concerns. (Kothari, 1994: 169)

For the study period following ratios are analyzed.

1. Current Ratio

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

2. Liquid fund to Current liabilities ratio

$$Liquid\ Fund\ To\ Current\ Liabilities\ Ratio\ \text{X} \frac{Liquid\ Fund}{Current\ Liabilities}$$

3. Liquid fund to Total Deposit Ratio

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

4. Total Assets to Total Liability Ratio

$$Total\ Assets\ To\ Total\ Liabilitiest\ Ratio\ \text{X} \frac{Liquid\ Fund}{Total\ Liabilities}$$

5. Loans and Advances to Total Assets Ratio

$$Loan\ \&\ Advances\ To\ Total\ Assets\ Ratio\ \text{X} \frac{Loan\ \&\ Advances}{Total\ Assets}$$

6. Loans and Advances and Investment to Total Deposit Ratio

$$Loan\ \&\ Advances\ \&\ Investment\ To\ Total\ Deposit\ Ratio\ \text{X} \frac{Loan\ \&\ Advances\ \&\ Investment}{Total\ Assets}$$

7. Loans and Advances to Shareholders Equity

$$Loan\ \&\ Advances\ To\ Shareholders\ Equity\ Ratio\ \text{X} \frac{Loan\ \&\ Advances}{Shareholders\ Equity}$$

8. Interest Income to Total Income Ratio

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

9. Interest Expenses to Total Deposit Ratio

$$Interest\ Expenses\ To\ Total\ Deposit\ Ratio\ \text{X} \frac{Interest\ Expenses}{Total\ Deposit}$$

10. Interest Income to Interest Expenses Ratio

$$Interest\ Income\ To\ Interest\ Expenses\ Ratio\ \mathrm{X} \frac{Interest\ Incomes}{Interest\ Expenses}$$

11. Growth Rate of Total Deposit

Growth Rate = Ending Deposit- Beginning Deposit

12. Growth Rate of Loans and Advances

Growth Rate = Ending Loan & Advances- Beginning Loan & Advances

13. Growth Ratio of Total Investment

Growth Rate = Ending Investment - Beginning Investment

14. Growth Ratio of Net Profit.

Growth Rate = Ending Net Profit - Beginning Net Profit

3.5.2 Statistical Tools

3.5.2.1 Standard Deviation

It is defined as the positive square root of the mean of the square of the deviations taken from the arithmetic mean. It is denoted by σ. It is said to be the best measure of dispersion as it satisfies most of the requisites of a good measure of dispersion.

If x be the variate value and ……………..their arithmetic mean, then the s.d i.e σ is given by

3.5.2.2 Coefficient of Variation

The coefficient of dispersion based on standard deviation multiplied by 100 is known as the coefficient of variation (C.V.). if ……..be the arithmetic mean and σ , standard deviation of the distribution, then the C.V is defined by

3.5.2.3 Correlation Coefficient Analysis

The analysis identifies and interprets the relationship between the two or more variables. Karl-Pearson’s Correlation Coefficient has been used to find out relationship between the variables in order to know the effect in one variable may have effect on other correlated variable. In our study co-efficient of correlation has been used to find out the relationship between the following variables.

- Correlation Analysis between Deposit and Loans and Advances
- Correlation Analysis between Investment and Loans and Advances
- Correlation Analysis between Total Income and Loans and Advances.
- Correlation Analysis between Interest Income and Net Profit.

Probable Error or P.E. (r) = 0.6745 $\frac{1Zr^2}{\sqrt{N}}$

3.5.3 Trend Analysis

Trend Analysis is an analysis of a firm’s financial ratio over time used to estimate the likelihood of improvement or deterioration in its financial condition.

It is important to analyze trend in ratios as well as their absolute level, for trends give clues as to whether a firm’s financial conduction is likely to improve or to deteriorate. In our study the trend of following are studied.

- Trend analysis Loans and Advances and Total deposit.

) Trend analysis of Investment and Total Deposit Ratio.

Let the trend line between the dependent variable y and the independent variable x ie time be represented by:

Y= a+bx…………………i

Where, a= Y intercept or value of y when x=0

b= slope of the trend line or amount of change that comes in y for a unit change in x.

CHAPTER 4

PRESENTATION AND ANALYSIS OF DATA

In this chapter, all the efforts have been made to analyze and present the collected data from the various sources. This chapter determines the quality of the study because the collected data are present and analyzed with the help of various financial and statistical tools, tables, graphs etc as of meaningfully and clearly. This chapter his performed to know the clear picture of the loan management of the commercial banks.

4.1 Measurement of Liquidity Position of the Bank

To determine the liquidity position of the two banks under the following measures of liquidity ratio have been calculated and a brief analysis of the same has been conducted below.

4.1.1 Current Ratio

This is a crude measurement of liquidity ratio. It measures the ratio between total current assets and total current liabilities.

The current asset include cash and bank balance with cheque in hand, balance with NRB, money at call and short notices, investment in government securities, bills purchased and discovered loans, and advances and other current assts, similarly, current liability includes borrowing from other banks, deposit, bills payable, and other current assets.

Table 4.1

Current Ratio

	Fiscal Year (Mid July)							
Banks	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	S.D	C.V.
EBL	1.1212	1.1501	1.1312	1.1411	1.0477	1.1183	0.0409	3.667
HBL	0.0620	.08748	0.8432	.08609	0.9801	0.7242	0.3740	51.64

Source: Annual Report of EBL and HBL.

The combined mean ratio is .9212, if we measure the performance of these banks based in this mean, the performance of EBL is weak and the HBL has maintained good liquid assets. The mean current ratio of EBL is 1.1183 and HBL is 0.7212 which is higher than HBL.

Table 4.1 measures the current ratio of two banks of five consecutives years. The ratio has been ranged from .0620 to 0.9801 of HBL. Table explains that the current ratio of EBL is 1.0477 to 1.1212. The s.d and c.v of the EBL is lesser than HBL. So, it is less risky and more consistent than HBL.

4.1.2 Liquid Fund to Current Liability Ratio

Table 4.2

Liquid fund to Current Liability Ratio Fiscal Year (mid July)

	Fiscal Year (Mid July)							
Banks	2005/06	2006/07	2007/08	2008/09	2009/10	Mean	S.D	C.V.
EBL	0.1114	0.1307	0.1194	0.2402	0.2061	0.1615	0.0579	35.83
HBL	0.062	0.056	0.0405	0.766	0.0952	0.066	0.0208	31.48

Source: Annual Report of EBL and HBL.

Since the current ratio gives only the short and crude idea of liquidity position of a firm, measuring its liquidity ratio depending on liquid fund is more significant. Liquid fund comprises of those assets, which can be converted into cash within a short period without decline in their value cash in hand balance with NRB balance with other banks and money at cell included in calculating the liquid fund. The ratio measures a bank ability to discharge its current liability in an adverse condition without undergoing its liquidity risk.

