A COMPARATIVE STUDY ON PROFITABILITY ANALYSIS OF RASTRIYA BANIJYA BANK AND NEPAL BANK LTD

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RECOMMENDATION

This is to certify that the thesis

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has been prepared as approved by this Department in the prescribed format of Faculty of Management. This thesis is forwarded for examination.

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And found the thesis to be the original work of the student and written according to the prescribed format. We recommended the thesis to be accepted as partial fulfillment of the requirements for the degree of

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DECLARATION

I hereby declare that the work reported in this thesis entitled **"A COMPARATIVE STUDY ON PROFITABILITY ANALYSIS OF RASTRIYA BANIJYA BANK AND NEPAL BANK LTD"** submitted to Office of the Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the Master's Degree in Business Studies (M.B.S.) under the supervision of my thesis supervisors Lect. Mr. Kailash Patindra Amatya and Mr. Lal Prasad Aryal of Shanker Dev Campus.

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I am solely responsible for any typing errors or omissions in this thesis.

March, 2013 **Ramesh Pangeni**

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ABBREVIATIONS

A.D.	:	Anno Domini
ABBS	:	Any Branch Banking System
ADB	:	Agriculture Development Bank
ATM	:	Automated Teller Machines
BFIs	:	Bank and Financial Institutions
B.S.	:	Bikram Sambat
C.A	:	Current Assets
C.B.S	:	Central Bureau of Statistics
CD	:	Credit Deposit
CL	:	Current Liabilities
Co.	:	Company
CR	:	Current Ratio
CRR	:	Cash Reserve Ratio
CAR	:	Capital Adequacy Ratio
DFID	:	Department of International Development
EBL	:	Everest Bank Limited
Ed.	:	Edition
EPS	:	Earning Per Share
FA	:	Fixed Assets
FAT	:	Fixed Assets Turnover
FSRP	:	Financial Structure Reform Program
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
HBL	:	Himalayan Bank Limited
i.e	:	That is
JVBs	:	Joint Venture Banks
Ktm.	:	Kathmandu
LA	:	Loan & Advance
LC	:	Letter of Credit
LLP	:	Loan Loss Provision

LTD	:	Limited
MBA	:	Master's of Business Administration
MBS	:	Master's of Business Studies
Misc	:	Miscellaneous
NABIL	:	Nepal Arab Bank Limited
NB	:	Nepal Bangladesh
NBBL	:	Nepal Bangladesh Bank Limited
NBL	:	Nepal Bank Limited
NRB	:	Nepal Rastra Bank
NIC	:	Nepal Industrial and Commercial
NEPSE	:	Nepal Stock Exchange
NGO's	:	Non- Government Organization
NI	:	Net Income
NIDC	:	Nepal Industrial Development Corporation
NIBL	:	Nepal Investment Bank Limited
No.	:	Number
NPAT	:	Net Profit After Tax
NPA	:	Non-performing Assets
NPL	:	Non-performing Loan
PNB	:	Punjab National Bank
RBB	:	Rastriya Banijya Bank
ROTA	:	Return on Total Assets
ROE	:	Return on Equity
SBI	:	State Bank of India
SCBNL	:	Standard Chartered Bank Nepal Limited
SD	:	Standard Deviation
SDC	:	Shankar Dev Campus
SEBON	:	Secutities Board of Nepal
T.U.	:	Tribhuwan University
T.T	:	Telegraph Transfer

CHAPTER – I

INTRODUCTION

1.1Background of the Study

In a country like Nepal, banking consciousness is lacking as well as majorities of the people are economically and financially immobile. So,the country is facing great problem to get economic prosperity. Sustainable economic growth requires intermediary channels for efficient allocation of funds. Through intermediary channels such as financial institutions and financial markets, funds should be efficiently channeled from depositors and investors to borrowers in need of funding, for example, to expand their business or buy a house. By mobilizing the scattered idle resources from the savers, intermediary channels pools up the funds in a sizable volume in order to feed the fund requirement of productive sector of the economy. The role played by financial institutions and financial markets in this process is referred to as the function of financial intermediation. Financial institutions as important financial intermediary channels need to maintain sound business operations. Financial institutions need to better satisfy various financial demands for customers and enhance profitability by continually improving the ways in which they manage risks and their business operations and to remain as the major contributing factors to the growth of the nation's economy, they themselves have to have sustainable existence and growth of themselves for which profitability is necessary.

Profitability is a deviation of the term profit, which explains the ability to make the profit. Profit is primary a measuring rod of a success of a business enterprises. Profit is essential for the survival of the business. It is the difference between revenue generated and expenses occurred over the period of time but the term profit has several different interpretations. It is basic test of the performance of any business concern. Without profit a firm could not attract the outside capital.

Moreover, the owners and creditors would become concerned about the company's future and attempt to recover their funds. Owner creditors and management pay close attention for boosting profit due to the great importance placed on earning the market place. Profitability is a technical term, used to compare performance analysis of different trading systems or different investments within one system. This is computed for each system or investments being compared over the same period long enough to include significant "ups" and "downs". So analysis of the profitability of the business is very essential which can be used to measure the overall efficiency of the business.*(Ronald;2005:345)*

Profitability of the business can be analyzed through the financial analysis which refers to the assessment of the viability and stability of the business. Profitability of a company is usually based on the income statement. A properly conducted profitability analysis provides invaluable evidence concerning the earnings potential of a company and the effectiveness of management. While analyzing profitability different profitability ratios are calculated. A profitability ratio provides a definitive evaluation of the overall effectiveness of management based on the returns generated on sales and investment. The most widely used profitability measurements are profit margin on sales, return-on-investment ratios, and earnings per share.*(Rose; 1991:35)*

1.2 Brief Profile of the Selected Commercial Banks

1.2.1 Nepal Bank Limited

Nepal Bank Limited, the first commercial bank of Nepal, was established in November 15, 1937 A.D (Kartik,30,1994 B.S.). Nepal Bank Limited is the pioneer financial institution of Nepal. From the very conception and its creation, Nepal Bank Ltd, was joint venture between the government and the private sector. Out of 2500 equity shares of Rs.100 face value, 40% was subscribed by the government and the remaining i.e. 60% was offered for the subscription to private sector.

The bank stands its operation with the authorized capital of Rs.10 million with only 10 shareholders when the bank first started. In that era, very few understood or had confidence in this new concept of formal banking. Rising equity shares were not easy and mobilization of deposits even more difficult. This was evident when the bank floated equity shares worth Rs. 2500000, but was successful only in raising Rs 842,000 but now its paid-up capital is Rs.380,383,000. The inception of the bank helped to remove dual currency system and circulating the Nepalese currency throughout the country gradually.

During the past 7 decades, the bank experienced many ups and downs, but it has remained the leading financial institution in Nepal. It has helped vastly in by accumulating the scattered money in small amount in each and every nook and corners of the country and granting loans and advances in various ways.

The bank is running under the leadership of Nepal Rastra Bank (NRB) appointed three management team under the leadership of NRB director, Mr. Maheshwor Lal Shrestha. At present the bank is operating 114 branches in 55 districts of the country with 2815 staffs. The bank plays great role to develop the economic condition of country by providing different facilities and services to their customers like collection of bills and cheques, safe keeping of valuables, financial advising etc

1.2.2 Rastriya Banijya Bank

Rastriya Banijya Bank(RBB), the fully government owned bank and commonly accredited as the people's Bank in Nepal, established in 1996 B.S. has completed glorious 42 years of its service. RBB has Nepal’s most extensive banking network with over 140 branches (140 ABBS Branches). The bank's slogan "It's Your Own Bank" signifies the importance of RBB in the socio- economic development of the country. Since its establishment, RBB has remained an indispensable financial institution of the Nepalese society and economy.

Although RBB ranks No.1 position in terms of total deposits (Rs.773.92billion) and in the terms of loan/investment portfolio, as of FY 2011/12. The Bank's performance has been irregular in past years necessitating the government of Nepal to contract a team of 19 banking professionals to restructure the Bank with financial assistance of the World Bank and DFID. The new Management Team, of whom 16 are Chartered Accountants, joined RBB in January, 2003 A.D. under a two year contract and in January 2005 A.D., the Team was extended for an additional year until December, 2007 A.D key elements of the Team was expected to be retained for an additional period until the restructuring is sustainable.

RBB has the largest branch network in Nepal, covering 52 branches in the mountainous region, 57 in terai region, and 19 in the Kathmandu valley. The Branch Operation Department is responsible for supervising all 118 branch network. The Internal Audit Department monitors the work of the branches and regional offices. With the corporate office located at singhadurbar plaza, RBB has staff of 1500 and maintains 118 branches location throughout the country enabling the bank to provide banking products and services to all segments of the national economy accompanying the rural and agricultural needs as well as the largest industrial and commercial enterprises.

1.3 Statement of the Problems

Commercial Banks play vital role in economic growth of the country. As being a commercial institution, a commercial bank must make profit out of its operation for its survival and fulfillment of its responsibilities. The major activities of the commercial banks include mobilization of resources, which involves cost, and profitable deployment of the resources, generating income. The excess return income over expenses is the main source of profit to the bank. In case the bank fails to generate sufficient returns on the resources deployed, it makes a drain on the company's resources and country's resources as well.

Till the early 1980's A.D, the financial sector was not opened up for private sector, Only two commercial banks- Rastriya Banijya Bank and Nepal Bank Ltd, that are government controlled, are functioning in Nepal. The economic reforms initiated by the Government more than one and half decade ago have changed the landscape of several sectors of the Nepalese economy. The Nepalese banking industry is no exception. As a result of this policy, large number of banks and financial institutions mushroomed across the country. Both the government owned and privately incorporated banks co-exist in Nepalese economy. However, the performance of the privately incorporated banks is doing better than those with the government control. Because of the tailor-made product and services provided by the private institutions, they have been able to perform significantly well in the market.

Profit is the main objectives of every business organization. Besides other tasks they have to achieve the minimum objectives. The successful operation of any organization whatever the nature of it is largely depends upon the planning system that it adopts. So the planning for project is also the most important device to get success for a period. It plays a key role for the effective coordination between various functional budgets. It is important not only for manufacturing industries but also for commercial banks.

Banks generate their profit by mobilizing its deposits by providing short term and long term loans. Besides this, it can gain profit by investing productive resources mutilation sector. The RBB and NBL both are able to generate profit during the study period. The study aims to find out the answer to the following some questions.

- Are the bank's operating profit is satisfactory?
- How is the bank's return over the study period?
- What is the position of income and expenses?
- What step should be taken to improve the profit planning system in the bank so that overall profitability of the bank can be increased?

1.4 Objectives of the Study

Profit plays a vital role in every business organization. It is equally important for commercial banks. Banks are the institutions, which provide many facilities to develop the economic conditions for a country by providing facilities for trade, industry, business, agriculture, tourism etc. Without profit it cannot operate its functions and cannot provide banking facilities to the public. The main objective of the study is to analyze the profitability position of Rastriya Banijya Bank and Nepal Bank Ltd. Besides that, the specific objectives of the study are as follows:

- To compare and evaluate the profitability and operating financial efficiency of Rastriya Banijya Bank and Nepal Bank Ltd.
- To analyze the income and expenditure.
- To analyze costs and profit trends of the banks.
- To provide suggestions and recommendations for the improvement of the overall profitability of the banks and provide information to the stakeholders.

1.5 Significance of the Study

To get the maximum profit and to maintain the profitability of every business firm has to follow the process of profit planning. It leads an organization ultimately a success. Profit planning acts as a vital instrument for minimizing future risks and achieving its objective. The study of profitability of Rastriya Banijya Bank and Nepal Bank Ltd. will prove useful to all the parties interested on profit planning. It may give guideline to follow the profit planning process to any banking sectors. It may also help the bank to develop future plan, to maximize profit.

Furthermore, the study will be useful to the various parties as follows:

- This study will be helpful to management, to make effective profit planning strategy for future. This also will be valuable for researcher, students who want to investigate into the profitability of the selected commercial banks of Nepal. It will also be important to the bank, investors and stakeholders concerned.
- The study will compel the management of Nepal Bank Ltd and Rastriya Banijya Bank Ltd. for self assessment of what they have done in the past and provides guidance for their future plans and program.
- The study enlightens the shareholders, depositors, creditors, NRB, Tax office etc. about the financial performance of the bank as well as the customer, depositor and debtors can identify the better bank to deal with in terms of profitability, safety and liquidity.
- Policy makers, the government and NRB at the macro level will be benefited regarding the formulation of further policies to facilitate economic development of the country.

1.6 Limitations of the Study

There are limitations that weaken the generalizations – e.g. adequate coverage of industries, time constraint, reliability of statistical tools used and other variables. This study is simply for partial fulfillment of the requirement of the Master in Business Studies (M.B.S). So this study will be limited by the following factors.

- The study was concerned only with Nepal Bank Ltd. and Rastriya Banijya Bank.
- The study was only to analyze profitability aspect. It ignored other aspects like assets management, risk management and other activities like investment policy of bank.
- The whole study was based on the data of 5 fiscal years period from the F.Y 2007/08 to 2011/12 and conclusions were confined to the above period.
- This study was based on the financial statements like balance sheet, profit and loss account and cash flow statement which provides the quantitative information.
- This study is mainly based on secondary data. So the result depends on the reliability of secondary data.

1.7 Organization of the Study

The study will be divided into five chapters. They are introduction, review of literature, research methodology, presentation and analysis of data and summary, conclusion and recommendation.

Chapter ─ I Introduction

This chapter deals with introduction, which includes background of the study, simple introduction of selected commercial banks, statement of the problem, objectives, significance, limitation of the study and organization of the study .

Chapter ─ II Review of Literature

The second chapter deals with review of literature which included review of related books, journals, articles, and previous unpublished Master Level Dissertation etc.

Chapter ─ III Research Methodology

The third chapter explains the research methodology used in the study. It included research design, population and sampling, types and source of data, collection procedure, method of analysis and analytical tools used.

Chapter ─ IV Presentation and Analysis

Fourth chapter is the analytical chapter, which is the main chapter. This chapter is mainly concerned with the analysis of the different profitability ratios related to the financial statements of Rastriya Banijya Bank and Nepal Bank Ltd. and the trend analysis of profit with forecast of trend line.

Chapter ─ V: Summary, Conclusion and Recommendations

Ultimately, fifth chapter discusses summary of main findings, recommendation and suggestions. Further, thesis includes reference books. Magazines, newspaper, previous dissertations are shown under bibliography. Bibliography and Appendix have been presented at the end of the report.

CHAPTER – II

REVIEW OF LITERATURE

Literature review is a “stock taking” of available literature in one’s field research. Review of literature is an important part of any research work. It provides the boundary line for any research. Previous studies provide the foundation for present study. So, previous studies cannot be ignored. There must be continuity in research. This continuity in research is insured by linking the present study with past research studies. From this, it is clear that the purpose of literature review is to find out what research studies have been conducted in one’s chosen field of study and what remains to be done. Thus a literature review, the process of locating , obtaining, reading and evaluating the research literature is the area of the student’s interest*(Wolff & Pant;2005)*

Thus the related literature section should conclude with a discussion of the findings and their implications. Here, the author shares the insights he/she has gained from the review of the literature and points out the gaps presently existing in what is known about his/her topic, and thus leads directly to the question he/she proposes to investigate.

The review of literature is a crucial aspect because it denotes planning of the study. The main purpose of literature review is to find out what works have been done in the area of the research problem under study and what has been done in the field of the research study being undertaken. For review study, the researcher uses different books, reports, journals and research studies published by various institutions, unpublished dissertations submitted by master level students.

2.1 Conceptual Framework

Conceptual framework deals with the theoretical aspects of banking in Nepal, commercial banks, working profit, profitability, liquidity, theory of profit, need for profit, tradeoff between profitability and liquidity, financial statement of commercial bank, profit and loss a/c, income statement etc.

2.1.1Banking In Nepal

The evolution of banking industry had started a long time back, during ancient times. There is reference to the activities of money changes in temple of Jerusalem in the New Testament. In ancient Greece, the famous temple of Delphi and Olympia served as the grant depositors for people's surplus funds and these were the centers of money lending transactions. However, as public enterprise, banking made its first beginning, around the middle of the twelfth (12^{th}) century in Italy. The bank of Venice, founded in 1157 was supposed to be the most ancient bank. Following it were established the Bank of Barcelona and the Bank of Geneva in 1401 and 1407 respectively. Subsequently, Bank of Amsterdam was set up in 1609, which was very popular then. The Bank of Venice and the Bank of Geneva continued to operate until the end of eighteenth century with the expansion of commercial banking activities in Northern Europe, there spa rang up a numbers of private banking houses in Europe and slowly it spread throughout the world.

In the context of Nepal, the development of banking is relatively recent. Like other countries, landlords, moneylenders, merchant, goldsmith etc. are the ancient bankers of Nepal. Though establishment of banking industry was very recent, some crude banking operations were in practice even in the ancient times. In the Nepalese Chronicle, it was recorded that the new era known as Nepal sambat was introduced by Shankhadhar, a Sudra Merchant of Kantipur in 880 A.D. after having paid all the outstanding debts in the country. This is the basis of money lending practice in ancient Nepal. The establishment of "Tejarath add" did not collect deposit from public but granted loans to public against the collateral of bullions. Consequently, the major part of the country remained untouched from this limited banking activities. The "Udyog Parishad" was constituted in 1936 A.D. to facilitated trade with India and other countries. One year after its formulation, it was established under the company Act and 'Nepal Bank Act' in 1937 A.D.