Table 4.2 explains that the ratio has been ranged from 0.1114 of EBL in 2005/06 to 0.062 of HBL in FY 2005/06. The ratio of EBL of first four years is in increasing trend, then it is decreased in 2009/10. The ratios of HBL of last three years is in increasing trend but it has fallen in 2006/07. Unlike current ratio, the liquid fund to current liability ratio has been declined, this declined in two banks has caused due to high degree of increase in investment and decreased or lower level of increase in placement. The s.d and c.v of the HBL is lesser than EBL. So, it is less risky and more consistent and uniformity of liquidity over the periods.

4.1.3 Liquid Fund to Total Deposit Ratio

The deposit constitutes the major part of the banks' liability. Flow of this liability is always uncertain in the bank's fund management. Hence, the ratio of liquid fund to total deposit indicates the banks' strength to meet uncertain flow of deposit.

Table 4.3

Liquid Fund to Total Deposit Ratio

Banks	Fiscal year (Mid July)					Mean		
	2005/06	2006/07	2007/08	2008/09	2009/10		S.D	C.V
EBL	0.1125	0.1314	0.1112	0.1849	0.2116	0.1503	0.0454	30.2488
HBL	0.0582	0.0524	0.0396	0.0766	0.1028	0.0659	0.0245	37.2269

Source: Annual Report of EBL and HBL.

Table 4.3 explains that the ratio of both banks seem similar. The trend of this ratio has not deviated from liquid fund to current liability ratio and the up and down in this ratio has caused by the some reason. Ratios of HBL is up and down. Ratio of EBL is in increasing trend in last two years 2008/09 to 2009/10.

The combined mean ratio of these two banks is 0.1081. The mean ratio of EBL is 0.1503 and HBL is 0.0659 .The s.d and c.v of the HBL is lesser than EBL. So, it is less risky and more consistent than EBL.

4.2 Measuring the Lending Strength

The lending strength of these two banks is measured in relative measures in this section. The relationship between various assets and liabilities of the balance sheet has been established to show the active strength of lending of each bank comparatively. An attempt is made to determine the lending strength in absolute figure of each bank, since these two banks are comparable in volume of deposit loans and advances and other variables also.

4.2.1 Total Asset to Total Liabilities Ratio

The ratio of Total Assets to total liabilities measures the volume of total liability in total assets of the firm. Then banking organization creates credit by way of lending activities and multiplies their assets many items, than their liability permits. Thus, this ratio measures the banks ability to multiply its liability into assets. It is always recommended to have higher ratio of total assets to total liabilities ratio. Since it signifies overall increase of credit and overall development of the organization. The higher the ratio, higher the productivity and higher the assets conversion and vice versa.

Table 4.4

Total Assets to Total Liabilities Ratio

Banks	Fiscal year (Mid July)					Mean		
	2005/06	2006/07	2007/08	2008/09	2009/10		S.D	C.V
EBL	1.1805	1.2015	1.153	1.124	1.1367	1.159	0.0317	2.737
HBL	1.0379	1.0237	1.009	1.006	1.166	1.048	0.0669	6.381
Combined Mean						1.103		

Source: Annual Report of EBL and HBL.

Table 4.4 explains that one unit of liabilities of concerned bank has tabulated value of assets in respective years. All these banks have high degree of similarity in maintaining this ratio. The trend of this ratio is decreasing in EBL from 2007 to 2009. The ratio has been ranging from 1.201 of EBL in 2006/07 to 1.166 of HBL in 2009/10.

The combined mean ratio of these two banks over the period is 1.103. The mean ratio of EBL is 1.159 and this is higher than that of HBL. Taking the standard of Mean ratio the performance of EBL is the best. However, the ratio of these two banks represents a poor performance. The ratio should not be below 2 times in the developing country like Nepal. This represents that these two banks have not successfully converted their liability into asset. Table explains that the ratio of two banks is decreasing in some extend. Looking this fact, it can be concluded that these banks are not utilizing their fund efficiently and effectively to extent, their liability permits them. As comparing among the banks the performance of EBL can be regarded the best. The s.d and c.v of the EBL is lesser than HBL. So, it is less riskier and more consistent than HBL.

4.2.2 Loans and Advances to Total Deposit Ratio

Loans and advances are the major area of fund mobilization of commercial Banks. Loans and Advances is the first type of application of funds, which has more risk. Loans and Advances and total deposit ratio indicates the firm's fund mobilization power in gross. The main sources of bank's lending are its deposit. Thus, this ratio measures how well deposit have been mobilized. This ratio measures the ability of a bank generating income from bank's deposit liability.

Table 4.5 explains the relation between a unit of deposit with the tabulated value of loans and Advances of concerning banks in given years. The ratios have been ranged from 0.7856 of EBL in FY 2007/08, 0.7439 of HBL in FY 2009/10. HBL has the high ratio for the whole period from 2005 to 2010.

Table 4.5

Loans and Advances to Total Deposit Ratio

Banks	Fiscal year (Mid July)					Mean		
	2005/06	2006/07	2007/08	2008/09	2009/10		S.D	C.V
EBL	0.7343	0.7743	0.7856	0.7343	0.7623	0.7581	0.0232	3.0719
HBL	0.5266	0.5272	0.5471	0.6356	0.7439	0.596	0.0945	15.778
Combined Mean						0.677		

Source: Annual Report of EBL and HBL.

The combined mean ratio of these two banks is 0.677. The overall performance of EBL seems the best with mean ratio 0.596. HBL has maintained the lowest ratio. From this analysis, EBL can be concluded as the best performer in utilizing its deposit irrespective the area of its utilization. The s.d and c.v of the HBL is more than EBL. So, it is more riskier and less consistent than EBL.

4.2.3 Loans and Advances and Investment to Total Deposit Ratio

Loans and Advances and Investment are the major area of fund mobilization of commercial banks. Loans and Advances is the first type of application of funds, which has more risk as compare to Investment and gives more returns. Investment is cushion against the liquidity risk and at the same time it gives return. Loans and advances and investment to total deposit ratio indicates the firm’s fund mobilizing power in gross. The main sources of bank’s lending and investment is its deposit. Thus, this ratio measures how well the deposits have been mobilized. This ratio measures the ability of a bank in generating income from bank’s deposit liability.

Table 4.6 explains the relation between a unit of deposit with the tabulated value in loans and advances and investment of concerning banks in given years. The ratios have been ranged from 1.048 of EBL in FY 2006/07 , 0.9685 of HBL in FY 2009/10. HBL has the increasing ratio for the whole period. EBL has decreasing trend in ratio from 2007 to 2010.

Table 4.6

Loans and Advances and Investment to Total Deposit Ratio

Banks	Fiscal year (Mid July)					Mean		
	2005/06	2006/07	2007/08	2008/09	2009/10		S.D	C.V
EBL	0.8267	0.8369	1.0038	0.9720	1.0355	0.9349	0.0969	10.3634
HBL	0.7825	0.9342	0.9042	0.8864	0.8830	0.8780	0.0571	6.5077
Combined Mean						0.9064		

Source: Annual Report of EBL and HBL.

The combined mean ratio of these two banks is 0.877. The overall performance of EBL seems the best with mean ratio 0.9789. HBL has the mean ratio of 0.7764. From this analysis EBL can be concluded as the best performs in utilizing its deposit irrespective of the area of its utilization. The s. d. and c. v. of the HBL is lesser than EBL. So, it is less risky and more consistent than EBL.

4.2.4 Loans and Advances to Shareholders Equity

Shareholders’ equity is consisted of share capital, share premium, reserves, funds and retained earnings etc. The ratio between loans and advances to shareholders’ equity provides the measures regarding how far the shareholders equity has been able to generate assets to multiply its wealth. The shareholders equity refers to the net shareholders in take in the business. Thus, the ratio measures size of the business and their success in covering liabilities into assets.

Table 4.7

Loans and Advances to Shareholders Equity

Banks	Fiscal year (Mid July)					Mean	S.D	C.V.
	2005/06	2006/07	2007/08	2008/09	2009/10			
EBL	26.8153	37.2558	38.3321	38.3055	33.9029	34.9223	4.8805	13.975
HBL	20.098	21.817	19.7287	20.7994	17.4878	19.9861	1.6073	8.0424
Combined mean						11.1933		

Source: Annual Report of EBL and HBL.

Table 4.7 explains that the overall ratio of these two banks has ranged from 38.3321 of EBL in FY 2007/08 to 20.7994 of HBL in 2008/09. The ratio of EBL has continuously increasing trend from FY 2005 to 2008

The combined mean ratio of these two banks 27.4542 and mean ratio of EBL is 34.9223 and mean ratio of HBL is 19.9861 respectively. This indicates that EBL succeed in generating proportionately higher volume of loan due to the entire business. The s.d and c.v of the HBL is lesser than EBL. So, it is more riskier and more consistent than EBL.

4.3 Analysis of the Lending Efficiency and its Contribution in Total Profitability

4.3.1 Interest Income to Total Income Ratio

Income is one of the most important parts of any business organization. Interest income occupies a greater portion of the total income in a banking business. This ratio measures the volume of interest income in total income. It helps to measure the banks performance on other fee-based activities also. The high ratio indicates the high contribution made by lending and investment whereas low ratio indicates the low contribution made by lending and investment and high contribution by other fee based activities in total income. The ratio measures the volume of interest income in total income of the bank. This ratio helps to measures the banks performance on how well they are mobilizing their fund for the purpose of income generation. This ratio also helps to measure the banks performance on other fee-based activities, since after investing functions fee based activities are the major source of banks income to total income.

Table 4.8

Interest Income to Total Income Ratio (%)

Banks	Fiscal year (Mid July)					Mean
	2005/06	2006/07	2007/08	2008/09	2009/10	
EBL	0.8507	0.8448	0.8379	0.8524	0.8862	0.8544
HBL	1.655	1.2711	1.2263	1.17	1.4504	1.2566
Combined Mean						1.055

Source: Annual Report of EBL and HBL.

The above table shows that HBL has the higher ratio than that of EBL. The ratio of these two Banks has ranged from 0.8862 of EBL in FY 2009/10 to 1.45 of HBL in FY 2009/010.

The combined mean ratio of these two banks is 1.05. Mean ratio of EBL is 0.8544 and mean ratio of HBL is 1.2566. HBL has higher ratio which indicates that it is largely dependent on lending activities and low ratio indicates it has low dependency on lending activity and high dependent on lending activities and low ratio indicates it has low dependency on lending activity and high dependency on other fee based activities.

4.3.2 Interest Expenses to Total Deposit Ratio

This ratio measures the cost of total deposit in relative term. The commercial banks performance depends upon its ability to generate cheaper funds. More the cheaper fund more will be the profitability in generating loans and advances and vice-versa. The high ratio indicates costly fund and this adversely affects its lending performance.

Table 4.9

Interest Expenses to Total Income Ratio (%)

Banks	Fiscal year (Mid July)					Mean
	2005/06	2006/07	2007/08	2008/09	2009/10	
EBL	0.029	0.0284	0.0263	0.0303	0.0425	0.0264
HBL	0.022	0.0228	0.0225	0.0234	0.0413	0.0313
Combined Mean						0.030

Source: Annual Report of EBL and HBL.

Above table shows that the ratio of HBL is in decreasing trend. The ratio of EBL is in fluctuating trend. The ratio ranges from minimum of 0.022 in FY 2005/06 to maximum of 0.0413 in FY 2009/010 of HBL. And ratio ranges from minimum of 0.029 in FY 2005/06 to maximum of 0.0425 on FY 2009/10 of EBL.

The combined mean ratio of these two banks is 0.030. The mean ratio of HBL is 0.0264 and mean ratio of EBL is 0.0313. The mean ratio of EBL is higher than that of HBL. Due to lack of lending opportunities, the supply of the fund is exceeding the demand of the fund.

4.3.3 Interest Income to Interest Expenses Ratio

The ratio of interest income to interest expenses ratio measures the difference between interest rates offered and interest rate charged. The spread between the interest income and interest expenses is the main foundation for the profit of the bank. NRB had restrictions on the interest rate spread of the commercial banks. The interest offered and the interest charged should not be more than 5 percent. The commercial banks are free to fix interest rate on deposit and loans. Interest rate on all types of deposit and loans should be published in the local newspapers and communicated to Nepal Rastra Bank quarterly and immediately when revised.

Table 4.10

Interest Income to Interest Expenses Ratio

Banks	Fiscal year (Mid July)					Mean
	2005/06	2006/07	2007/08	2008/09	2009/10	
EBL	2.26	2.238	2.44	2.158	1.97	2.21
HBL	2.50	2.31	2.39	2.49	2.02	2.35
Combined Mean						2.28

Source: Annual Report of EBL and HBL.

From the above table we can analyze that the ratio of HBL and EBL are fluctuating over five years.

The combined mean of these two banks are 2.21 and 2.35 of EBL and HBL respectively. Mean ratio of HBL is higher than EBL. It means income from interest is more in HBL.

4.4 Analysis of Growth Rate

Growth analysis of the banks involves of growth in deposit, loans, investments and net profit. Growth analysis ascertains has much growth in deposit liability is supported by growth in assets. The analysis also concerns which asset portfolio has significant increment corresponding to the increment in deposit liability.

To examine and analyze the expansion and growth of the banking business, following growth ratios are calculated in this part of the study. The higher ratios represent the better performance of the bank. Growth ratios are directly related to the fund mobilization and investments decision of the bank. This ratio represents how well the commercial banks are maintaining their economic and financial position. These ratios can be calculated by dividing the last period figure by the first period figure then by referring to the compound interest tables. Under these topic four types of ratios namely growth ratios of total deposit, loans and Advances, Total Investment, and net profit of EBL and HBL for the study period have been analyzed.

4.4.1 Growth Rate of Total Deposit

Deposits are the main source of capital for the commercial banks. Bank utilize these funds in loans and advances and as investments.