In Nepal, modern banking practices emerged with the establishment of Nepal Bank Limited in 1937 A.D. However, the stand of Nepal Bank Limited alone in total monetary and financial sector was not sufficient and satisfactory. Thus, Nepal Rastra bank was set upon 2013/01/14 B.S as a Central Bank under Nepal Rastra Bank Act 2012 B.S. Similarly on 2022/10/10 Rastriya Banijya Bank was established as fully government owned Commercial Bank. With the emergence of RBB, banking service spread to both the urban and rural areas but customer failed to have taste of quality/competitive service because of excessive political and bureaucratic interference. For industrial development, Industrial Development Center was set up in 2013 B.S. which was converted into Nepal Industrial Development Corporation (NIDC) in 2016 B.S. with an objective to promote agricultural product so that agricultural productivity could be enhanced through introduction of modern agricultural techniques. After the establishment of Nepal Arab Bank Ltd. In 2041 B.S under the commercial bank act 2031 B.S. with the allocation of 50% share of Emirates Bank Ltd., Dubai, 20% share of Nepalese financial institutions and 30% share of general public , the new phase of development of the commercial bank started. Nepal Indosuez Bank Ltd. (now Nepal Investment Bank) emerged in 2042 B.S. as the second and Nepal Grindlays Bank Ltd. (now Standard Chartered Bank Ltd.) established in 2043 B.S. as the third joint venture bank in the country. *(Website;NRB)*

After that, there was gradual increase in the number of joint venture commercial banks in Nepal. 'Now, there are 32 commercial banks, 88 development banks, 77 financial companies, 22 Micro credit development banks,16 saving and credit co operatives(limited banking) and 37 NGOs. *(Gorkhapatra daily ;2012)*

The open and liberal policy in the financial sector has helped in establishment of commercial and financial institutions in the country.

2.1.2 Commercial Banks

Commercial Bank on a financial institution transfers monetary sources from savers to users. In the process of such intermediation, commercial banks deploy funds raised from different sources into different assets with a prime objective of profit generation. They also provide technical and administrative assistance to industries, trade and business.

Commercial Banks are one of the most important institutions in the economy. The main function of commercial bank is to lend money to merchants, home owners, farmers and industrialists and to hold Government bond. Commercial Bank is also working as intermediates between surplus-spending units to deficit- spending units.

According to commercial bank act 2031 "Commercial Banks are those banks which are established under this act to perform commercial function except those which are established for specific purpose like Development Banks, Co-operatives etc."

In order to operate the commercial banks incorporated in Nepal, various laws have been consolidated. Commercial Bank Act 2031 B.S. has also been amended quite several times in accordance to the need. After 1955 A.D., NRB permitted the establishment of other Commercial Banks, Finance Companies, Gramin Bikas Banks, Co-operative Societies & NGO's.

2.1.2.1 Functions of Commercial Bank

a) Accepting Deposits

Oldest or main function of commercial bank is accepting deposits. A bank accepts deposit in three forms namely. Saving, current and fixed deposits.

- **Current Account**: The account in which any amount can be deposited and withdrawn at any time is known as current account. The bank gives no interest to the account holders under this account. Nowadays, the banks under this account as per their own rule has determined minimum limit of deposit.
- **Saving Account:** The account which is managed to collect the small saving of people is known as saving account. This account can be opened with nominal amount. The main objective of this a/c is promoted the saving of the people. Limited amount can be deposited and withdrawn from the bank in the specified time. If a person needs the amount more than limit then the prior information should be given to the bank as per their rule. Bank provides nominal rate of interest in this account.
- **Fixed Deposit Account:** The account, which is managed to accept the deposit for fixed period of time providing higher rate of interest, is known as fixed Deposit Account. Amount cannot be withdrawn from bank before the expiry to time. If it is necessary account holder can take loan against the security deposit after paying 2% extra interests.

b) Advancing Loan:

The second major function of a commercial bank is to provide loans and advances from the money, which receives by way of deposit loans, are granted by bank in form of overdrafts, cash credit, direct loans and discounting bills of exchange.

c) Transfer Money

Commercial Banks transfer the amount of public and organizations from one place to another place or one account to another account with the help of T.T.,draft etc

d) Agency Functions

A bank also performs number of services on behalf of its customer. A commercial bank undertakes the payment of subscriptions, insurance premium, rent and collection of cheques, bills, salaries, pensions and dividends. The commercial bank arrange to remit money from one place to another place by means of cheque, draft, wire transfers and also acts as representative of correspondent for his customers.

e) Helps in Issue of Capital

On the request of company, corporation and other organization, it sells shares and debentures, gives guarantee and performs agency function for which it take commission from those organizations against issue of capital made on behalf of those organizations.

f) Exchange Foreign Currency

Commercial Bank exchanges foreign currency on the permission of Central Bank and considering to the directions provided by Central Bank time and again .Now days Commercial Bank fixed the rate of foreign currency as per market demand and competition.

g) Opens Letter of Credit (L.C.)

It opens L.C. for the import and export (foreign trade) of goods. It has got right to issue and accept traveler's cheque. This provision is specially made by the bank to facilitate to the foreign trade. L.C. is the act of providing guarantee to the foreign businessman on behalf of local businessman.

h) Other Functions

It manages locker to keep gold, silver and valuable items safely, collects and publishes the financial information, purchase and sells bill of exchange, provides overdraft facility on the agreement. In case of joint venture commercial bank, it issues internationally valid credit cards, ATM cards, telebanking etc. Beside, bank has many more functions and roles in the development of national economy.

2.1.2.2 Role of Commercial Bank

"Commercial banks have succeeded in becoming a heart of financial system as they hold deposits of government agencies, business firms, millions of people of the nation and make them available through their lending and investing activities to other government agencies, business firms, millions of people of the nation, like many other developing countries including Nepal lack capital formation and proper mobilization of funds. This also stands the major problem in the economic development of a nation. Commercial banks grant long – term loans to industries, which result in increase in the productivity capacity of an industry. The loans given to agricultural sectors enhance the agricultural production. Similarly the loans advanced to different people and corporate bodies help them to increase their incomes and profits."*(Bhandari; 2003:53)*

Commercial bank plays vital role by providing different facilities and services. The important roles of commercial bank are as follows:

- Capital formation
- Monetization of economy
- Price stability
- Control in interest rate
- Availability of credit

- Development of neglected and deprived sectors
- Promotion of saving
- Implementation of monitory policy
- Long term loan
- Transfer of funds

2.1.3 Profit and Profitability

Generally profit is defined as the excess of revenue over cost. In other words, profit is the residual income, which is equal to sale proceeds minus costs. Profit is the resources left to the firm for future growth and explanation or reward to be distributed to the entrepreneurship in the form of dividends etc. In a simple term, profits mean the residual balance of earning expected to be available with the firm that is obtained after deducting entire expenses, costs, charges and provision form total revenue of a period of time.

It is lifeblood of each type of business. Every business organization should earn profits to survive and grow over the long period of time. Obviously, organization will have no future if it is unable to make reasonable profit from its operation. As a matter of fact, the overall efficiency of an organization is reflected in its profits. Profits to the managements are the test of efficiency of an organization is reflected in its profits. Profits to the managements are the test of efficiency and a measurement of control : to the owners, a measure of worth of their investment; to the creditors, the margin of safety to the employees; a source of fringe benefits to the Government, a measure of fixed paying capacity and the basis of legislative action; to customers, a hint to demand for better quality and price cuts; to a bank, less burdensome source if finance existence and finally to the country ,profit are index of economic progress. Thus, if an organization fails to make profit, capital invested erodes and if this situation prolongs it ultimately cease to exist.

Profit has been universally recognized and accepted as measure of business efficiency. Thus, the larger the profits, the more efficiency and profitable the business organization is deemed to be. This criterion has the greater advantage that it provides a common standard of measuring the efficiency if different bank. Regarding this, Laxmi Narayan clearly states, "Profit is the simple, convenient and the most popular yardstick of jugging the efficiency of private and public business enterprises. Profit helps in judging the overall efficiency and is easy to calculate. Even through profit maximization, unlike private enterprise, is not objective of public enterprises, yet profit services as well accepted criterion for the judging the overall efficiency of public enterprises too."*(Narayan;1980:260).*

The profit is the ultimate measure of effectiveness. A profitable company is likely to offer not only security of employment but also promotion prospects, job opportunities and the intense personnel motivation that comes from being associated with success. John Argent observes, "Profit is the barometer of the success of business. It is, indeed, a magic eye that mirrors all aspects of entire business organizations including the quality output."*(Argent;1968:34)*

The term 'profitability' is composed of two words profit and ability. It reflects the capacity of a business organization to earn profit. It is also referred to as earning capacity or earning power of the concern investment. Thus , the term profitability may be taken as the ability to earn profit. According to Howard and Upton, "The word profitability may be defined as the ability of a given investment to earn return on its use."

It may be mentioned that the term 'profitability' is distinguished from the word profit. Profit refers to the absolute quantum of profit whereas profitability alludes to the ability to earn profit. The former is an absolute measure in itself while the latter is a relative one. According to W.M Harper, the profitability is a relative measure. It indicates the most profitable alternative. The profit, on the other hand is an absolute measure. It indicates the overall amount of profit earned by transaction. As the profitability is the relative measure, it is used to judge the degree of operational efficiency of management. Furthermore, it is essentially employed to measure the relative efficiency of different trading systems or different investment within one system. In the profitability analysis, the profit making ability of an organization is measured in terms of size of investment in it or its sales volume. Such an analysis of profitability reveals how particularly such a position stand as a result of transactions made during the year. It is particularly interesting to the suppliers of funds who can evaluate their investment and take necessary decision thereon.

The state of profitability is a variable thing like the temperature and humidity of a day. The determination of profitability by an accountant or analyst is very much similar to temperature reading and study of humidity by a meteorologist. A meteorologist records the weather on daily basis with an intention to forecast its future prospects. Likewise, an analysis records yearly profit of bank with a view to make prediction of the future prospects.

The purpose of profitability measurement is to see whether a bank has effectively used its resources to achieve its profitability objectives. The profitability objectives refer not to the maximum profit the business can produce but to the minimum it must produce. The minimum profit is the profit at the minimum rate required for the desired type of investment in the bank. However, there must not be enough profit to yield the capital in the market rate of return on money, which is already sunk in business, but also to provide additional capital needed to cover the cost of staying in business.

2.1.3.1 Meaning of Profit

Profit, form Latin means "to make progress". It is defined in various ways. In economics, profit is the concept of reward of the entrepreneur for risk taking and management. In business operations, it is the gain from manufacturing; merchandising and selling operations after all expenses are met. Since profit is added to net worth, it may be measured by the increase in net worth over that of the previous accounting period. The amount of concerns profit thus may be determined not only through the profit and loss statement but also by the comparison of the earned surplus or net worth in the balance sheet which, however, is the residue of profits after dividends and any other appropriations and does not reveal details of sources of income and expenses, which are found in profit and loss account. In speculative transactions, profit is the excess of the net selling price over the costs (including all charges) of the security or commodities traded in. *(Woelfel;1999:540)*

Profit is a motivating factor behind many managerial activities. Much has been written about the role (as opposed to the method of calculation) of profit. Profit plays three roles in the capitalistic society. Profit is the financial reward of risk taking; profit is the financial reward for having monopoly power; profit is the financial reward for the efficient management. The promise of profit provides a strong incentive to owners and managers to act efficiently. "Profit is essential for every enterprise to survive in the long run as well as to maintain capital adequacy through retained earnings. It is also necessary to accept market for both debts and equity to provide funds for increased assistance to the productive sectors."*(Robinson;1951:21-22)*

Account and economics are two disciplines in which profit is viewed in different concept. Pure economic profit is the increase in wealth that an investor has form making an investment, taking into consideration all costs associated with that investment including the opportunity cost of capital. Accounting profit is the difference between retail sale price and the costs of manufacture.

A key difficulty in measuring either definition of profit is in defining costs. Accounting profit may be positive even in competitive equilibrium when pure economic profits are zero. In economics, a firm said to be making an economic profit when its revenue exceeds the total (opportunity) cost of its inputs. According to Adam Smith (The father of economics),"Profit is the sum remaining after the payment of a wages(wage) in economics includes payments to officers of corporations, to proprietors, to partners and to farmers, as well as to what we today term (labor), and rent on the unimproved value of land, as the return to capital."

Profit in the accounting sense is the net figure of different between all types of measurable revenues and all measurable costs. In accounting, profit is expressed only on explicit and measurable accounting terms and on the book value basis. However, in economics, profit is measured in the realizable term."Profit is the accounting sense is the excess of revenue receipts over the cost incurred in producing this revenue. This concept of profit is also known as residual concept. But, in economics, both implicit and explicit costs are deducted from total sales revenue in determining profits."*(Cauvery;1997:122-123).*

As a matter of fact over the years there has been quite an evolution as to what particular items should be duducted form gross income to arrive at an "accounting" profit. Thus, "accounting " profit is a concept of man- made legislation, of the courts, of the Security of exchange Commission, of a accounting organizations; a concept, which has always been in evolution. "Economic" profit on the other hand, is a concept of a naural law of economics, and like the law of gravitation has remained and will remain unchanged over the ages. However, the profit under discussion is concerned with accounting profit, which in a simple language, is the positive and fruitful difference between two revenues and total expenses over a period of time. Multiple meaning of the word "profits" have always been troublesome. Accounting have made energetic efforts in recent years to discard the word for that purpose and to refer ot the conventional concept as business income a natural term at avoids any overlap with economic theory, the most important points of difference between the economists and accountants are as follows:

- The inclusiveness of costs i.e what should be subtracted from revenue to get profit.
- Meaning of depreciation
- The treatment of capital gains and losses
- The price level basis of valuation of assets and liabilities

Although there may be arguments in favor and against profit generating almost all firms require earning it. Their rate of earning differs from firm to firm and time to time.

2.1.3.2 Theories of Profit

Economists have propounded several theories of profits to explain profits of entrepreneurs. Most of the theories are centered on the controversy about the role of the entrepreneur. In the following section some to the fundamental theories of profit have reviewed in brief.

a) Theory of Risk and Uncertainty Bearing: It was F.B. Hawley who first developed the theory of risk bearing and concluded that profit is a reward of the entrepreneurs for bearing risks. But, the theory was picked up Professor F.H. Knight who divided risk into insurable risk and uncertainties. Thus according to Knight, profit is a reward to the entrepreneur for his non- transferable function of bearing non- insurable risk and uncertainties.

b) Dynamic Theory of Profit: This theory was propounded by J.B Clark. According to this theory, 'dynamic changes in the economy' are the basic caused of emergence of profits. There is no profit in the static economy as no changes take place. In a dynamic economy there are constant changes in population, capital, methods of production and industrial set up. These changes multiply wants of consumers, which earn profits to the entrepreneur.

c) Innovation theory of profit: Joseph Schumpeter singled out 'innovation' from the dynamic theory of profits and developed economy and innovation in the changing world gives rise to profits. In his views, the entrepreneur plays an important role of introducing innovation in an economy and profits are the rewards for his role as an innovator. The innovation could be changes or techniques that reduces cost of production or increases demand for the product.

2.1.3.3 Need of Profit

Profit is necessary for the following reasons:

- **Measurement of performance**: Profit is only factor to measure the management efficiency, productivity and performance. Profit is the most widely used yardstick to see what really is to be achieved and where the firm is to go in the future.
- **Premium to cover costs of staying in Business:** Business environment is full of risks and uncertainties, to grasp the globally changing technologies, to stay in the market uncertainties, to replace and acquire assets and enhancing business scope etc. require a profit margin.
- **Ensuring Supply of Future Capital:** Profit is necessary to plough back in the investments like innovations, business expansion and self-financing. It also attracts investors for further investment.

- **Return to the investors:** Shareholders provide equity capital to the business because they expect the entity will provide return to their funds at least equal or above market rate of return. To maintain the shareholders expectation, it is most important that a firm should earn sufficient profit so that it can distribute dividends.

2.1.3.4 Profitability of Commercial Banks

"Banks today are under great pressure to perform to meet the objectives of their stockholders, employees, depositors, and borrowing customers, while somehow keeping government regulators satisfied that the banks policies, loans, and investments are sound."*(Rose;1991:155)*

The majority of the needs of the stakeholders are related with the profitability of the banks. For example, in case the bank earns profits, the investors get dividends, employees get bonus, government gets benefits in forms of taxes etc. Thus, the foremost objective of the banks is the profit maximization. As other types of business entity, commercial banks are also inspired by the profit.

The major source of funds of the bank is the public deposit. Commercial banks invest public deposits on those sectors where they can attain the maximum income or higher rate of return as the bank is liable to pay certain rate of interest to the public in their deposit. Hence the investment or granting of loan and advance by them are highly influenced by profit margin. Generally the profit of commercial bank depends upon the interest rate of the bank, volume of loan provided, time period of loan, and nature of investment in different securities. However, the bank at the same time has to ensure that their investment is safe form default.