Table 4.11

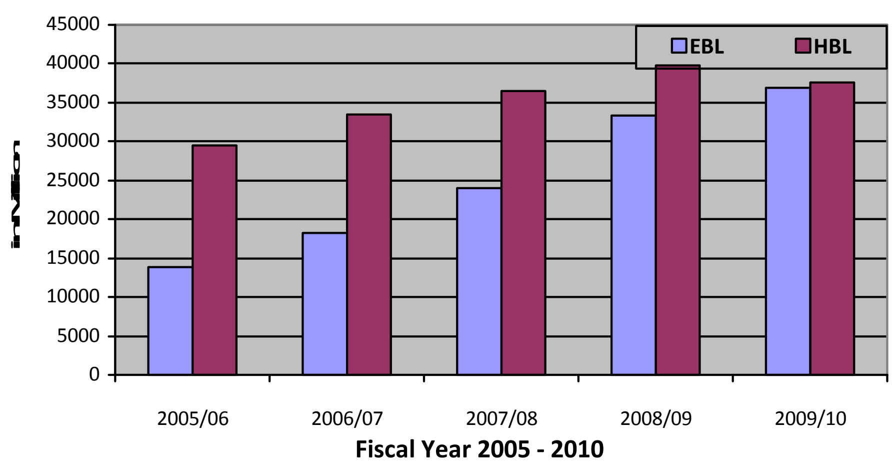
Growth Rate of Total Deposit of EBL and HBL

(Rs. in Million)

Banks	Fiscal year (Mid July)				
	2005/06	2006/07	2007/08	2008/09	2009/010
EBL	13802.4	18186.2	23976.3	33322.9	36932.3
HBL	29460.39	33519.14	36526.8	39790.23	37609.37

Source: Annual Report of EBL and HBL.

Figure 4.1: Growth Trend of Deposit over the Study Period



The above table shows the growth of total deposit by analysis of five years period of EBL and HBL. HBL has the highest deposit of Rs.39790.23 million in 2008/09 and EBL has highest deposit of 36932.3 million in 2009/2010. According to highest range of the total deposit, we can conclude that HBL has good performance than EBL.

4.4.2 Growth Rate of Loans and Advances

Loans and Advances is the major function of the commercial banking of those loans and advances determines the book performance.

Table 4.12

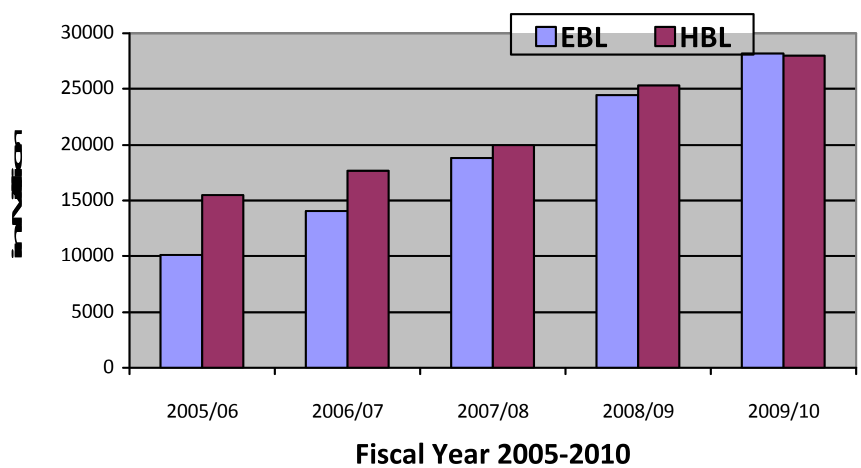
Growth Rate of Loans and Advances of EBL and HBL

(Rs. in Million)

Banks	Fiscal year (Mid July)				
	2005/06	2006/07	2007/08	2008/09	2009/010
EBL	10136.2	14082.7	18836.4	24469.6	28156.4
HBL	15515.7	17672	19985.2	25292.1	27980.62

Source: Annual Report of EBL and HBL.

Figure 4.2: Growth Trend of Loan and Advances over the Study Period



The above table shows the growth of loans and advances of EBL and HBL. There is increasing trend on loans and advances of EBL and HBL. Loans and Advances of HBL is higher than that of EBL in five year during the study period. During the study period it has a significant growth of these two banks and explains its aggressiveness.

4.4.3 Growth Rate of Total Investment

Investment is another important function of banking besides loans and advances. Investment determines the proper utilization of funds.

Table 4.13

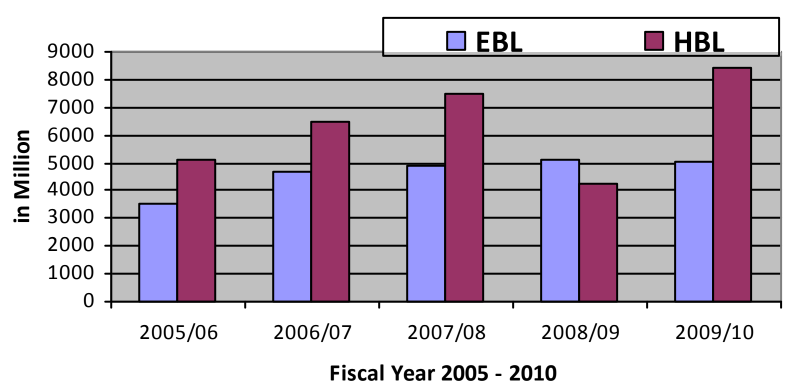
Growth Rate of Total Investment of EBL and HBL

(Rs. in Million)

Banks	Fiscal year (Mid July)				
	2005/06	2006/07	2007/08	2008/09	2009/010
EBL	3548.6	4704.6	4906.5	5146	5008.3
HBL	5144.4	6454.8	7471.7	4212.3	8444.91

Source: Annual Report of EBL and HBL.

Figure 4.3: Growth Trend of Total Investment of EBL and HBL Over the Study Period



The above table shows that there is an increasing trend in HBL from 2005 to 2008 and then it is decreased in 2009 again increased in 2010. Investment of EBL shows increasing trend during all the study period. During the study period total investment of HBL is heigher than that of EBL.

4.4.4 Growth Ratio of Net Profit

A commercial banks performance measuring criteria is its net profit. The growth of net profit reveals the overall performance of the banks.

Table 4.14

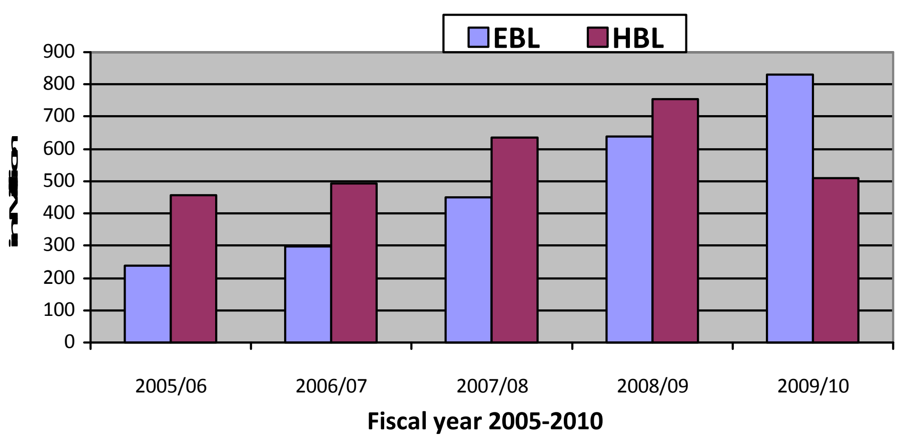
Growth Rate of Net Profit of EBL and HBL

(Rs. in Million)

Banks	Fiscal year (Mid July)				
	2005/06	2006/07	2007/08	2008/09	2009/010
EBL	237.3	296.4	451.2	638.6	831.8
HBL	457.46	491.82	635.86	752.83	508.79

Source: Annual Report of EBL and HBL.

Figure 4.4: Growth Trend of Net Profit of EBL and HBL



The above table describes the growth rate of net profit of EBL and HBL of five years the study period. EBL has the highest profit of Rs.831.8 million in FY

2009/10 and HBL has the highest profit of Rs.752.83 million in FY 2008/09. It has increasing trend of profit of EBL and HBL. But profit of HBL has fluctuation over the year 2009/10.

4.5 Statistical Analysis

4.5.1 Correlation Coefficient Analysis

Correlation coefficient is the measure of correlation between two variables that summarizes correlation in one figure. If the change in the value of are variable is accompanies by the charge in the value of the other, the variables are said to be correlated. Analysis of correlation coefficient explains to what extent two variables are correlated. In this analysis Karl Pearson's Correlation Correlation Coefficient has been used to find out the relationship between variables. Correlation analysis describes the relationship between variables i.e. positive or negative. It helps to determine the following.

- A positive or negative relationship exists.
- The relationship is significant on insignificant.
- Establish cause and effect relation if any.

The statistical tool-correlation analysis is used in the study to measure the relationship between variables in determining within the relationship is significant or not. For the purpose decision making interpretation are based on the following terms.

1. When, r = 1, then is perfect positive correlation.
2. When, r = 1, then is perfect negative correlation.
3. When, r = 0, then is no correlation.
4. When, 'r' lies between 0.7 to 0.999 (-0.7 to 0.999), then is high degree of positive (or negative) correlation.

5. When, ‘r’ lies between 0.5 to 0.6999 there is moderate degree of correlation.
6. When, ‘r’ is less than 0.5, there is low degree of correlation.

4.5.1.1 Correlation Coefficient between Deposit and Loans of EBL and HBL

Table 4.15

Relationship between Deposit and Loans

Banks	Correlation Coefficient	r^2	P.Er.	6×P.Er.
HBL	0.860	0.7396	0.078	0.468
EBL	0.997	0.994	0.0018	0.0108

Source: Annual Report of EBL and HBL.

The above table shows the Correlation Coefficient between deposit and loans and advances of EBL and HBL is 0.997 and 0.860 respectively. There is high degree of positive relationship between deposit and loans and advances of HBL and EBL.

4.5.1.2 Correlation Coefficient between Total Investment and Loans and Advance

This correlation measures the degree of relationship between investment and loans and advances. This measure of correlation explain where the banks have a rigid policy to maintain a consistent relationship between two assets or other factor such as seasonal opportunity, economic demand, NRB directives etc. has impact on the volume of these two variables. Since the volume of investment does not impact on loans and advance as every bank has first priority an loans and advance directly reduce or increases the level of ideal fund and this idleness of fund increases the investments.

Table 4.18 reveals the good relationship between investment and loans and advance. There is high degree of positive relationship between these two variables. However both sample banks have maintained a steady ratio between investment and loans and advances.

Table 4.16

Relationship between Total Investment and Loans and Advances

Banks	Correlation Coefficient	P.Er.	6×P.Er.
HBL	0.790	0.1133	0.3798
EBL	0.996	0.0024	0.0144

Source: Annual Report of EBL and HBL.

Through the above table, we can conclude that EBL has the good opportunity of lending and investment than HBL due to highest degree of positive correlation.

4.5.1.3 Correlation Coefficient between Total Income and Loans and Advances

The correlation between total income and loans and advances measures the degree of relationship between these two variables. The value of r explains whether a percentage change in loans and advances it is independent variable and total income is dependent variable.

Table 4.17

Relationship between Total Income and Loans and Advances

Banks	Correlation Coefficient	P.Er.	6×P.Er.
HBL	0.928	0.042	0.252
EBL	0.963	0.022	0.132

Source: Annual Report of EBL and HBL

Tale 4.19 presented above has shown the high degree of positive correlation of EBL and HBL. The value of r is significant as it is greater than six time of probable error. This explains that a percentage charge in loans and advances is most likely to change the same percentage of income.

4.5.1.4 Correlation Coefficient between Interest Income and Net Profit

The correlation between Interest Income and Net profit measures the degree of relationship between these two variables. The interest income contributes a major portion of total volume of commercial banks income. In this analysis, interest income is independent variable and net profit is dependent variable.

Table 4.18

Relationship between Interest Income and Net Profit

Banks	Correlation Coefficient	P.Er.	6×P.Er.
HBL	0.162	0.204	1.22
EBL	0.993	.0042	0.025

Source: Annual Report of EBL and HBL.

The table explains that the value of r of EBL is high degree of correlation, as the value of r of HBL is low. There is a significant, as role of ‘r’ of EBL is more than 6 times of P.Er. But there is not significant, as the value ‘r’ is less than 6 times of P.Er.

4.5.2 Trend Line Analysis

Least square method is the most popular mathematical method to determine trend of time series. The main objective of this analysis is to analyze the trend of deposit utilization in terms of loans and advances, investment, deposit and of EBL and HBL under five years of study period. A commercial bank may grant loans advances and invest some of the funds in government securities and share and debenture of other companies to utilize its deposit. Using this method of least square in the study, it has been tried to analyze the trend of prospective net profit in future by analyzing the trend of past net profit of banks.

This topic will be used to forecast the ratios of Total deposit, Total Loan and Advances, Total Investment and Net Profit of the banks for next five years on the base of past five years. The analysis is done under limited factors which are as follows.

- The economy will remain unchanged as of present stage.
- Banks will run as of present position.
- The guidelines by NRB for banks will remain unchanged.
- The forecast will be true only when the limitations of least square method are carried out.
- The main assumption is that other factors are constant.