Aspiration of profit to commercial banks seem reasonable as the bank has to cover all the expenses as interest to the depositors and other administrative costs, they should make payment in the form of dividend to the shareholders who contributed to build up the bank's capital and keep aside for the provision and reserves. For this the bank calculates the cost of fund and likely return, if the spread is enough irrespective of risk involved and absorbs its liquidity obligations, it will go ahead for investment.

A successful bank is one who invests must of its funds in different earning asset standing safely from the problem of liquidity i.e. keeping cash reserve to meet day- to-day requirements of the depositors. After all the commercial bank is simply a business corporation organized for the purpose of maximizing the value of the shareholders wealth invested in the firm at an acceptable level of risk. So bank has to make a crucial decision regarding a mixture of liquidity and profitability cause lower the liquidity higher the profitability and higher the liquidity lower the profitability and both are equally important, banks cannot afford to ignore any of them.

2.1.4 Liquidity

In banking, liquidity is the ability to meet obligations when they come due without incurring unacceptable losses. In other words, the capacity of bank to pay cash against any upcoming obligations is called liquidity. Managing liquidity is a daily process requiring bankers to monitor and project cash flows to ensure adequate liquidity is maintained. Maintaining a balance between short-term assets and short-term liabilities is critical as the commercial banks have liability to the deposits collected and they immediately should give it in the time when the depositors asked. Banking is the business of financial dealing whose major source of financing is the public deposit. Deposit accounts represent the primary funding in traditional commercial banks, and the loan portfolio represents the primary asset. The investment portfolio represents a smaller portion of assets, and serves as the primary source of liquidity. Investment securities can be liquidated to satisfy deposit withdrawals and increased loan demand. Banks have several additional options for generating liquidity, such as selling loans, borrowing from other banks, borrowing from a Central Bank and raising additional capital. Most banks are subject to legally-mandated reserve requirements intended to help banks avoid a liquidity crisis.

Banks pay the depositors money at the demand, and if this is not meet, it damages the banks image. The confidence of the public will be lost and this leads the banks towards downfall. So bank should not invest all the money on investment. It has on exposure based assets only, as it will not be repaid when required. Therefore, banks keep a certain percentage of their fund on such assets that can be utilized as need arises, which is known as liquidity assets.*(Shrestha;2007:204)*

Central bank ensures liquidity of commercial banks by enforcing the letter to maintain a certain percentage of their deposits liability in the form of reserve fund with the central bank and in its vaults.(*Shrestha;2007:204)*

A large part of bank deposits are withdrawn on demand and hence the bank must be prepared with sufficient degree of liquidity of its assets. Once the confidence is lost in depositors eye, they may withdraw all the deposits within the brief period when the bank is unable to generate adequate cash without incurring substantial financial losses since most of assets of the bank are attached in the loan and advances. Even the best bank can hardly survive in such a situation. Confidence depends upon the ability of bank to meet the readily demand for cash made by customers. Commercial banks maintain liquidity in all or any forms of following:

- Cash in self vault and in other banks-specially in NRB (First Line of Defense)

- Overnight placements, moony at call or short notice or any other very short term placements (Second Line Defense).
- Investment in marketable securities like government securities, which can be easily sold and readily convertible into cash (Third line of Defense) (*Dahal & Dahal;1996:41*

2.1.5 Tradeoff between Profitability and Liquidity

Profitability of commercial banks is highly dependent on the optimum utilization of available resources and invests the deposit collected in safe and profit generating assets like loan, and advances and investments. However , banks cannot ignore the necessity of maintaining a portion of the deposits in their cash vault, or in the immediate approach like in the account of central banks or in any highly liquid assets like government treasury bills, other government bonds that can be easily sellable without losing and further value.

A sound liquidity position of the bank satisfies the demand of the deposit holder, which maintains the goodwill of the banks. Since, banks are faithfully considered as the last resort for monetary needs of the public, the incapability of fulfilling their demands will lose the faith of the depositors/public. Once any signaling effect is negatively attached in the perception of the depositors, they tend to doubt in the banks dependability and the can consequent in the bank run. Further, banks must maintain the certain portion of deposits in the vault and in NRB.

However, liquid assets are almost all idle. They do not generate any profits. The cash in the vault meets any upcoming obligations immediately but banks will not be able to generate any returns in such a case. Further, banks do not get any interests or other returns in the accounts maintained in the central banks, NRB in our case.

A balance of assets must be stroked to ensure both profitability and liquidity. These paradoxical principles of liquidity and profitability are reconciled to the maximum benefits of the bank (in order to avoid difficulty in meeting the various commitments), banks strike a balance by arranging their assets in different proportion of liquidity and profitability. *(Shrestha;2007:205)*

Profitability and liquidity maintain a highly negative co-relation. Since both are equally important for commercial banks, banks cannot ignore any of them. So, the crucial decision for the management of the banks is to trade-off between them. The more liquidity the less will be the profitability and vice versa.

2.1.6 Financial Statement of Commercial Bank

The financial statement of a commercial bank includes balance sheet, profit and loss account, cash flow statement and other relevant disclosures. Merely presenting the financial statement does not satisfy the aim of the study as financial statements are just of financial information to this analysis. Thus, the focus of the study will go to the analysis of the financial statements of the bank, especially on profitability of the bank. This will make some attempts to identify the financial position of the bank and to give necessary suggestions there to.

A. Balance sheet

Balance sheet is not an account but it is a statement of assets and liabilities of business enterprises at the given date. It is a statement summarizing the financial position of the firm. The balance sheet is prepared at the end of accounting period. Bank's balance sheet is composed of shareholder's fund, borrowings, debentures and other liabilities and provision on the liabilities side and cash and bank balance, stock, debtors, loan and advances, branch accounts, investment and fixed assets on the assets side.

The brief explanation on accounting heads of the balance sheet is provided below:

a) Capital and Liabilities

i) Share Capital

The amount of paid up capital of the bank should be mentioned under this head. The amount received against calls made should be credited in this share capital account.

ii) Reserves and Funds

This accounting head shall contain the amount of reserves appropriated from profit, as well as created through any other process and accumulated profit. Generally, this account shall be credited by debit to profit & loss appropriation account and utilization of such reserves shall be debited to the concerned reserve and fund accounts. The following account heads fall under this heading.

- **Generally reserve fund**: This is stationary reserve. Under this head, only the amount appropriated from profit as per Commercial Banking act shall be credited. Currently, 20% of the net profit should be transferred to this account. Distribution of dividend by utilizing this fund is restricted and approval of Nepal Rastra Bank shall be obtained for the use of this fund for any other purposes. *(NRB;2006:29)*
- **Capital Reserve Fund**: Profit on revaluation of assets and capital ,assets received in grant from other shall be accounted under this head.
- **Share Premium:** This represents the amount of money collected on issue of share in excess of its face value. The outstanding amount in this account shall not be considered eligible for distribution of dividends. However, it may be used for issue of bonus shares under approval of Nepal Rastra Bank.
- **Other Reserve:** Funds and reserves, other than those mentioned above shall be included under this head.

- **Accumulated Profit/Loss:** Under this head, the balance of the cumulated profit or loss as per shown in the Profit and Loss Appropriation account shall be shown.

iii) Borrowing

The borrowing funds of the bank shall be disclosed under this head. Bank borrowings, placements, overnight placements, borrowing from central banks, foreign banks falls under this heading.

iv) Deposits

The principal liability of a commercial bank is its deposits collected from general public,business and government agencies. Deposits receive dfrom the depositors as well as the interest payable on the deposits shall be credited to the account of the depositors. The deposit liabilities accepted by the bankshall be exhibited under this head.

v) Other Liabilities

Other than the capital and liabilities mentioned above, all other liabilities of whatsoever mature shall be included under this heading. Any other accounting heads that could not be exhibited elsewhere may be included under this head as required.

b) Assets Side

i) Cash Balance

The most liquid assets held by any commercial bank is cash. This heading shall be used for showing the total amount of cash-in-vault, consisting of local and foreign currency. Since cash is the most liquid asset, it is used to cover deposit withdrawals, handle credit demands from customers, and to meet all regular and emergency expenses.

ii) Balance with banks

The balances of amounts in non-interest bearing accounts maintained by the bank with Nepal Rastra Bank as well as with other local and foreign banks shall be exhibited under this head.

iii) Money at call or short notice

The amount of all interest bearing placement with other banks with maturity of less than 7 days with stipulated condition for payment at call or at short notice (48 hours) shall be exhibited under this head.

iv) Investments

As a line of defense to meet demands for cash and serve as a quick source of funds, banks invest certain proportion of funds in the liquid assets. These typically include holding of shorter-term government bonds like treasury bills, development bonds etc. and other securities purchased in the open market and readily convertible into cash in the financial market. Other forms of investment include investment in the shares and debentures of other companies. These investments are mainly made for their ability to generate income. The investments are to be valued at market price or cost price whichever is lower.

Commercial banks invest the funds to the shares, debenture and bond of the other company. They generally do so when there is excess of funds than required and there are no alternative opportunities to make investment in the profitable sector. Now-a-days the commercial banks of Nepal have purchased share and debenture of regional development bank, NIDC and other development banks etc. these type are mainly held for their income-generating power and for other advantage like tax shelter etc. The investments are to be valued at market price or cost price whichever is lower.

v) Loan Advances and Bill Purchased

This is a primary source of income and most profitable asset to a bank. The sum outstanding of all loans and advances extended to the customers as well as bills purchase and discounted bills less the amount of provisions made shall be exhibited. However, the loans extended to the staffs shall not be disclosed under this head and should be shown under other assets.

vi) Fixed Assets

All assets of long-term nature owned by the bank (land &building, machinery, vehicles, office equipments etc) shall be accounted under this head and be exhibited in the balance sheet at written down value after deducting the depreciation from the total cost.

vii) Other Assets

The heading shall be used for accounting of any other tangible or intangible assets, not mentioned above. Stationery stock, accrued interest on investment, accrued on loan, sundry debtors, assets in transit, non-banking assets, expenses not written off etc.

B. Profit & Loss Account

The bank's profit &loss account is composed of interest, administrative expenses, provision for possible losses, bonus provision, tax provision, investment provision, etc. as expenses and interest, discount, commission, charges etc, as incomes. The summary of the heads of account in the profit and loss account in the profit and loss account of a commercial bank is given below.

a) Expenses Side

i) Interest Expenses

Payment of interest on deposits accepted by the bank and on the borrowings is shown under this head. Interest is regularly expensed off for various deposits; interbank borrowings, central bank borrowings and other external obligations.

ii) Employee expenses

All expenses related to the employees of the bank for the specific period shall be included under this head. Expenses included are salary, allowances, pension, gratuity, training expenses, uniform expenses etc.

iii) Office Overhead Expenses

All expenses related to the office overhead of the bank during the specific period shall be included under this head. Some of the expenses under this head are house rent, insurance, audit expenses, newspapers and magazines, advertisement etc.

iv) Exchange loss

The negative balance in exchange fluctuation gain/loss account shall be exhibited under this head.

v) Non-Operating Expenses

These are the expenses that have no direct relationship with the operation of banking transaction. Some of the examples are loss on sale of investment and on sale of assets.

vi) Bad debts written off

Where the bank has written off loans on account of being unrecoverable, such written off amount to the extent not covered by loan loss provision shall be charged to profit and loss account under this head.

vii) Provision for Possible Loss

This is one of the most important heads of account related to the profitability of bank. As per the directive of the Nepal Rastra Bank, the banks are required to make provision for loan losses. The provisions are to be made on the basis of the expiry dates on the principal amount of the loans and advances. As per the directive the provisions to be made is as follows.

However, in case of bills purchased items, provision is to be provided at 1% if it stands due for 90 days and in case it remains due for more than 90 days 100% provision is required. *(NRB;2005:36)*

viii) Provision Staff Bonus

The amount of bonus set aside for payment to staffs is disclosed under this head. As per the Nepal Rastra Bank directives the bank is entitled to make provision for the staff bonus at 10 % on the net profit after adjustment for loan loss provision.

ix) Provision for Income Tax

The amount of income tax on net taxable profit for the period shall be determined through this head. Taxable profit has to be determined considering the allowable and disallowable expenses as per the prevailing income tax act and finance bill.

x) Net Profit

This figure represents the excess of total income over total expenses of the bank during the period.

b) Income side

i) Interest Income

This is the primary source of income of any commercial bank. Under this head the interest received from the customers on behalf of the loans and advances and on the investments of the bank is exhibited. However, Nepal Rastra Bank has established several criteria for the recognition as interest income.

- The interest income should be recognized on cash basis.
- The amount of interest accrued but not received; have to be credited to the interest suspense account.
- In cast of the interest accrued is realized within one month from the date of closure of fiscal year, such amount may be recognized in the income of the earlier fiscal year.

- The interest on loans and advances should not be recovered by overdrawing the borrower's current account or where overdraft limit has been extended by overdrawing such limit.

ii) Commission & Discounts

The total amount of commission, service charges and discount earned by the bank from the transactions during the period shall be exhibited under this head. Some examples are commission on issue of guarantees, commissions on issuance of L/C etc.

iii) Exchange Gain

Banks deal with foreign currencies. Foreign currencies are remitted outwards and inwards. Banks involve in trade while dealing this transaction. Banks make trading gain while selling and buying foreign currency stocks for their trade as well as banks gain from revaluation the stock whenever the exchange rates are in their favor. Both the trading gain and revaluation gain are exhibited under this head.

iv) Non- Operating Income

Income or profit that has no direct relationship with the operation of banking transaction has to be recognized into profit and loss account under this head. These incomes are casual source of income and are not from regular course of business but from sources where the business entity can be involved legally as prescribed by the directives if related government authority. Nepalese commercial banks are allowed to invest in the share of another entity like other commercial banks, rural development banks, financial institution and other government institutions. The investing bank receives dividend income and other income.

v) Other Income

Receipts of all other income not specifically provided under the income heads as above shall be booked under this head e.g. rental income of safe deposit boxes, income from telex, service charge, renewal charges etc.

vi) Net Loss

The figure represents the excess of total expenses over total income of the bank during the period.

2.2 Review of Related Studies

2.2.1 Review of Journals and Articles

Dhungana (2005), *"Problem encountered by the Nepalese financial system"*,NRB Samachar, Annual Publication, 2005,highlighted the major weakness of the banking sector, mainly of RBB and NBL. According to the writer, the financial sector is dominated by banking sector and which in turn, is dominated by two old government owned banks. These two banks constitute the largest component of total deposit of banking system. These two banks suffer from various problems, which results the unsound health of the banking industry of Nepal. The major weaknesses of these banks are

- Concentration of loan to limited borrowers
- Large number of branches with limited transaction
- Inefficient staff and absence of manpower development and planning
- Poor supervision and follow up after credit disbursement
- Insufficient records and bookkeeping
- No application of modern banking equipments in bank branches

To improve the productivity and quality of banking sector the authorities have created a new environment given raise to JVBs.

Panthi (2005), "*The importance of human resource management",* RBB Newsletter VOL 6. September 2005, highlights that the human resources management always plays key role in a commercial bank like RBB where the banking services are only made by human skills, if the size of the employees is suitable and skillful, the optimum objectives of the bank will be nearer to achievement. The objectives of the profitability and the liquidity of the bank may be fulfilled if and only if its human resources are perfect in and suitable in quality. So, the selecting process of human resources should go through the straightway of identifying workforce requirement, Recruiting - Selecting- Placement-Promotion-Apprasing-Training and Retirement.

An article published in **Kantipur Daily, July 06, 2007,***"Results of FSR are Encouraging: NRB Governor"* the governor of Nepal Rastra Bank (NRB) Bijaynath Bhattrai has said the achievements of financial sector reform programs till now are encouraging. He informed that reforms in Rastriya Banijya Bank (RBB) and Nepal Bank Limited (NBL) have resulted in profits there. Till the end of 2006, NBL has earned operating profit of Rs 3.84 billion while RBB has earned operating profit of Rs 5.3 billion. Government had invited foreign management to look after these financially bankrupt state-owned banks. They were running in loss before the foreign management took over. Bhattrai said data will help better understand the importance of reforms. On Wednesday, senior political leaders had said the reforms were unsuccessful and said the foreign management should not be renewed. In the four year period, Rs 824.3 million and Rs480 million have been spent on foreign management group in NBL and RBB, respectively.

An article published in, **New Business Age August 2008,** "*Banks & Profit"*,highlights about the increase in reserve and surplus of all banks with the exception of Nepal SBI, Global and NB Bank. Overall deposits in the banking sector have increased by 25 percent with increase in deposits of all the banks except Lumbini. Government banks such as RBB, NBL and ADB have the highest diposits followed by Nepal Investment Bank Ltd. (NIBL), Himalayan Bank Ltd.(HBL), Nabil Bank and SCBN. NIBL has surpassed the deposit of ADB in the current fiscal year 2007-2008. Deposits in Laxmi, Siddhartha, Global and Citizens Banks have substantially increased by 43 percent,55 percent, 142 percent and 295 percent respectively. There has been an increase in overall interest income because of overall increase in loans and advances. ADB, RBB, NBL, Nabil,NIBL and HBL have the highest interest income. Among these banks, NBL has lowest loans and advances but have highest interest income. NBL, RBB, and NB bank have negative capital adequacy ratio (CAR) but it has improved compared to last year in NBL and RBB which it deteriorated in NB Bank. NPL to total loan ratio of all these banks has reduced. Laxmi, Siddhartha, Everest, Nabil, NIC and SCBNL have the lowest NPL to total loan ratio while NB Bank, RBB, NCC Bank and Lumbini Bank have the highest ratio.

Dhungana (2008),"*Financial sector reform program (FSRP) in Nepal*" RBB Newsletter Vol 6. September 2008, has concluded that Nepalese financial sector is being strengthened under the financial reform program. The expediting of the liberalization and privatization processes within the financial reform programs has succeeded to place the private sector rather than the government in charge of determining who gets credit and at what price. The FSRP has also been able to establish the system of prudential regulation and supervision design to restrain the private actors so that we can reasonably sure that their decisions will also be broadly in the general social interest. Many Acts are being promulgated to obtain and maintain a strong legal environment required for the system. It is also equally and important that the enforcement aspect in all respects plays a vital role, which is continuously improving. Within this reform program the two largest commercial banks NBL and RBB are being restructured, institutional building program are being lunched, greater autonomy and responsibility have been provided to the central bank, entry and exit norms are being prepared, laws are being prepared, laws are being prepared for the banking sector. These all are positive aspects to boost up the system. It has been widely recognized that

- Less government involvement in the financial sector
- A strong central bank, a strong banking environment
- Adequate banking services to the poor
- Adequate legal frame work and enforcement of law

are six basic pillars for the development of the healthy financial architecture. The government has launched this program to eliminate financial problems. Except some aspects, the progress made within the FSRP seems are satisfactory.

An article published in **New Business Age, September 2009** entitled *"All Banks in Profit",* focused that in general all banks for the fiscal year 2003-2004 A.D. are bullish in their performance. During the year all the banks were in profit but in the previous year two commercial bank, NBL and RBB were in a loss of 202 million and 3246 million respectively. NBL, RBB, Siddhartha Bank, Laxmi Bank, kumari Bank and Machapuchhare Bank have increased their operating profit in substantial amount. Also the old banks with huge losses in the previous year's NBL and RBB have succeeded to improve their performance.

Shrestha (2011), "*Liquidity crunch Govt. banks new lenders"* an article published in Kantipur daily, has concluded that the liquidity crisis has the private sector banks especially, and borrowers are thronging government- owned banks as private banks have failed to provide credit. Rastriya Banijya Bank(RBB) and Nepal Bank Limited (NBL) are getting a rising number of applications for credit in recent days. The concerned banks officials said they were facing pressure for additional credit from an increasing number of borrowers who used to deal with other banks. The liquidity situation of the government banks is relatively better compared to private ones although government banks also are facing pressure with no growth in deposits in recent months. Till mid- March, the liquidity-deposit ratio of commercial banks declined to 29.3 percent from 34.2 percent in mid-July 2009, showing the declining liquidity situation of the banks. The rise of credit-deposit ratio to 90.2 percent during the first eight months of the current fiscal from 81.2 percent in mid-July 2010 shows the shrinking liquidity situation.

Pradhan(2012), an article published in Aviyan Dainik,*"Crisis impact delayed here: IMF –International Monetary Fund"* has said Nepal's economy is experiencing a delayed impact of the global economic crisis. The IMF's Article IV report prepared by the IMF mission after its visit to Nepal in March, says, After years of macroeconomic stability, Nepal's economy is experiencing a substantial, albeit somewhat delayed, impact of the global crisis, which is exposing the country's structural weaknesses. The IMF said external and financial sector risks have risen in Nepal. "External and financial sector risks have risen as evidenced by the significant deterioration of the current account, the reserve decline, wavering confidence, and banking sector liquidity stress," states the IMF report. Liquidity risk and exposure to the real estate sector, the IMF suggested not to add more financial institutions in the country. "Bank licensing policy needs to be tightened and financial sector consolidation facilitated," the report added. The central bank has stopped entertaining applications for commercial bank licenses since the past one year. However, it has been facing mounting pressure to open up the process. With the government not able to appoint the chief executive of Nepal

Bank Limited (NBL) and Rastriya Banijya Bank (RBB), the IMF has asked Nepali authorities to proceed with the restructuring of these two banks. As of now, the central bank appointee is managing the NBL, while the tenure of the RBB chief executive is ending in mid- July. The IMF has also asked the authorities to expand regulatory oversight over savings and credit cooperatives. Around 6500 savings and credit cooperatives in the country are said to be mobilizing Rs 78 billion of deposits. A recent government study on 10 big savings and credit co-operatives revealed that they lacked transparency and were controlled by family members.

Joshi (2012), an article published on Nepal Rastra Bank Samachar as *"Problem in Nepalese Finacial Sector"* has said Nepalese BFIs has been grown over the years despite numerous challenges. At the same time, it also has various opportunities that can be explored. By becoming a member of the WTO, Nepal has opened its market for foreign banks to set up their branch from the beginning 2010 which will help to enter foreign investment and technology in the banking sector

The banking sector of Nepal is facing liquidity problem, slow-moving economy and various other macro and micro economic factors. The effect of global financial crisis of 2007-2008 has strike the Nepali banking sector as well. The opportunities can be created for the banking sector by strengthening the regulatory system and improving the implementation of new standards of capital, liquidity and risk management.

Currently, the major challenge for the banking sector is to improve the worsening liquidity problem which directly affects the operation of banks, the one of the contributing factor of liquidity problem is higher loan investment made by banks as compared to the deposits. The liquidity crisis leads to decline in private sector credit, whereas growth in the private sector credit is essential to create economic activities. Recently, there is high competition among the banks to increase deposits out of the same money which is in the system. In this process the banks are creating unfriendly competition and further aggravating the problem. Thus, it is required to convey a positive message to the depositors to win back their trust in the banking sector for all BFIs. Further, the existing level of Non- Performing Assets (NPA) is not a good sign for smooth growth of the Nepalese banking sector. Therefore, it is required to reduce NPAs with proper implementation prudent strategy. One of the measure causes of current distress of BFI in Nepal is due to the higher injection of real estate loan. It is essential to reduce the real estate exposure and increase the productive sector credit to create more economic activities.

2.2.2 Review of Previous Thesis

Bhattarai (2010) in her study "*Evaluation of Financial Performance of Nepal Bank Limited In the Comparision of Bassel II and Industry Average*" stated the objectives as follows:

- Analyzing financial performance of NBL by calculating the value of different financial indicators.
- Comparing the financial performance of the NBL with the banking industry average. The value ascertained of financial indicators shall be used to compare the financial performance of NBL with banking industry average. Such types of comparison with banking industry would help to track out the financial strength and weakness of the bank.
- Comparison of financial position of NBL with the Bessel II accord.

In her study, she has found & concluded as follows:

- The CD ratio of NBL is quite lower than banking industry average. The restult of productivity indicators of NBL is not satisfactory, over staffing in outed in head count.
- Deposit mix of NBL is dominated by intrest bearing deposit, non intrest income to total assets ratio of the NBL is highly unsatisfactory during the tenure of ICCMT the ratio was littlebit satisfactory, cost of fund of NBL is highly satisfactory.
- Shareholder position of NBL is very unsatisfactory or negative net worth as well as capital adequacy ratio of NBL is negative. CAR of NBL indicates the worst financial position of the required CAR as per Bessel II is 10% but NBL has negative CAR i.e. 13.45%.
- Similarly improper portfolio management also remains one of the significant problems in credit management of commercial bank. Average spread rate of NBL is 4.5% and the figure is better than of industry average.
- And her study she has fount negative value of NPA to net total loan ratio depict the position of NBL has sufficient amount aside from total operating revenue to cover the losses occurred due to bad loan.

Kafle (2010), completed the study on *"Financial Performance of Nepal Bank Ltd*". Main objective of this thesis is to analyze and evaluate the financial operation and the financial statement of Nepal Bank Ltd. Therefore, to attain the mentioned objective, following specific objectives have been set:

- To seefinancial performance of NBL in terms of liquidity position and other financial indicators.
- To see activity and operation with reference to collection, mobilizationand trend of deposit.

- To see the earning and profitability position.
- To see the relationship between total deposit and total investment.
- To observe return over the period.

Major Findings are as follows:

- Liquidity position of NBL is in sound condition. The cash and bank balance to total deposit raio is an average19.60%,. The fluctuation on mean value or SD of cash and bank balance to total deposit ratio is 12.68. In this reason the liquidity position is sound and high level compared to the directives prescribed by NRB where, NRB minimum requirement is 6.5% of total deposit for commercial bank. Cash and bank balance to current deposit ratio is 93.65 an average. The SD of this ratio is 10.40.
- The CD ratio of NBL is quite lower than banking industry average. NRB has instructed to maintain CD ratio to the maximum 80% the CD ratio of NBL just about 41.87% ,on average as well as SD of this ratio is 8.81, but it was improving the last year the ratio is around 58%.
- The position of net loan to total assets indicates that NBL has low level of loan assets balaance sheet the ratio is an average 40.88% & SD of this ratio is 7.96. Loan is earning assets other is non earning assets, high volume of non earning assets in assets mix leads to poor profitability.
- During the year 2006 gross NPA percentage was 18.18 and it was decrease on to 4.87% on 2010. After the holding of bank management by ICCMT the ratio has been improved.
- In the study period the highest return on assets ratio is 3.4% in the fiscal year 2005/06 and lowest ratio is 0.57% in the fiscal year 2007/08. In an average the ratio remains at 1.35%. The fluctuation on the mean value or SD of this ratio is 1.069.

Pandey (2010), has conducted a study on *"An analysis of Key Financial Ratio of Commercial Banks in Nepal: A Special Reference with Himalayan Bank Ltd and Everest Bank Ltd."* The main objective of this study was to find out exact financial ratio of these two commercial banks over the periods of time. He had taken Everest Bank Limited and Himalayan Bank Limited as sample. Mainly he had conducted this research based on secondary data available in both banks annual reports and manuals. He had presented data using both financial and statistical tools in his study.

Specific Objectives are as follows:

- To examine the overall financial ratio of the selected commercial bank.
- To examine the financial performance.
- To recommend the appropriate suggestion to concerned authority.

Major finding are as follows:

- Current ratio of both of the banks showed consistent trend. Both the banks could not maintain the conventional standard of 2:1
- EBL has higher average ratio which implies that EBL is more capable to meet short term obligation in comparison to HBL.
- Normally, the ratio remained consistent in HBL but the ratio of EBL is fluctuated more which is reflected by higher standard deviation.
- Both the selected banks were successful to mobilize their fund as loan and advance with respect to total assets. However, EBL has higher mean ratio than HBL over the study period which implies that EBL can be taken as better investor than HBL as concerned to consistency, both the sample banks able to maintain consistency.

- According to the analysis of assets management ratio, both the banks were successful in on –balance sheet utilization. Out of these two banks, EBL is found to be best in mobilizing the assets to the profitable sector.
- By analyzing the valuation ratio of selected bank, market value of EBL was higher position than HBL. Total deposits and loan and advances of both the bank were almost positively perfect correlated. Correlation coefficient between total deposit and total investment of both the banks were more than 0.5 with positive sign, which means investment will increase proportionally with the increment in total deposit.
- The trend analysis of EBL was better than that of HBL in all the cases. The growth rate of total deposit, total loan and advance, total investment and total net profit of EBL is higher than that of HBL.

Dahal (2011) conducted the study on *"Comparative Study of the Profitability Analysis(A case study of Nepal SBI Bank Ltd & Himalayan Bank Ltd)"* has the following objective:

- To evaluate the profitability and financial position.
- To evaluate the impact of deposit on profit.
- To evaluate the impact of loan and advances on profitability.
- To analysis the income and expenditure, cost and profit trends of the banks.
- To provide suggestion, recommendation and practical idea for improving competitiveness and strength.

In her study, she has found & concluded as follows:

- The liquidity position of HBL is comparatively not better than that of NSBI Bank. It has the lowest current ratio, cash and bank balance to the toal deposit ratio. The liquidity ratios of HBL bank which indicates the stable policy of Himalayan Bank has not made enough cash and bank balance while NSBI Bank has not good deposit collection in comparision to HBL.

- The profitability position of NSBI bank is comparatively not better than that of HBL. The bank has followed moderate position in comparation to other banks.
- Through the trend analysis it is found that the deposit collection position, lending position, investment position and net profit position HBL is better than NSBI Bank except in the case of EPS. Because the trend value of EPS of HBL Bank is declining.
- The Interest Spread is the difference between the buying and selling rates of the fund. The rate of Interest Spread has significant importance in the aspect of profitability. Interest spread of NSBI was found marginally higher than that of HBL. It can be concluded that interest expenses covered more portion in NSBI Bank compared in HBL. It may be the result of their success to attract the depositors due to higher rate of interest.
- Organization itself does nothing but their success or failure is mainly basede upon their employee, efficient and well motivated staffs, are the ornaments of any organization. HBL's staff expenses per employee is very high than that of NSBI Bank. Moreover, there are more staffs working in HBL Bank. In this way staff expenses includes as the expenses made upon their employees such as salary and allowance, training, uniform, and other contribution to provident fund. Intensive fringe benefit etc. NSBI Bank should care more to its staff in future.

Lama (2012), conducted the study on *"Profitability of Nabil Bank Ltd. with Comparision to Other J/V Banks"*

The main objective of the study are:

- To examine the profitability situation of the JV bank industry as a whole and sample banks.
- To analyze the profitability trend of Nabil Bank and the JV bank industry the over the last five years.
- To ascertain the comparative position of profitability of Nabil Bank with respect to other JV banks.

The study concluded that

- Nabil had the second highest net profit and EPS followed by HBL, EBL & NSBI. The profitability ratio of SCBNL were the best among all. Nabil had utilized its assets more efficiently in generating income.
- Nabil was found the efficient in mobilizing its total deposit and the quality of extended credit was the moderate for Nabil.
- Based on overall performance assets mobilization, profitability ratios, quality of the lending, and market prices. Nabil occupied the second position and the SCBNL occupied the leading and the highest position among the other joint venture banks.
- Nabil bank is performing well above of the industry standard but also has highest performance among all players in the JV Bank Industry in Nepal. In conclusion, Nabil Bank's past and present earning generating potential is assessed as high in every parameters of profitability in comparision to the industry as well as other joint venture banks in the country.

2.3 Research Gap

Research Gap is the difference between previous works done and the present research works. Lots of study has been conducted to analyze the profitability position of the commercial banks. But the main theme of this research is to analyze the profitability position and operating financial efficiency of Rastriya Banijya Bank and Nepal Bank Ltd. Recent data and information of both banks have been used in this study. This research covers the five years period of the banks operation after the implementation of the FSRP and clarifies the progress operating under FSRP.

Commercial banks invest its deposit in different profitable sectors according to the directives and circulars of the Nepal Rastra Bank and the guidelines and policies of their own bank. The policy of Nepal Rastra Bank is being changed time to time. So the updated study over the change of time frame is major concern for the researchers and concerned organizations as well. The study is based on the more recent financial data.

The study differs itself from others research by specially focusing on the profitability of Rastriya Banijya Bank and Nepal Bank Ltd. and covers the period of F.Y 2007/08 to 2011/12. This research therefore will facilitate readers to identify the profitability position and operating financial efficiency of Rastriya Banijya Bank and Nepal Bank Ltd. which will help to evaluate past and present performance of both the banks as well as it will help to project future prospect of both banks.

CHAPTER – III

RESEARCH METHODOLOGY

Research is the process of a systematic and in depth study or search of any particular topic, subject or of investigation backed by the collection, presentation and interpretation of relevant details or data. Research methodology is a way to solve the research problem systematically. This is the steps, guidelines and tools used in the research by the researcher. It considers the logic behind the methods used in the context of research study and explains why particular method or technique is used. It highlights about how the research problem has been defined, what data have been collected, what particular method has been adopted, why the hypothesis has been formulated etc. Really, it is one of the most important parts of the research which provides outlines of the research and also present method and process of entire research.

3.1 Research Design

Research design is a conceptual framework within a researcher conducted. Research design is plan for the collection and analysis of data. It presents the series of guide posts enable the researcher to progress in the right direction in order to achieve the goal. The design may be a specific presentation of the various steps in the research process. These steps include the selection of a research problem, presentation of the problem, formulation of hypothesis, conceptual clarity and methodology, survey of literature and documentation, bibliography, data collection, testing of hypothesis, interpretation, presentation and report writing. Generally, a common research design possesses the five basic elements viz. (i) selection of problem (ii) methodology are used (iii) data gathering (iv) data analysis and (v) report writing.

Research design of the study is descriptive as well as analytical research design. Financial and statistical tools have been used for analytical purpose. This process of investigation involves a series of well throughout activities of gathering, recording, analyzing and interpreting the data with the purpose of finding answers to the problem. The main objective of the study is to analyze the profitability of the Nepal Bank Ltd. and Rastriya Banijya Bank. The study depended on the secondary data. The study is designed as to give a clear picture of the bank's profitability with the help of available data and with some useful suggestion and recommendation.

3.2 Population and Sample

The population for this study comprises all the license commercial banks of the country. A list of licensed commercial bank was obtained from NRB. There are altogether 32 commerial banks in Nepal. Out of them, 18 banks have crossed five year annual general meeting. Out of these 18 banks, 2 banks selected as sample for the study by using judgemental sampling method.