4.5.2.1 Trend Line Analysis of Total Deposit

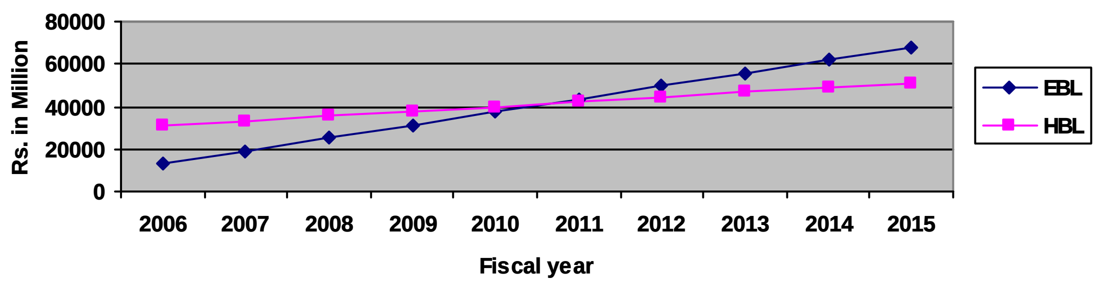
The trend analysis total deposit of EBL and HBL under five years study period 2006 to 2010 and projection for the next five years i.e. 2011 to 2015 is calculated. The following table describes the trend value of total deposit of the bank for 10 years.

Table 4.19

Trend Line Analysis Total Deposit of EBL and HBL

Fiscal Year (Mid July)	EBL (Trend Value)	HBL (Trend Value)
2006	12964.72	30867.38
2007	19104.37	33124.28
2008	25244.02	35381.18
2009	31383.67	37638.08
2010	37523.32	39894.98
2011	43662.97	42151.88
2012	49802.62	44408.78
2013	55942.27	46665.68
2014	62081.92	48922.58
2015	68221.57	51179.48

Figure 4.5: Trend Line Analysis of Total Deposit



The above table shows that the total deposit of EBL and HBL is in increasing trend. EBL has the highest trend value of 68221.57 in the year 2015 and HBL has the highest trend value of 51179.48 in the year 2015. The increasing trend of total deposit ratio of both banks show the good performance of the selected banks in collecting deposits.

4.5.2.2 Trend Line Analysis of Loan and Advances

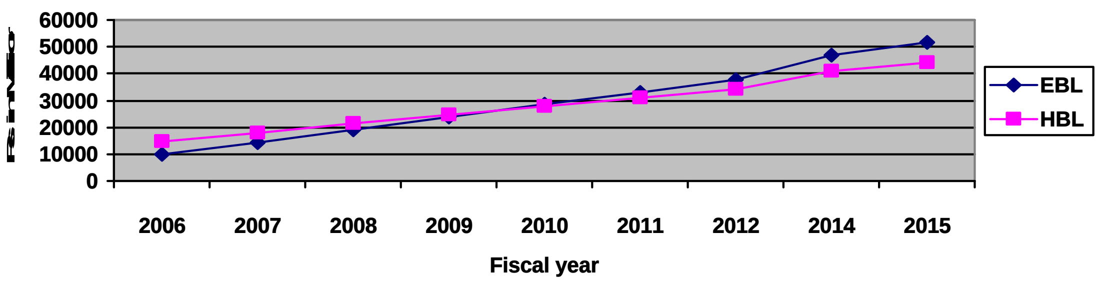
The trend analysis of Loan and Advances of EBL and HBL shows the trend values of five years 2006 to 2010. Over the study period the analysis makes projection for the next five years 2011 to 2015. The following table describes the trend values of Loan and Advances of the selected commercial banks.

Table 4.20

Trend Line Analysis of Loan and Advances of EBL and HBL

Fiscal Year (Mid July)	EBL (Trend Value)	HBL (Trend Value)
2006	9850.8	14779.14
2007	14493.53	18034.13
2008	19136.26	21289.12
2009	23778.99	24544.11
2010	28421.72	27799.1
2011	33064.45	31054.09
2012	37707.18	34309.08
2013	42349.91	37564.07
2014	46992.64	40819.06
2015	51635.37	44074.05

Figure 4.6: Trend Line Analysis of Loan and Advances of EBL and HBL



The above table shows that the total Loan and Advances of EBL and HBL is in increasing trend. EBL has the highest trend value of 51635.37 in the year 2015 and

HBL has the highest trend value of 44074.05 in the year 2015. The increasing trend of Loan and Advances of banks show the good performance in mobilizing the Loan and Advances to different productive and profitable sector.

4.5.2.3Trend Line Analysis of Investment

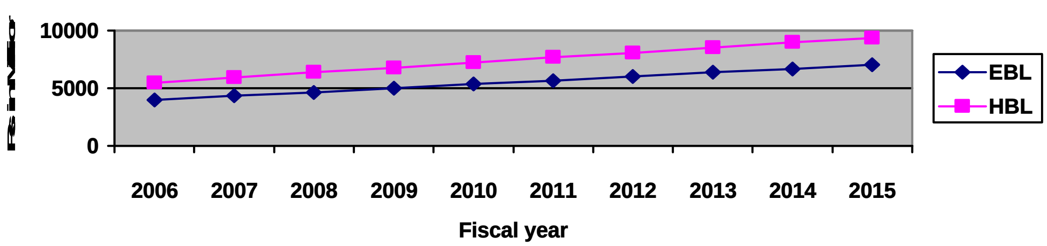
The following table analyzes the trend values of Investment of sample banks for five years and prediction for next five years

Table 4.21

Trend Line Analysis of Investment of EBL and HBL

Fiscal Year (Mid July)	EBL (Trend Value)	HBL (Trend Value)
2006	3990.64	5473.91
2007	4326.72	5909.77
2008	4662.8	6345.62
2009	4998.88	6781.47
2010	5334.96	7217.32
2011	5671.04	7653.17
2012	6007.12	8089.02
2013	6343.2	8524.87
2014	6679.28	8960.72
2015	7015.36	9396.57

Figure 4.7: Trend Line Analysis of Investment of EBL and HBL



In above table, the trend values of EBL and HBL is in increasing trend, which means futures of total investments and deposits of these sample banks are good. EBL has the highest trend value of 1715.36 in the year 2015 and HBL has the highest trend value of 9396.57 in the year 2015.

4.5.2.4 Trend Line Analysis of Net Profit

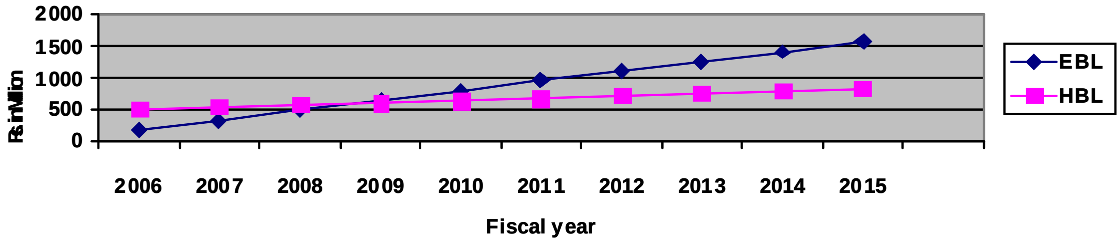
The following table analyzes the trend values of Investment of sample banks for five years and prediction for next five years

Table 4.22

Trend Line Analysis of Net Profit of EBL and HBL

Fiscal Year (Mid July)	EBL (Trend Value)	HBL (Trend Value)
2006	184.82	496.61
2007	337.94	532.98
2008	491.06	569.35
2009	644.18	605.72
2010	797.3	642.09
2011	950.42	678.46
2012	1103.54	714.83
2013	1256.66	751.2
2014	1409.78	787.57
2015	1562.9	823.94

Figure 4.8: Trend Line Analysis of Net Profit of EBL and HBL



In the above table, the trend values of both sample banks are in increasing trend, which means futures of Net Profit of banks are good. In comparison to EBL , HBL is not able to have high trend in Net Profit.