Table 3.1

Population and Sample

Population	**Samples**
32 commercial banks	1.Rastriya Banijya Bank (RBB) 2. Nepal Bank Limited (NBL)

Population comprises of the data published by the concerned authority or institution to make the descriptive and analytical study. For the analytical part, sample of data should be taken into consideration within which the analysis and evaluation is made. For, this purpose the study has taken a sample data of recent five year's financial statement.

3.3 Source of Data

The researcher can use two methods of data collection i.e. Primary and Secondary data. Primary data are the data collected directly from the site. It can be called as first hand data. These data are very reliable if researcher can reach the correct destination with required tools. Secondary data are second hand data collected from different other sources such as magazines, newspapers, journals, second persons, etc. here only the secondary data is used for the study. The study is based on secondary data. All the data are collected from the respective commercial bank's annual reports especially from profit and loss accounts, balance sheet and other publications made by the banks, which are the secondary data.

Further, secondary source of data are presented as under:

- Annual reports of Rastriya Banijya Bank and Nepal Bank Ltd.
- Financial statistics of Nepal Rastra Bank
- Unpublished official records
- Other published journals of RBB and NBL
- Various published and unpublished Nepalese thesis
- Text books of different writers
- Various related websites
- Laws, guidelines and directives regarding the subject matters etc

3.4 Data Processing Technique

After the necessary data has been collected, relevant facts and figure have to be tabulated under the different headings. Such tables and formats are to be interpreted and explained as required. Different tools and techniques are used to interpret and explain the data. Scientific calculator and simple Microcomputer has been used to compute data.

3.5 Data Analysis Tools

Various statistical and financial tools are used in this study. Wide varieties of methodology have been applied accouting to the reliability and consistency of data before using the analytical tools to compare the result, the data containing in the financial statements have been grouped and rear ranged so as to make comparion easy. For the purpose of analysis the data of five years were taken as sample from 07/08 to 11/12. The data are analyzed financially and statistically. The calculated results are also tabulated under different heading for ease of reading, and then they are compared with each other to interpret results. To make the study more specific and reliable, the researcher uses two types of tools for analysis.

- Financial tools
- Statistical tools

3.5.1 Financial tools

“This study is to Comparative Financial Analysis. So, financial tools are more useful. They help to identify the financial strengths and weaknesses of the firm. In spite of various financial tools available, the research has primarily stressed on ratio analysis assuming it to be the most suitable one. A ratio is a number expressed in terms of other number and it expresses quantitative relation between any two variables.”*(Kothari;1996:187)*

Financial tools are used to examine the financial strength and weakness of bank. Financial statements such as balance sheet and profit and loss account can be analyzed to assess the financial health of the bank. In this study, financial tools like ratio analysis were used.

A. Ratio Analysis

Financial ratio is the mathematical relationship between two accounting figures. Ratio analysis is a part of the whole process of analysis of financial statements of any business or industrial concern especially to take output and credit decisions. Thus, ratio analysis is used to compare the firm's financial performance and status to that of other firm's or to itself over time. The qualitative judgment regarding financial performance of a firm can be done with the help of ratio analysis.

Ratio is the expression of one figure in terms of another. It is the expression of the relationship between mutually independent figures. It is a simple mathematical expression of the relationship of one item with another. Absolute figures alone convey no meaning unless they are compared to each other. Accounting ratios show the interrelationship existed among various accounting data *(Munankarmi;2003:12.04).*

The relationship between two numerical figures expressed mathematically is known as ratio. Similarly, analysis of the relationship between various items of financial statements is called financial ratio analysis which helps to summarize the large quantity of financial data and to make qualitative judgments about the firm's financial performance. Financial ratio reflects the quantitative relationship which helps the manager to take qualitative judgments. *(Shrestha;2008:57)*

There are various types of ratios that can be used to analyze the financial performance of the firm. Here, in this research only the relevant ratios are used to find the financial position of RBB and NBL

A.Profitability Ratios

Profitability ratios are designed to highlight the end-result of the business activities, which in the imperfect world of ours, is the sole criterion of cover all efficiency of business unit. A company should earn profit to survive and grow over a long period. It is a fact that sufficient profit must be earned to sustain the operations of the business, to able to obtain funds from investors for the welfare of society. The profitability ratios are calculated to measure the operating efficiency of the company. Management of the company, creditors and owners are interested in the profitability of the firm. Creditors want to get interest and repayment of principal regularly. Owners want to get a reasonable return from their investment.

Profitability ratios are used to measure the efficiency of operation of a firm in terms of profit. It is the indicator of the financial performance of any institution. This implies that higher the profitability ratios, better the financial performance of bank and vice versa.

The profitability of Nepal Bank Ltd. and Rastriya Banijya Bank is evaluated through following different rations;

a) Net Profit Margin

The ratio measures the overall profitability of the firm by establishing relationship between net profit and total income indicates management's ability to operate the bank with sufficient success not only to recover the interest expenses/operation expenses of bank but also to leave a margin of reasonable compensation to the owners for providing their capital at risk. This ratio is calculated by dividing the net profit by the total operating income and it is expressed as percentage as follows:

$$\text{Net Profit Margin (NPM)} = \frac{\text{Net Profit After Tax}}{\text{Total Operating Income}}$$

b) Return on Total Assets (ROTA)

Return refers the profit after interest and taxes. It is also known as Net Profit on Total Assets. These ratios evaluate the efficiency of company in utilizing and mobilizing of assets and its survival. It is useful for measurement of the profitability of all financial resources invested in the bank assets. It also provides the foundation necessary for company to deliver a good return on equity. Higher return on Assets (ROA) indicates higher efficiency in utilization of total assets and vice-versa. ROA is calculated by dividing the amount of net profit by the total assets.

$$\text{Return on Total Assets (ROTA)} = \frac{\text{Net Profit After Tax}}{\text{Total Assets}}$$

c) Return on Equity (ROE)

The shareholders are true owners of the bank and thus the profit belongs to them. Return on equity measures the rate of return on shareholder's investment. It indicates the profitability of the owner's investments. This is the most commonly used ratio for measuring the return on owner's investment and is calculated as follow:

$$\text{Return on Equity (ROE)} = \frac{\text{Net Profit After Tax}}{\text{Shareholders Equity}}$$

d) Operating Efficiency Ratio

The bank during its operation has to undergo various expenses. Some of the expenses are rent, insurance, depreciation, postage, telephone, electricity, advertisement etc. This ratio shows the proportion of operating expenses on the total operating income of the year. To maximize profitability and the value of the shareholder's investments in the bank, bank management must maintain efficiency in their operations. This usually means reducing their operating expenses and increasing the productivity of their employees. Lower the ratio means greater the success of management.

$$\text{Operating Efficiency Ratio} = \frac{\text{Total Operating Expenses}}{\text{Total Operating Income}}$$

e) Return on Capital Employed

The ratio measures management efficiency on how well the total fund including external funds were used to generate profit. This ratio provides a test of profitability in relation to long term fund. Higher ROCE implies more efficiency in utilizing the capital employed.

$$\text{Return on Capital Employed} = \frac{\text{Net Profit After Tax}}{\text{Total External Capital}}$$

f) Interest Payout Ratio

We are well aware that the main function of a bank is to collect deposit and advance loans. The bank pays interest on the deposits and charges interest on the loans and advances. It also realizes income from the investments and call deposits. Similarly, the ratio provides the proportion of interest payment of the bank as compared to the interest income generated by the bank.

$$\text{Interest Payout Ratio} = \frac{\text{Interest Expenses}}{\text{Interest Income}}$$

g) Net Operating Margin

This is also to measure operating efficiency of commercial banks. The net operating margin of commercial banks signifies what portion of operating profit remains after deducting all operating costs. Higher the margin, the better is the efficiency of the management.

$$\text{Net Operating Margin} = \frac{\text{Total Operaing Revenue} - \text{Total Operating Expenses}}{\text{Total Earning Assets}}$$

B. Income Expenses Analysis

a) Interest Income to Total Income

Total interest earned to total income ratio indicates the extent to which the bank has successfully mobilize its fund in interest earning asset. Higher ratio indicates higher performance. This ratio can be calculated as follows.

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

b) Fee and Commission Income to Total Income

The major source of income of the Nepalese commercial banks is fee income. Commercial banks now-a-days have moved towards the near banking agency services like underwritings, counseling, various service charges, renewal fees and other consultancy functions. They have expose to non-funded fee based services like LC, guarantee, bills/clearing, safe deposit, credit card, ATM, etc. from these services banks earn fees and commission.

$$\text{Fee \& Commission Income to Total Income} = \frac{\text{Fee \& Commission}}{\text{Total Income}}$$

c) Interest Expenses to Total Operating Expenses

Commercial bank’s major expenses head is interest expenses. Interest expenses incurred on various saving and fixed account, inter bank borrowings, borrowings from NRB and from other foreign banks. These borrowings are the input of the bank. These provide banks higher interest spread to get more profitability. Therefore, lower the cost of deposits and borrowing cause higher profitability. An objective of calculation of this ratio is to know about the portion of interest expenses incurred. In the other word, to know about the portion of interest occurred by the bank as a whole expenses. This ratio is also presented in percentage and is calculated by the following formula:

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

d) Staff Expenses to Total Operating Expenses

In a service industry, the importance of the human element cannot be ignored. The service organizations have to keep their employees satisfied. Although cost minimization is one way to maximize the profits, the minimum level of staff expenses can work other way round. Unmotivated and unsatisfied workforce can be highly inefficient and unproductive in their work thereby affecting the profitability of the organization. Thus, the perks and benefits should be designed at an appropriate level keeping both the organization and staff satisfied. The ratio provides the average staff expenses out of total operating expenses.

$$\text{Staff Expenses to Total Operating Expenses} = \frac{\text{Total Staff Expenses}}{\text{Total Operating Expenses}}$$

e) Office Operating Expenses to Total Expenses

Office operating expenses comprises expenses incurred in house rent, electricity, water, repair and maintenance of various fixed assets, insurance, stationary, telex, telephone, advertisements, legal expenses, expenses relating to board of directors, expenses relating to board of audit, depreciation, amortization, professional service fee, security expenses, commission and discount and other.

$$\text{Office Operating Expenses to Total Expenses} = \frac{\text{Office Operating Expenses}}{\text{Total Expenses}}$$

3.5.2 Statistical Tools

Statiscal tools are the mathematical techniques used to analyze and interpret performance. It is used to describe the relationship between variables and interpret the result. Statistics is also used to test the hypothesis that is set to know the information of population.

3.5.2.1 Mean/Average $\overline{(x)}$

The arithmetic mean or average is the sum of total values to the number of observations in the sample. It represents the entire data which lies almost between the two extremes. For this reason an average is frequently referred to as a measure of central tendency. An average is the typical value around which other items of distribution congregate. Arithmetic mean of a given set of observation is their sum divided by the number of observations. In general X1, X2, X3…..Xn are the given observations then their arithmetic mean, usually denoted by $\bar{x}$

Symbolically,

Arithmetic mean, $\bar{x} = \frac{x1+x2+x3+\cdots+xn}{n}$

$$\bar{x} = \frac{\sum x}{n}$$

Where,

$\bar{x}$ = arithmetic mean

x1, x2, x3,………………, xn = values of the variable

∑x = sum of the values of the variables x

n = number of observation

3.5.2.2 Trend Analysis

The arrangement of statistical data chronologically (according to occurance of time) is known as time series and the statistical analysis of this chronological variation is termed as Trend Analysis. It helps to know the past behavior of data in certain span of days. This least square method is the most popular and widely used mathematical method of measuring trend. This is frequently used for future prediction. There are various types of curves that may be used to describe the given data but in this text, an attempt has been made to discuss only the fitting of linear trend by the least square method.

Let, the equation of Trend Analysis would be

$Y = a + bx$

Where,

Y=the given value of the variable in time series. It is a dependent variable.
a= Intercept of trend line or y- intercept
b=Slope of Trend Line
x= Time variable

CAHPTER – IV

PRESENTATION AND ANALYSIS OF DATA

Introduction, review of literature and research methodology are presented in the previous chapters and they preceded the basic inputs to analyze and interpret the data. In this chapter, collected data are analyzed and interpreted according to the methodology presented in the previous chapters. This chapter presents the data and facts, which are related to different aspects of Rastriya Banijya Bank and Nepal Bank Ltd. The included data are collected from various sources. These available data are tabulated, analyzed and interpreted so that financial forecast of banks can be done easily. The main objective of analyzing the financial performance and interpretation is to highlight the strengths and weakness of the banks. The collected data are analyzed and interpreted by using the various financial and statistical tools.

4.1 Ratio Analysis

A. Profitability Ratio

The ultimate objective of banks is to earn profit. Strictly speaking, no bank can survive without profit. Profit is the indicator of efficient operation of bank. The bank acquires profit by providing different services to its customers or by making investment of different kinds.

Sufficient profit is a must to have good liquidity, grab investment opportunities, expand banking transaction, finance government in need of development fund, overcome the future contingencies and meet fixed internal obligation for the bank. Profitability ratios measure the efficiency of a bank. The following profitability ratios were used to evaluate the profitability of the selected commercial banks.

4.1.1) Net Profit Margin

The ratio signifies the effectiveness of expenses management and cost control and gives the direction to the management for service pricing policies. It means how much of total revenue hasbeen declared as net profit after all the charges are over up. The higher ratio means the management has been able to control its operational costs and maintain efficiency.

$$\text{Net Profit Margin} = \frac{\text{Net Profit After Tax}}{\text{Total Operating Income}}$$

Table:4.1

Net Profit Margin (%)

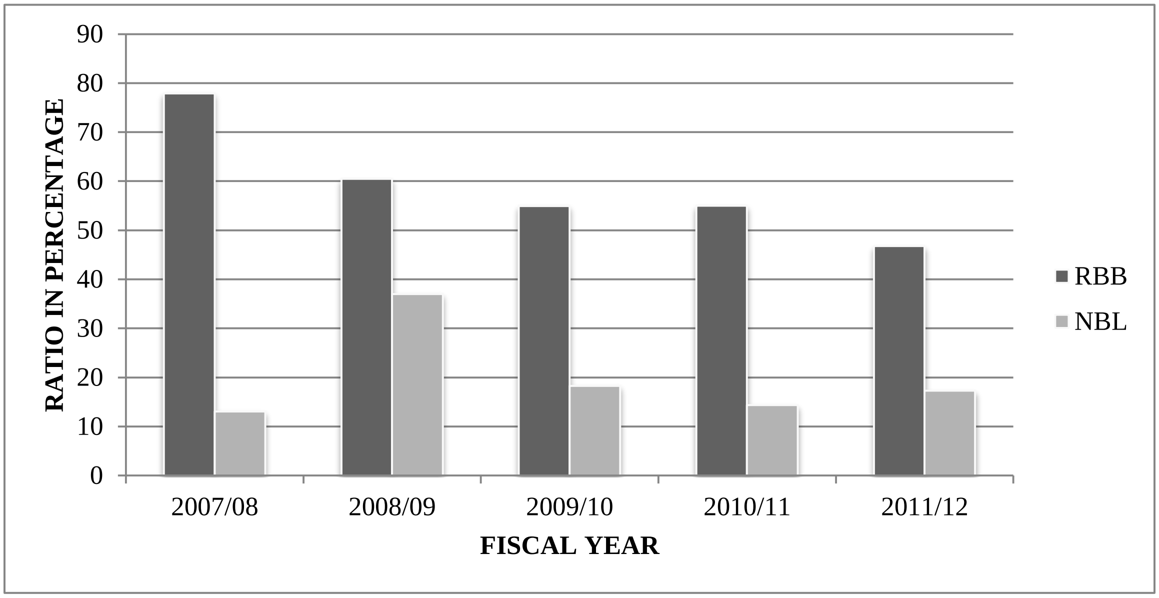
Fiscal Year	Name of the Bank	
	RBB	**NBL**
2007/08	77.89	13.08
2008/09	60.46	36.99
2009/10	54.95	18.28
2010/11	54.98	14.34
2011/12	46.76	17.27
Average	59.01	19.99

(Source: Appendix XI & XII)

The table 4.1 shows that both the banks net profit ratios are not in consistency. The ratio of RBB was highest of 77.89% in FY 2007/08 where as the lowest ratio of 46.76% in FY 2011/12. Similarly, the ratio of NBL was highest of 36.99% in FY 2008/09 where as the lowest ratio of 13.08% in FY 2007/08. The table shows that on an average net profit ratios of RBB seems to better than NBL (i.e 59.01% > 19.99%) and the net profit generated by the banks are not consistent.

Figure: 4.1

Net Profit Margin Ratio



In the figure 4.1, the net profit margin of RBB and NBL for the five fiscal year are shown. X-axis represents fiscal year and Y-axis represents percentage of net profit margin. The trend of net profit margin of RBB is decreasing over the study period and the trend of NBL is fluctuating, But the net profit margin of RBB is higher than NBL.

4.1.2 Return on Total Assets (ROTA)

The ratio is a primary indicator of managerial efficiency. It indicates how efficiency the assets were utilized by the bank. The ratio measures how far the management has utilized all the assets of the bank for profit generating activities. Higher ROTA indicates higher efficiency in the utilization of the total assets and vice versa.

$$\text{Return on Total Assets (ROTA)} = \frac{\text{Net profit after tax}}{\text{Total Assets}}$$

Table : 4.2

Return on Total Assets (%)

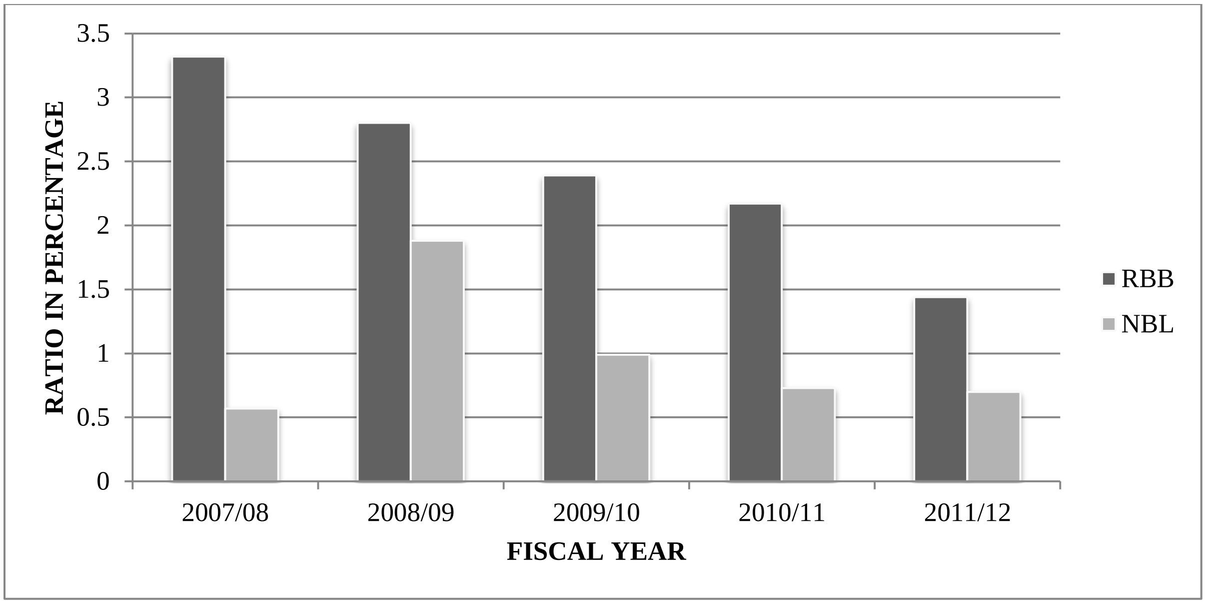
Fiscal Year	Name of the Bank	
	RBB	NBL
2007/08	3.32	0.57
2008/09	2.8	1.88
2009/10	2.39	0.99
2010/11	2.17	0.73
2011/12	1.44	0.7
Average	2.42	0.97

(Source: Appendix XI & XII)

The table 4.2 exhibits that the ratio of RBB ranged between 1.44% in FY 2011/12 to 3.32% in the FY 2007/08. Whereas, the ratio of NBL ranged from 0.57% in the FY 2007/08 to 1.88% in the FY 2008/09. It shows that the ratio of RBB is decreasing over the study period but the ratio of NBL is in fluctuating trend , in an average RBB has higher ratios than NBL (2.42%>0.97%). Although both banks do not seem to be utilizing their assets more efficiently, RBB is more capable than NBL.

Figure:4.2

Return on Total Assets Ratio



In the figure 4.2, the Return on Total Assets of RBB and NBL for the five fiscal years are shown. X- axis represents fiscal year and Y- axis represents percentage of return on total assets. The figure shows that ratio of RBB is in decreasing trend which is not good sign for the bank and ratio of NBL also decreased after FY 2008/09 to FY 2010/11.However, RBB is in good condition than NBL but is not good enough in compare to other banks of Nepal. There are enough opportunities for the management of both banks to effective utilization of accrued assets.

4.1.3 Return on Equity (ROE):-

Equity refers to the owner's claim of a bank. The excess amount of total asset over outsider's liabilities is known as shareholders equity. It is also known as net worth. This ratio measures how prudently the management has employed shareholders fund keeping the interest of shareholders and maximize their net worth. It is the measurement of the rate of return available to the banks shareholders. paid up capital Shareholders equity includes only, general reserve is negative beacuse negative networth is include in shareholders euity figure so it doesn't cannot provide exact ROE. The ratio provides the company to deliver a good return on equity. This ratio is calculated by dividing net profit by total equity capital

$$\text{Return on Equity (ROE)} = \frac{\text{Net profit after tax}}{\text{Shareholders Equity}}$$

Table: 4.3

Return on Equity (%)

Fiscal Year	**Name of the Bank**	
	RBB	**NBL**
2007/08	150.88	62.89
2008/09	164.09	235.09
2009/10	171.5	112.7
2010/11	150.1	100.8
2011/12	26.3	22.94
Average	132.57	106.88

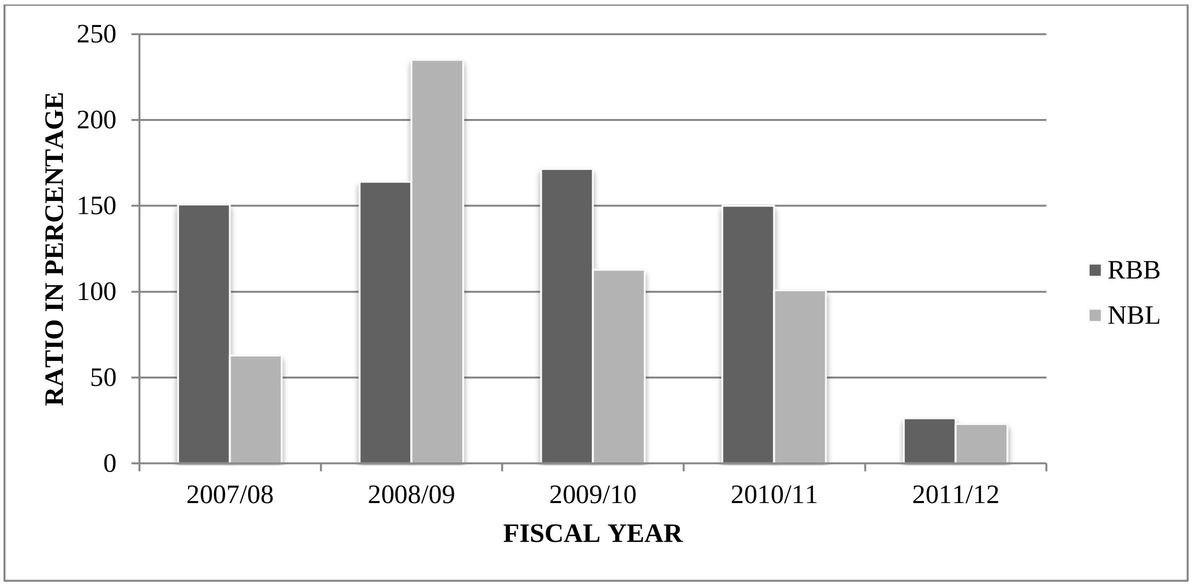
(Source: Appendix XI &XII)

The table 4.3 shows the return on equity of both RBB and NBL . Whereas the ratio of RBB ranged between 26.3% in FY 2011/12 to 171.5% in the FY 2009/10. Whereas, the ratio of NBL ranged from 22.94% in the FY 2011/12 to 235.09% in the FY 2008/09. It shows that both bank have fluctuating trend but in an average RBB has higher ratios than NBL (132.57%>106.88%). Although both banks do not seem to be utilizing their equity more efficiently but RBB is more capable than NBL.

In the figure 4.3, the Return on Equtiy of RBB and NBL for the five fiscal years are shown. X- axis represents fiscal year and Y- axis represents percentage of return on Equity. After the FY 2009/10 both bank's ratios are decreasing it is due to low profit and high capital.

Figure:4.3

Return on Equity Ratio



4.1.4 Operating Efficiency Ratio

Operating efficiency ratio is that ratio which is typically used to analyze how well a company is using its assets and its liabilities internally. Operating efficiency ratios can also be used to calculate the actual turnover of receivables, the repayments of liabilities, the quantity and usage of company's equity and can also be used to calculate the general use of machinery and inventory. These are simply defined as expenses as a percentage of revenue. Unlike other ratios these ratios are better when they are low because low efficiency ratios means that expenses are low and earnings of company are high. It is also related to operating leverage, which is used to measure the ratio between variable cost and fixed costs. Since banks are to pay huge amount of the interest costs for their funds, they like to reduce non- interest costs especially, staff costs, wages and overhead costs.

$$\text{Operating Efficiency Ratio} = \frac{\text{Total Operating Expenses}}{\text{Total Operating Income}}$$

Table :4.4

Operating Efficiency Ratio (%)

Fiscal Year	**Name of the Bank**	
	RBB	**NBL**
2007/08	53.05	87.85
2008/09	56.02	80.15
2009/10	55.93	120.3
2010/11	60.75	90.39
2011/12	65.91	94.58
Average	58.332	94.654

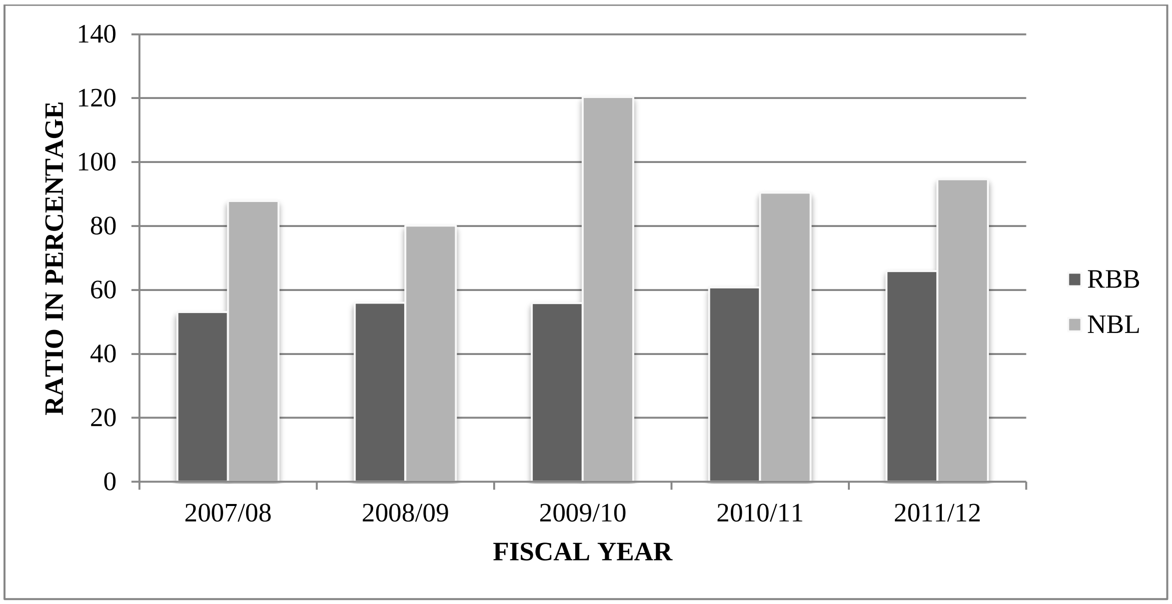
(Source: Appendix XI &XII)

The table 4.4 shows that the ratio of RBB ranged from 53.05% in the FY 2007/08 to 65.91% in the FY 2011/12 with an average of 58.33%. Similarly, the ratio of NBL ranged from 80.15% in the FY 2008/09 to 120.3% in the FY 2009/10 with an average of 94.65%. Both the banks operating efficiency ratios were alarming indication of poor performance and management. This showed that both bank have fluctuating trend but RBB has higher efficiency than NBL. So to operate efficiently both bank should reduce operating expenses and increase operating income.

The figure 4.4 reveals the operating efficiency ratio for the five fiscal years affecting from 2007/08 to 2011/12. Fiscal year is represented by x- axis and percentage of operating efficiency ratio represented by y-axis. However, RBB is in good condition than NBL in the context of operating efficiency ratio.

Figure:4.4

Operating Efficiency Ratio



4.1.5 Return on Capital Employed (ROCE)

The Return on Capital Employed ratio (ROCE) tells us how much profit we earn from the investments the shareholders have made in their company. The ratio measures management efficiency on how well the total fund including external funds were used to generate profit. This ratio provides a test of profitability in relation to long term fund. Higher ROCE implies more efficiency in utilizing the capital employed. Here the external fund comprises total of borrowings and share capital.

$$\text{Return on Capital Employed} = \frac{\text{Net Profit After Tax}}{\text{Total External Capital}}$$

Table 4.5

Return on Capital Employed (%)

Fiscal Year	**Name of the Bank**	
	RBB	**NBL**
2007/08	47.94	10.87
2008/09	38.12	38.04
2009/10	38.58	17.11
2010/11	29.39	17.25
2011/12	17.17	10.36
Average	34.24	18.726

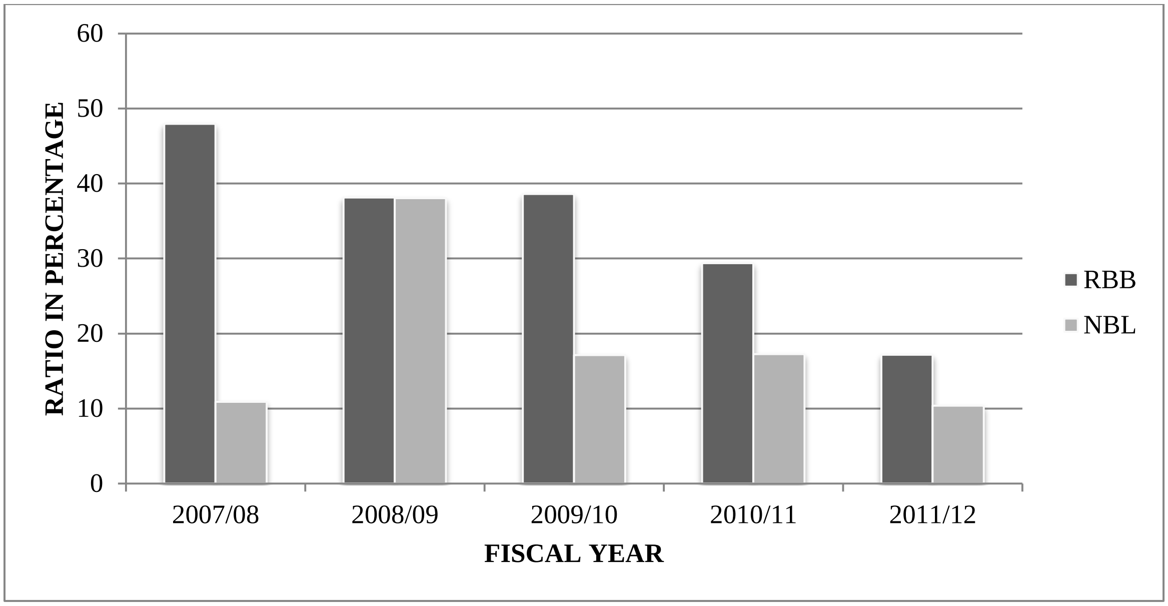
(Source:Appendix XI & XII)

The table 4.5 shows that the return on capital employed of RBB and NBL are in fluctuating trend throughout the five fiscal years. The higest ratio of RBB is 47.94% in the fiscal year 2007/08 and the lowest ratio of RBB is 17.17% in the fiscal year 2011/12. Whereas the higest ratio of NBL is 38.04 % in the fiscal year 2008/09 and lowest ratio of NBL is 10.36% in the fiscal year 2011/12 .In an average the ratio of RBB is higher than NBL. This result depicts that the fund of external capital of RBB is more utilizing than NBL

The figure No 4.5 shows the tendency of capital employed ratio of RBB and NBL. Fiscal year is represented by x- axis and percentage of return on capital employed ratio represented by y-axis. In overall the ratio of RBB is in decreasing trend and the ratio of NBL is fluctuating as well, the ratio of RBB is higher than NBL in every fiscal year.

Figure:4.5

Return on Capital Employed



4.1.6 Interest Payout Ratio

The main function of a bank is to collect deposit and advance loans. The bank pays interest on the deposits and charges interest on the loans and advances. It also realizes income from the investments and call deposits. Similarly, the bank has to pay interest on its borrowings. Thus, this ratio provides the proportion of interest payment of the bank as compared to interest income generated by the bank.

$$\text{Interest Payout Ratio} = \frac{\text{Interest Expenses}}{\text{Interest Income}}$$

Where,

Interest expenses= expenses on deposits and borrowings

Interest Income= Income on (loans and advances + investment + money at interbank lending etc.)