4.6 Major Findings of the Study

In the research data mainly secondary data are used and the analysis is computed with the help of different financial and statistical tools. In financial tools ratio analysis has been used and on statistical tools correlation coefficient, and trend analysis has been used. A primary data analysis is done from the information collected from structured interview with the concerned banks officials. This chapter focuses on the major findings from analysis of Everest Bank Limited and Himalayan Bank Limited from the year 2005/06 to 2009/10.

The major findings of the financial and statistical analysis are presented below.

Finding of Secondary Data

1. Current ratio of both banks showed slightly fluctuating trend. Both of the banks could not maintain the conventional standard of 2:1. However, the average of the ratios appeared higher in EBL, which signifies that EBL is more capable of meeting immediate liabilities in contrast to HBL. The ratio was found more consistent in EBL.EBL is capable in paying the current obligation. However banks show satisfactory level of current ratio.

2. Liquid fund to current liability ratio of EBL and HBL is in fluctuating trend. After analyzing the ratio we can conclude that both the sample banks do not differ significant with respect to this ratio. Both banks have unsatisfied ratios.
3. Liquid fund to total deposit ratio of banks. EBL and HBL are in fluctuated trend. Mean ratio appeared marginally greater in EBL, which means that EBL has maintained greater portion of fixed deposit as liquid asset. The ratio has maintained less consistency in EBL Hypothesis test showed that the mean ratio of two banks does not differ significantly.
4. Total assets to total deposit ratio of EBL is higher than that of HBL. The ratio remained more consistency in EBL. Hypothesis test showed that the mean ratio of the sample banks does not differ significantly.
5. Loans and advances to total deposit ratio of EBL is in fluctuating trend. The mean ratio of EBL is higher than that of HBL. The overall performance of EBL seems to be the best with the higher mean ratio. EBL has more consistency than HBL.
6. Loans and Advances and investment to total deposit ratio of appeared significantly higher in EBL. It indicates the better utilization of loans and advances and investment in EBL than HBL. The ratio remained fluctuating in EBL.
7. The ratio of loans and advances to shareholders equity has gained the significant importance in measuring the capital fund and contribution in loans and advances. The analysis explains that the ratio of EBL the higher than HBL. This indicates that the EBL succeeded in generating proportionately higher volume of loans and advances due to the entire business in future.
8. Interest income to total income ratio of HBL is greater than EBL which reveals that HBL is successful to earn the interest than that of EBL.

9. Interest expenses to total deposit ratio of EBL is more than HBL which reveals that HBL invested the fund and more successfully earn the interest from total deposit.
10. Interest income to interest expenses ratio of EBL is lower than that of HBL which signifies that HBL earns more interest rather than paying the interest for debt.
11. Growth ratio of total deposit of HBL is higher that of EBL by analysis over the study period, so it seems better performance of HBL in total deposit.
12. Growth ratio of loans and advances of HBL is higher than that of EBL over the study period.
13. Growth ratio of total investment of HBL is higher than that of EBL. The highest value increase in total investment of HBL explains it aggressiveness.Groth ratio of HBL in year 2008/09 is low.
14. The growth ratio of net profit of EBL is in increasing trend. But the growth ratio of net profit of HBL is decreased in year 2009/10.So the increasing trend of net profit of EBL explains its aggressiveness.
15. Correlation coefficient between total deposit and loans and advances were found positively correlated of EBL and HBL. EBL has high degree of positive correlation shows the significant relation between net deposit and loans and advances.
16. Correlation coefficient between investment and loans advances were found positively correlated of EBL and HBL. EBL has high degree of positive correlation shows the significant relation between net deposit and loans and advances.
17. Correlation coefficient between total income and loans and advances were found positively correlated in HBL and EBL. The high degree positively correlation coefficient of EBL shows significant relationship between total income and loans and advance. This shows that the bank has succeeded in contribution of significant proportion both investment and loans and

advances. Both the banks have similarity in the correlation coefficient between total income and loans and advances.

18. Correlation coefficient between interest income and net profit of EBL shows high degree of correlation.Due to high degree of positive correlation EBL shows significant relationship between interest income and net profit.
19. Trend line of total deposit of both sample banks is in increasing trend. EBL has the highest trend. It means EBL is successful in mobilizing and collection the deposit.The trend value of HBL and EBL reach to 51179.48 and 68221.57 respectively.
20. Both the sample banks have increasing trend in loan and advances. Among them EBL has high trend which reached up to 51635.37.The trend of sample banks show that futures of total loan and advances are good. They are successful in mobilizing the loan and advances to different productive sectors.
21. Trend lines of sample banks are in increasing trend. HBL has the highest increasing trend which is 9396.57 in 2015.It shows that HBL is successful in mobilizing the investment than EBL.
22. Both the banks have increasing trend in net profit. Among them trend line is high in EBL. The trends of both sample banks are in increasing trend and, which means futures of banks are good.

CHAPTER 5

SUMMARY, CONCLUSION AND RECOMMENDATION

This chapter highlights some selected actionable conclusions and recommendation on the basis of the major findings of the study derived from the comparative analysis of EBL and HBL. The study has covered 5 years data from the year 2006/07 to 2009/10. The major findings of the study based on financial and statistical analysis listed in chapter-4, of this report in order to carry out this study mainly secondary data are used. The analysis of the data is carried out with the help of various financial and statistical tools. The findings of the study are summarized and conclusion and some recommendations drawn as below:

5.1 Summary

Lending is one of the most important functions of a commercial bank and the composition of loans and advances directly affects the performance and profitability of the bank. There is intense competition in banking business with limited market and less investment opportunities available. A study on the liquidity position, loans and advances, profitability, deposit position of EBL and HBL is analyzed.

The mean of current ratio of those two banks over the five year period is 1.1183 and 0.7242 of EBL and HBL. Although the current ratio of 2:1 is considered as standard, acceptability of the value depends on 1:1 or above would be considered acceptable.

Mean of liquid fund to current liability ratio of these two banks over the five years period is 0.1615 and 0.066 respectively and it is less consistent, analyzing this ratio we can conclude that both the sample banks do not differ significant with this ratio.

Mean of liquid fund to total deposit ratio of EBL and HBL is 0.1503 and 0.0659 respectively and it is less consistent. The ratio measure how well the deposits are being mobilized. The ratios of these two banks are in fluctuating trend. Here, none of the ratios is above 1, which refers that some deposit is idle and there is not maximum utilization of the funds.