Table:4.6

Interest Payout Ratio

Fiscal Year	Name of the Bank	
	RBB	**NBL**
2007/08	37.86	36.88
2008/09	31	29.43
2009/10	32.96	26.68
2010/11	48.22	39.01
2011/12	56.4	54.17
Average	41.28	37.23

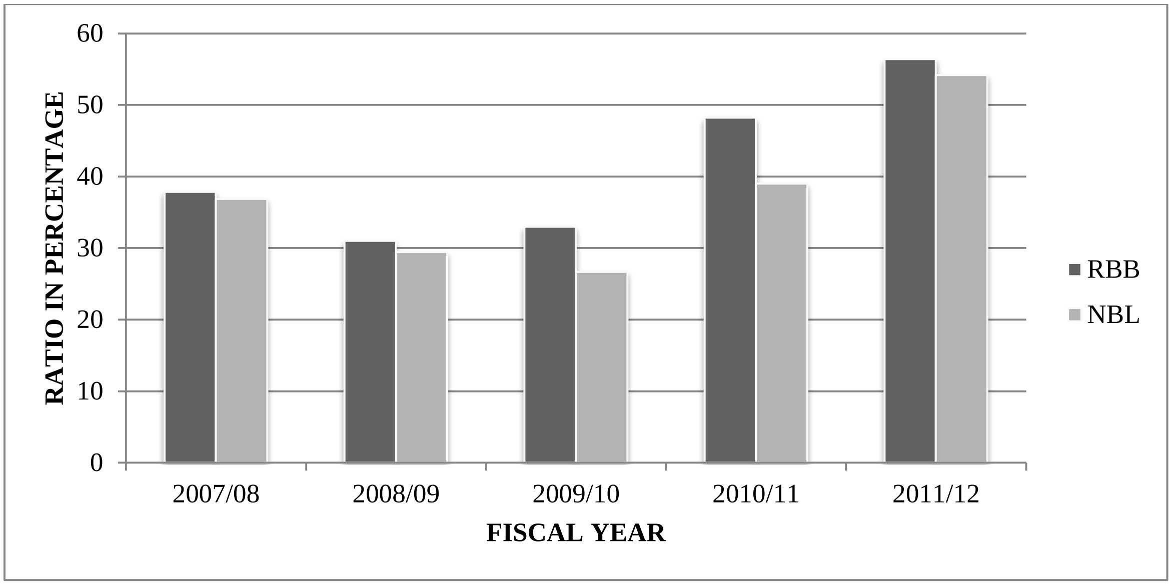
(Source: Appendix XI & XII)

In the table 4.6 , the interest payout ratio of RBB remained within the range of 31% to 56.40%. Whereas in NBL it remained within the range of 26.68% to 54.17%. In an average both the bank, RBB and NBL, had very high payout ratio of 41.28 % and 37.23% respectively. The main reason was due to high volume of NPAs and high cost deposits. Gradually in the recent year both the banks have high payout ratio , it is due to high volume of deposit and its cost which is paid on daily basis.

The figure 4.6 shows the interest payout ratio of RBB and NBL from FY 2007/08 to 2011/12, where the ratio of both bank is decreasing from 2007/08 to 2009/10 thereafter, the ratio is increasing trend, it means both the banks increasing trend of interest expenses are more than interest income.

Figure:4.6

Interest Payout Ratio(%)



4.1.7 Net Operating Margin

This is also to measure operating efficiency of commercial banks. The net operating margin of commercial banks signifies what portion of operating profit remains after deducting all operating costs. And the net operating margin is expressed with total earning assets to find out what percentage of net operating margin has contributed to total earning assets. Higher the margin, the better is the efficiency of the management.

$$\text{Net Operating Margin} = \frac{\text{Total Operaing Revenue} - \text{Total Operating Expenses}}{\text{Total Earning Assets}}$$

Table :4.7

Net Operating Margin (%)

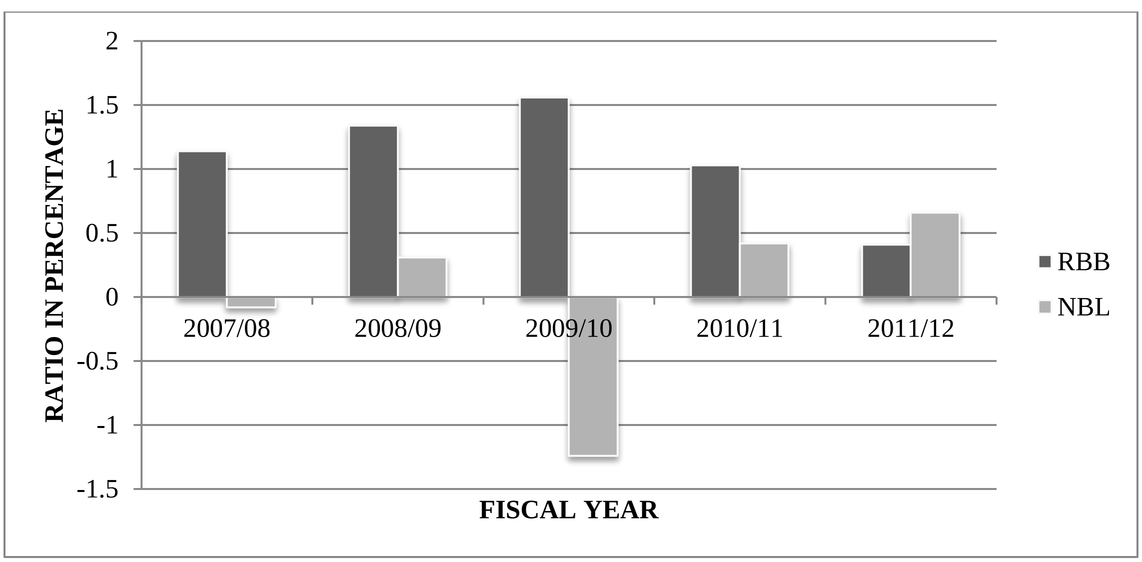
Fiscal Year	Name of the Bank	
	RBB	NBL
2007/08	1.14	-0.08
2008/09	1.34	0.31
2009/10	1.56	-1.24
2010/11	1.03	0.42
2011/12	0.41	0.66
Average	1.096	0.014

(Source: Appendix X & XI)

The table 4.7 exhibits that the ratio of RBB ranged from 0.41% in the FY 2011/12 to 1.56% in the FY 2009/10. Similarly, the ratio of NBL ranged from 0.31% in FY 2008/09 to 0.66% in the FY 2011/12 except for the negative ratio in the FY 2007/08 and 2009/10. Even though the ratio of RBB was better than NBL, the ratio of NBL is very inconsistent and low in comparison to RBB so NBL need to improve.

Figure: 4.7

Net Operating Margin



In the figure 4.7 the Net Operating Margin of RBB and NBL bank for the five fiscal years are shown. X- axis represents fiscal year and Y- axis represents percentage of Net Operating Margin. The figure shows that ratio of RBB is comparatively higher than NBL but trend of NBL is very much fluctuating and also negative it is because of heavy provision for possible losses.

4.2 Income Expenses Analysis

4.2.1 Interest Income to Total Income

Total interest earned to total income ratio indicates the extent to which the bank has successfully mobilize its fund in interest earning asset. Interest earned to total income ratio measure the magnitude of interest income in total income. Generally, banks earn interest thorough the provision of loans and advances, overdrafts and investment in securities. This ratio can be calculated as follows.

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

Table:4.8

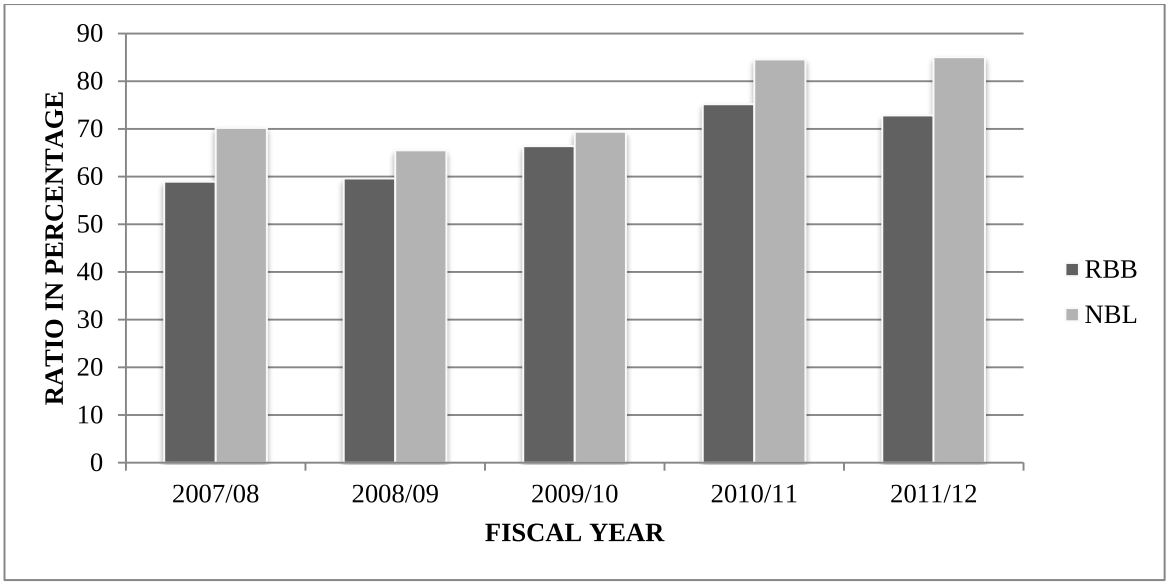
Interest Income to Total Income (%)

Fiscal Year	Name of the Bank	
	RBB	NBL
2007/08	58.93	70.21
2008/09	59.58	65.48
2009/10	66.33	69.36
2010/11	75.18	84.52
2011/12	72.77	84.98
Average	66.56	67.26

(Source:Appendix XI & XII)

Figure:4.8

Interest Income to Total Income



The table 4.8 exhibits that the interest income to total income ratio of RBB ranged between 58.93% in the FY 2007/08 to 75.18% in the FY 2010/11. Similarly, the ratio of NBL ranged from 65.48% in FY 2008/09 to 84.98% in the FY 2011/12.The average interest income to total income ratio of RBB and NBL are 66.56% and 67.26% respectively in past five years. This showed that both the bank were able to generate fair amount of interest income in its total income. The ratio of NBL and RBB had gradually improved in the FY 2010/11.

In the figure 4.8, interest income to total income of RBB and NBL for the five fiscal years are shown. X- axis represents fiscal year and Y- axis represents percentage of interest income to total income of the two banks. The figure shows that the ratio of NBL is comparatively higher than RBB which indicates that the portion of interest income on total income of NBL is high.

4.2.2 Fee and Commission Income to Total Income

The second measure source of income of the Nepalese commercial banks is fee income. Commercial banks now-a-days have moved towards the near banking agency services like under writings, counseling, various service charges, renewal fees and other consultancy functions. They have expose to non-funded fee based services like LC, guarantee, bills/clearing, safe deposit, credit card, ATM, etc. from these services banks earn fees and commission.

Fee & Commission Income to Total Income = $\frac{\text{Fee \& Commission}}{\text{Total Income}}$

Table: 4.9

Fees and Commission Income to Total Income(%)

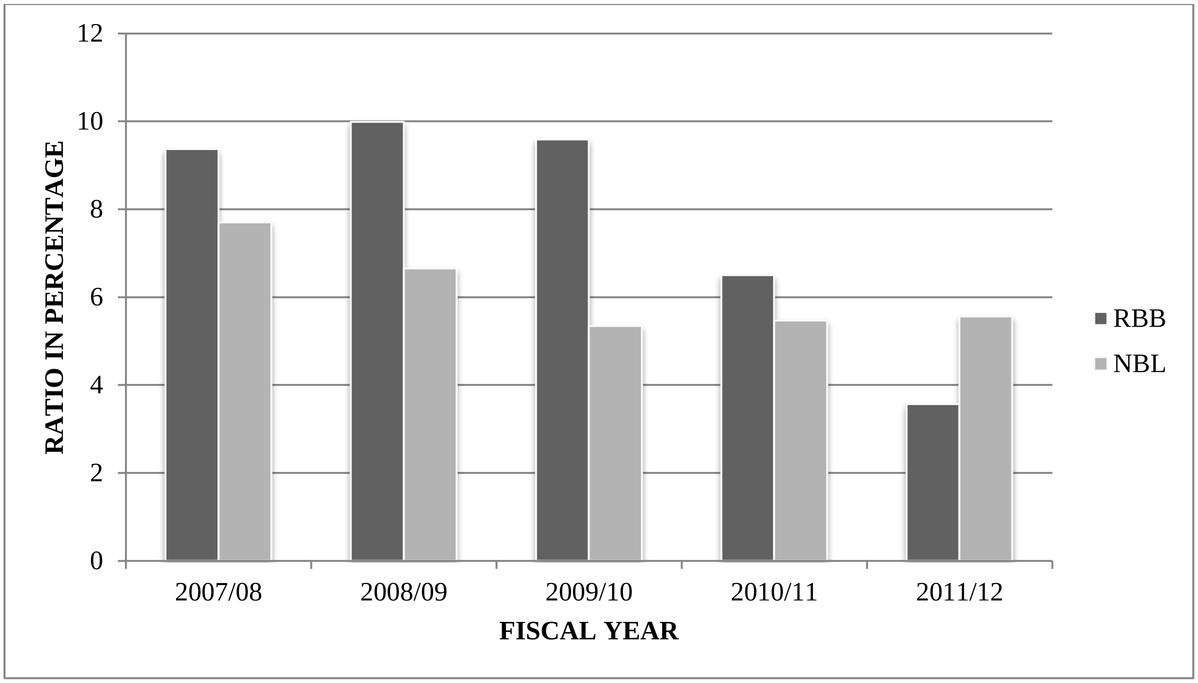
Fiscal Year	**Name of the Bank**	
	RBB	**NBL**
2007/08	9.37	7.7
2008/09	9.99	6.65
2009/10	9.59	5.34
2010/11	6.5	5.47
2011/12	3.57	5.56
Average	7.80	6.14

Source:Appendix X & XI

The table and figure 4.9 exhibits that the Fees and Commission Income to Total Income ratio of RBB ranged between 3.57% in the FY 2011/12 to 9.99% in the FY 2008/09. Similarly, the ratio of NBL ranged from 5.34% in the FY 2009/10 to 7.70% in the FY 2007/08. The average ratio of RBB and NBL are 7.80% and 6.14% respectively. The ratio of RBB is better than NBL in each year except FY 2011/12.

Figure:4.9

Fees and Commission Income to Total Income



4.2.3 Interest Expenses to Total Operating Expenses

The major expenses head of commercial banks is the interest expenses. Interest expenses occur on various deposits, interbank borrowers, borrowing from NRB and from other foreign banks. Since deposits are the raw materials inputs for the banks to produce loans, banks management should be able to screen up the various deposits, obtain an economic deposit mix and minimize the cost of deposit so that a higher spread gap remains to contribute in the profitability. In fact, the lower the cost of spread gap remains to contribute in the profitability. In fact, the lower the cost of deposits, the higher the profitability margin and vice versa. This ratio is also presented in percentage and is calculated by the following formula

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

Table:4.10

Interest Expenses to Total Operating Expenses

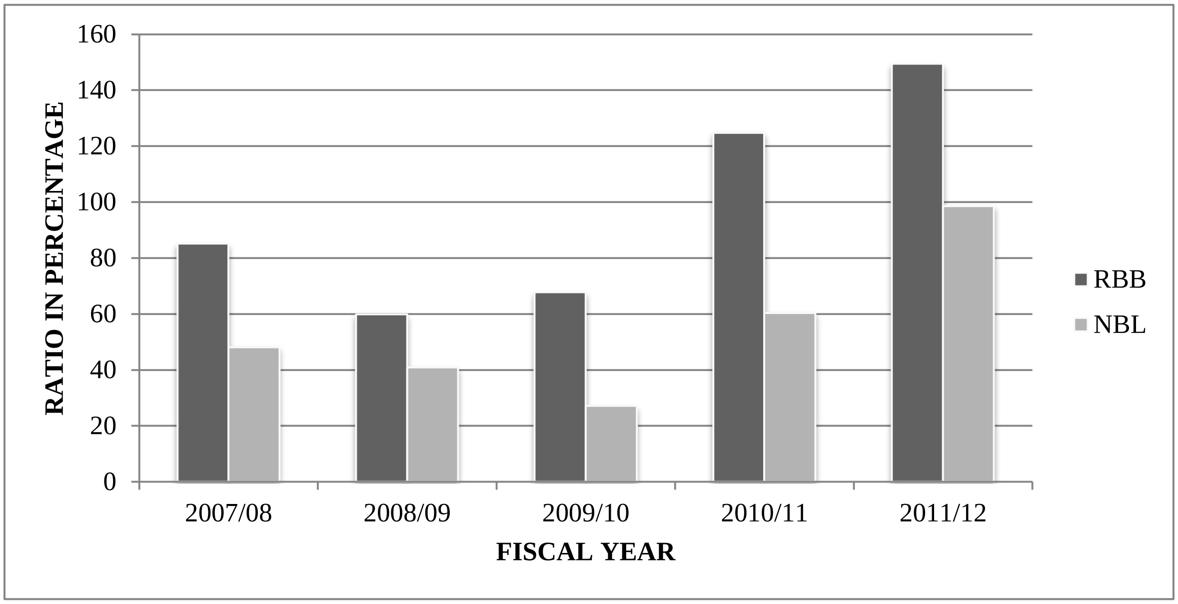
Fiscal Year	**Name of the Bank**	
	RBB	**NBL**
2007/08	85.13	48.09
2008/09	59.91	40.86
2009/10	67.76	27.09
2010/11	124.73	60.3
2011/12	149.39	98.53
Average	97.38	54.97

(Source: Appendix XI & XII)

The table and figure 4.10 exhibits that the Interest Expenses to Total Operating Expenses ratio of RBB ranged from 59.91% in FY 2008/09 to 149.39% in the FY2011/12. Similarly the ratio of NBL ranged from 27.09% in FY 2009/10 to 98.53% in FY 2011/12 but in an average ratio of RBB and NBL are 97.38% and 54.97 respectively which shows the ratio of RBB are higher over the study period than the ratio of NBL.The ratio of both bank seems highest in FY 2011/12 due increasing of total deposits.