The Analysis of Lending Strength

The mean ratio of EBL and HBL is 1.065 and 1.074 respectively and it is consistent over the years. After analyzing the total assets to total liabilities it can be concluded that these two banks are not utilizing their fund efficiently and effectively to extent their liability permits them.

Mean ratio of loans and advances to total deposit EBL and HBL is 0.7581 and 0.596 respectively and it is less consistent. The ratio measures how well the deposit are being mobilized and in the income generating sector. The ratios are in fluctuating trend.

Means ratio of loans and advances and investment to total deposit ratio of EBL and HBL is 0.9789 and 0.7765 respectively and is less consistent. This ratio measures how well the deposit are being mobilized and in the income generating sector. There is fluctuating trend of ratio. Here the ratio of EBL has above 1 in year 2005/06 and 2006/07 which refers that deposit is not idle and there is maximum utilization of the funds in these years.

Loans and advances to shareholders equity ratio of EBL and HBL over the five year period has mean ratio of 34.92 and 19.98 respectively. The ratio shows how well the investment made by the investor. It also measures the success of converting liability into assets and measures size of the business. The higher ratio of EBL in the year 2007/08, 2008/09 shows that the bank has been successful in generating proportionately higher volume of loans and advances in these years.

Lending efficiency and its contribution in total profitability

Interest income to total income ratio of EBL over the study period in decreasing trend but the ratio of HBL is in increasing trend. Lower ratio of EBL shows low contribution made by lending and investment and high contribution by other fee based activities in total income. But higher ratio of HBL shows high contribution made by lending and investment and low contribution by other fee based activities in total income.

Interest expenses to total deposit ratio of the banks over the study period are in decreasing trend with consistent values. This indicates the decrease in cost of fund. Interest income to interest expenses ratio of EBL and HBL over the study period are in decreasing trend.

From the analysis of growth ratio

The growth ratio EBL and HBL is in increasing trend. According to highest range of the total deposit, we can conclude that HBL has good performance than EBL. The growth ratio of loans and advances during the study period is found to be increasing trend in every year. It has a significant growth in loans and advances of these two banks and explains its aggressiveness. The growth ratio of total investment of HBL decreased in year 2008/09 and EBL decreased in year 2009/10. The growth ratio of Net profit of EBL and HBL is in increasing trend but the ratio of HBL is in fluctuated in year 2009/10.

From the analysis of correlation

The correlation analysis shows that the correlation coefficient ‘r’ between deposit and loans and advances of EBL and HBL is 0.997 and 0.860 respectively. There is high degree of positive relationship between deposit and loans and advances of HBL and EBL. There is high degree of positive relationship between these two variables. However both sample banks have maintained a steady ratio between investment and loans and advances. The correlation coefficient between total income and loans and advances of HBL and EBL is high degree of positive correlation , it shows good fund mobilization.The value of r of EBL is high degree of correlation, as the value of r of HBL is low. There is a significant, as role of ‘r’ of EBL is more than 6 times of P.Er. But there is not significant, as the value ‘r’ is less than 6 times of P.Er.

According to the trend line analysis the total deposit of EBL and HBL is in increasing trend. The increasing trend of total deposit ratio of both banks show the good performance of the selected banks in collecting deposits.

The total loan and advances of EBL and HBL is in increasing trend. EBL and HBL have the highest trend value in the year 2015.The increasing trend of Loan and Advances of banks show the good performance in mobilizing the Loan and Advances to different productive and profitable sector. The trend values of investments of EBL and HBL are in increasing trend, which means futures of total investments and deposits of these sample banks are good. EBL and HBL have the highest trend value in the year 2015.The trend values of net profit of both sample banks are in increasing trend, which means futures of net profit of banks are good.

5.2 Conclusion

The overall performance of sample banks is satisfactory. Analysis of the liquidity positions of these banks show EBL is found to have high liquidity ratio. It concludes EBL is successful in meeting the current obligation. Even HBL fail to maintain the current obligation, HBL is not fail in the point of working policy, it has taken the aggressive policy. Ratio of Loan and Advance of the EBL is higher than HBL. Both banks are satisfactory in the ratio of Loan and Advances. The main objective of a bank is to make profit providing different types of services to its customers. Profit is necessary for the survival of the business. They are able to earn high amount of interest by mobilizing their deposits and assets to different productive and profitable sectors. HBL is more successful in earning interest than EBL. From the profitability view HBL is better as it is able to expense less interest for the debt and earn higher interest.

As deposits, investment, loan and advances are key tools for developing banking performance, they must have a positive relation between them. Coefficient correlation of Deposit and Loans of both the banks show high positive relation. Total Income and Loans and Advances, Total Investment and Loan and Advances also show high positive relation in both banks. The correlation in Interest Income and Net Profit of HBL shows low degree of positive relation.

5.3 Recommendation

Based on above findings and conclusion the following recommendations have been forwarded.

1. The liquidity position of banks should be able to meet the daily cash transaction. Bank should not invest all the deposit as loan. According to the policy of NRB some percentage sho0uld be kept in the banks for fulfilling the required demand of the customers. The Standard liquidity ratio is 2:1. In this research none of the sample banks are able to maintain the standard ratio. They may fail to maintain the daily cash transaction if they do not increase the liquidity ratio.
2. The ratio of loans and advances and Investment to total deposit of HBL is the lowest and this has result in the highest ratio of interest expenses to total deposit. At the same time total deposit to total fund utilized is below the average and there is high chance of growth in deposit as compare to loans and advances.

3. The total deposit is less mobilized to loan and advances by HBL. The purpose of the loan is to generate income so HBL should increase a loan and advances in different productive and profitable sectors.
4. EBL should maintain stability in earning an interest, it has less interest to total income ratio.
5. EBL paid higher interest then HBL which means that it paid higher interest rate. S, more equity funds should be raised than the debt. It must maintain stability in paying interest.
6. Both banks have more debts financing in assets. Debt financing need more interest to be paid so they should decrease debt financing and increase equity financing.
7. The growth rate of net profit is high in both banks but the trend of net profit in HBL is low in last year i.e. 2009/10, it affects the trend of net profit for futures. It may be due to high retain of profit for future. It is recommended to launch different new product or invest in profitable sectors.
8. Without deposits, savings, loans, investments banks seem impossible to survive so for the experience of banking facilities by public the banking awareness is necessary.
9. Banking also has competition, for the survival attractive programs, facilities, easy services, security, new technology etc should be exercised even the sample banks have these all facilities, they are recommended to bring enhancement in banking sector.
10. The most important and customer seeking feature is security. So banks must focus in the security concern for the faith gain of customers.
11. Operating efficiency of the banks must be increase with different trainings providing to the officials.

The performance of both the sample banks is satisfactory. The situation of inflations caused due to different internal and external environments brought difficulty, impossibility, unpredictability and narrow scopes in Nepali economy. For all these NRB should come with strong supervision and action.

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