Figure:4.10

Interest Expenses to Total Operating Expenses



4.2.4 Staff Expenses to Total Operating Expenses

One of the major expenses of banks administration and operation is staff expenses. Staff expenses comprises of salary, allowances, provident fund and other incentives. In average, the staff expenses comprises share in total operating expenses is more than 15% of average Nepalese commercial banks.

$$\text{Staff Expenses to Total Operating Expenses} = \frac{\text{Total Staff Expenses}}{\text{Total Operating Expenses}}$$

Table:4.11

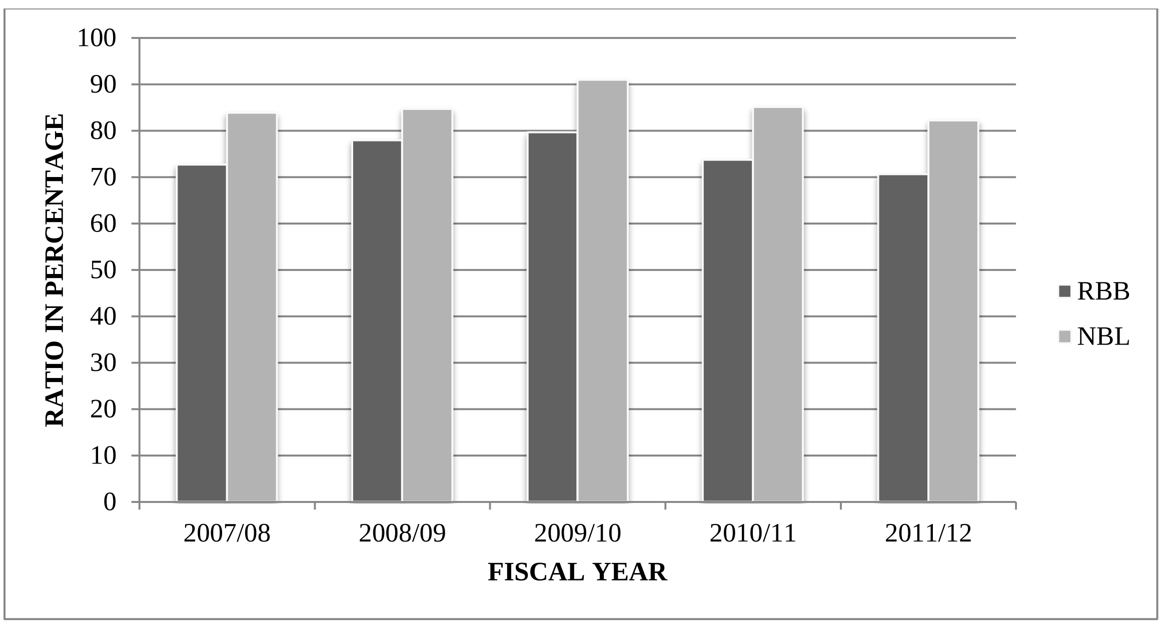
Staff Expenses to Total Operating Expenses

Fiscal Year	Name of the Bank	
	RBB	**NBL**
2007/08	72.68	83.83
2008/09	77.93	84.67
2009/10	79.6	90.96
2010/11	73.71	85.05
2011/12	70.61	82.21
Average	74.91	85.34

(Source: Appendix XI & XII)

Figure:4.11

Staff Expenses to Total Operating Expenses



The table and figure 4.11 shows the ratio of Staff Expenses to Total Operating Expenses of RBB and NBL over the study period. The ratio of RBB ranged from

70.61% in FY 2011/12 to 79.6% in FY 2009/10, similarly the ratio of NBL ranged from 82.21% in the FY 2011/12 to 90.96 in the FY 2009/10. In an average staff expenses of RBB and NBL are 74.91% and 85.34% respectively on Total Operating Expenses. It means staff expenses on NBL are higher than RBB over the study period.

4.2.5 Office Operating Expenses to Total Expenses

Office operating expenses comprises rents of office building and premises, electricity, water, repair and maintenance of various fixed assets, insurance, stationary, telex, telephone, advertisements, legal expenses, expenses relating to board of directors, expenses relating to board of audit, depreciation, amortization, professional service fee, security expenses, commission and discount and other.

It shows the percentage of expenses spent for day-to-day operation of the bank. High ratio shows the large amount of total expenses is spent for the operation activities of the bank . Lower ratio is favorable to the bank, as it is the reflection of operation efficiency.

$$\text{Office Operating Expenses to Total Expenses} = \frac{\text{Office Operating Expenses}}{\text{Total Expenses}}$$

Table:4.12

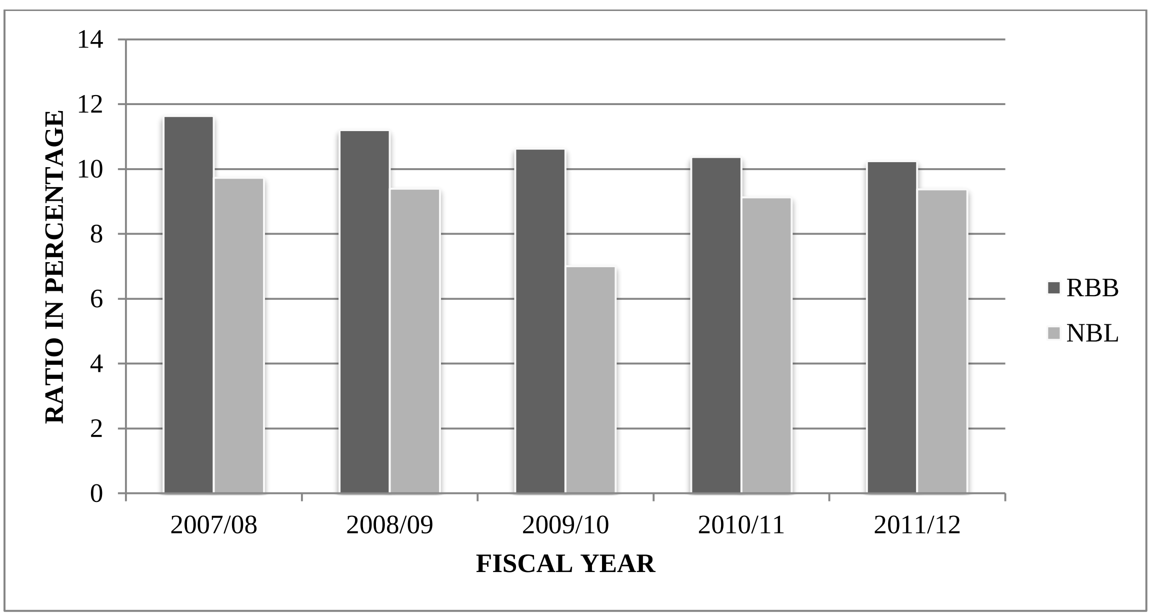
Office Operating Expenses to Total Expenses (%)

Fiscal Year	Name of the Bank	
	RBB	NBL
2007/08	11.64	9.73
2008/09	11.2	9.4
2009/10	10.63	7.01
2010/11	10.37	9.13
2011/12	10.24	9.38
Average	10.82	8.93

(Source: Appendix XI & XII)

Figure:4.12

Office Operating Expenses to Total Expenses



The table and figure 4.12 shows that the proportion of office operating expenses to total expenses. The ratio of RBB ranged from 10.24% in the FY 2011/12 to 1.64% in the FY 2007/2008 whereas, the ratio of NBL ranged from 7.01% in the FY

2009/10 to 9.73% in the FY 2007/08. This shows the average ratio (office expenses to total expenses) of RBB and NBL are 10.82% and 8.93% respectively. The trend of RBB seems decreasing and NBL is in increasing but in an average NBL seems better than RBB.

4.3 Statistical Analysis

Statistical tools help to find out the trends of financial position of the bank. It also analyzes the relationship between variables and helps banks to make appropriate decision. In this study, the least square linear trend was used to achieve the objective of the study. This topic analyzes the trend of net profit of RBB and NBL from the FY 2007/08 to 2011/12 and makes the forecast for the next five fiscal years till 2016/017.

4.3.1 Trend Analysis of Net Profit and Projection

The profit is the universal measurement tool of the performance of profit earning institution. Likewise, it also serves as an important yardstick to measure the performance of the banks. Profit is important to various parties like management, employees and the government. The employees may use it to validate their claim for better recommendations and the government to receive taxes.

Here the trend analysis of net profit of RBB and NBL was done. The forecast was made for the next five fiscal years. The forecast was based on the following assumptions:

- The main assumption is that other things remain constant and the forecast will be only when the limitations of least square method are carried out.
- The bank will run in present position.
- The economy will remain in the present trend.

- Nepal Rastra Bank will not change its guidelines to the commercial banks.

The following table shows the trend values of net profit of RBB and NBL for 10 fiscal years from 2007/08 to 2016/017

Table: 4.13

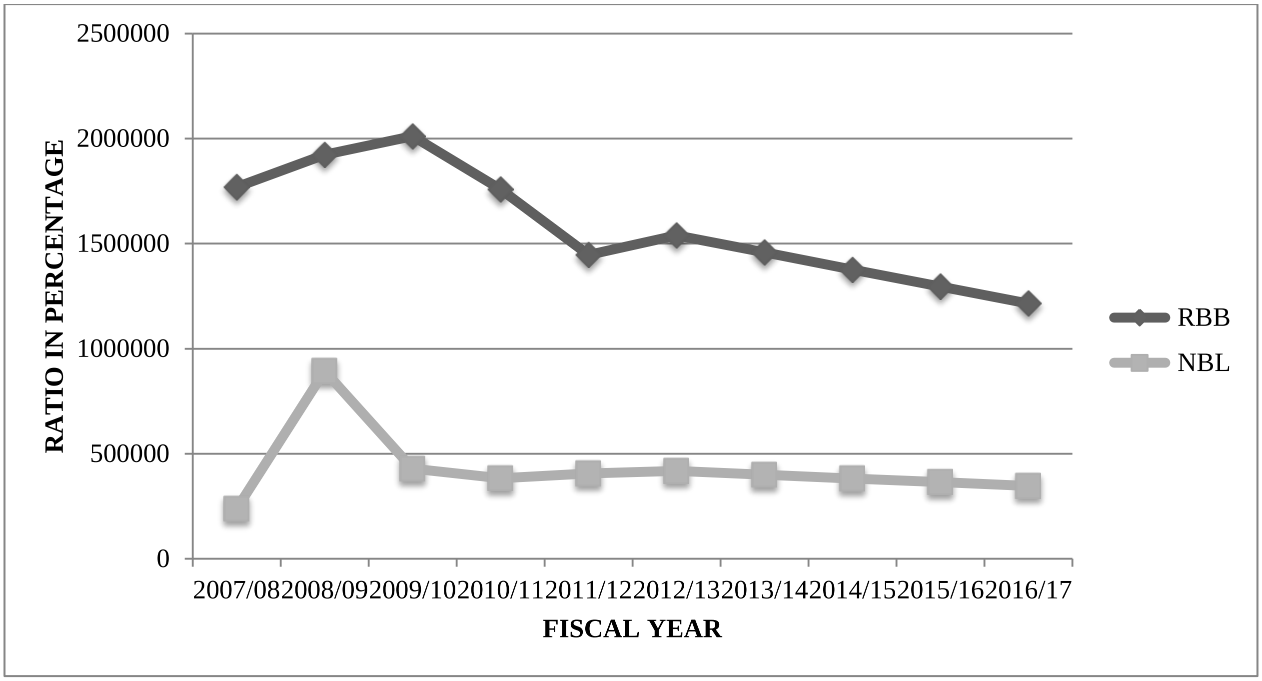
Trend Value of Net Profit of RBB and NBL

Fiscal Year	**RBB**	**NBL**
2007/08	1768772	239214
2008/09	1923682	894254
2009/10	2010687	428600
2010/11	1759255	383437
2011/12	1446220	406727
2012/13	1538863.9	417709.1
2013/14	1457910.8	400130
2014/15	1376957.7	382550.9
2015/16	1296004.6	364971.8
2016/17	1215051.5	347392.7

(Source: Appendix XIII & XIV)

Figure: 4.13

The trend line of Net Profit



The table and figure 4.13 shows the net profit of both banks. The actual profit from the FY 2007/08 to FY 2011/12 and the forecasted profit from FY 2012/13 to 2016/17. The Net Profit have the decreasing trend for the forecasted period. If other things remaining the same, the total net profit of Rastriya Banijya Bank and Nepal Bank Ltd will be Rs. 1215051.5 thousand and Rs347392.7 thousand respectively for the FY 2016/17.

4.4 Major Findings of the Study

As the bank has been improving from past performance, the net margins of both the banks were not consistent.

- The net profit margin of NBL is in fluctuating trend where as the net profit margin of RBB also in the decreasing trend over the study period. On an average net profit ratios of RBB seems to better than NBL (i.e 59.01% > 19.99%) and the net profit generated by the banks are not consistent.

- The ROTA of RBB was in decreasing trend whereas the ROTA of NBL also decreasing since last four years but in an average the ROTA of RBB was better than NBL(2.42%>0.97%) during the study period.
- ROE of RBB ranged between 26.3% in FY 2011/12 to 171.5% in the FY 2009/10. Whereas, the ratio of NBL ranged from 22.94% in the FY 2011/12 to 235.09% in the FY 2008/09. It shows that both bank have fluctuating trend but in an average RBB has higher ratios than NBL (132.57%>106.88%).
- Both the banks showed poor performance and highly fluctuating of operating efficiency ratio. The ratio showed that the NBL has high operating efficiency ratio than RBB which indicates the poor performance of NBL. In the FY 2009/10 the operating expenses of NBL was over the operating income which indicates its worst performance.
- The return on capital employed of RBB and NBL are in fluctuating trend throughout the study period. The ROCE ratio of RBB is higher than NBL in an average. Thus result depicts that the RBB is more capable than NBL in case of generating profit from uses of external funds.
- The RBB and NBL both has fluctuating interest payout ratio. The main reason of fluctuating is due to change in interest rate on deposit and lending. But the last year the ratio of both banks had increased. In an average RBB has higher payout ratio than NBL (ie 41.28 % >37.23%)
- The net operating margin of RBB was better than NBL. Both bank had very inconsistent ratio but the ratio of NBL was very low and need to be improved. Although the NBL had negative ratio in the FY 2007/08 and 2009/10.
- Interest income to total income ratio of RBB ranged between 58.93% in the FY 2007/08 to 75.18% in the FY 2010/11. Similarly, the ratio of NBL ranged from 65.48% in FY 2008/09 to 84.98% in the FY 2011/12. This

showed that both the banks are able to generate fair amount of interest income in its total income.

- Fees and Commission Income to Total Income ratio of RBB ranged between 3.57% in the FY 2011/12 to 9.99% in the FY 2008/09. Similarly, the ratio of NBL ranged from 5.34% in the FY 2009/10 to 7.70% in the FY 2007/08. The average ratio of RBB and NBL are 7.80% and 6.14% respectively. The ratio of RBB is better than NBL in each year except FY 2011/12.
- Interest Expenses to Total Operating Expenses ratio of RBB ranged from 59.91% in FY 2008/09 to 149.39% in the FY 2011/12. Similarly the ratio of NBL ranged from 27.09% in FY 2009/10 to 98.53% in FY 2011/12 but in an average ratio of RBB and NBL are 97.38% and 54.97 respectively which shows the ratio of RBB are higher over the study period than the ratio of NBL.The ratio of both bank seems highest in FY 2011/12 due increasing of total deposits.
- Both the banks has very high staff expense ratio. The ratio of RBB ranged from 70.61% in FY 2011/12 to 79.6% in FY 2009/10, similarly the ratio of NBL ranged from 82.21% in the FY 2011/12 to 90.96 in the FY 2009/10. In an average staff expenses of RBB and NBL are 74.91% and 85.34% respectively on Total Operating Expenses. It means staff expenses on NBL are higher than RBB over the study period
- Office operating expenses to total expenses ratio of RBB ranged from 10.24% in the FY 2011/12 to 1.64% in the FY 2007/2008 whereas, the ratio of NBL ranged from 7.01% in the FY 2009/10 to 9.73% in the FY 2007/08. This shows the average ratio (office expenses to total expenses) of RBB and NBL are 10.82% and 8.93% respectively. The trend of RBB seems decreasing and NBL is in increasing but in an average NBL seems better than RBB.
- Future trend value (net profit) of RBB and NBL are in decreasing trend.

CHAPTER- V

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

In this chapter, summary and conclusion of the research as well as recommendation are presented separately. After summarizing and concluding the research, recommendations are suggested for the effective liquidity management of Nepalese commercial banks. The researcher has tried to give suggestions and recommendations to the commercial banks based on this research.

5.1 Summary of the Study

The economic development of every country is always measured by its economic indicators. Therefore, every country has given emphasis on the development of its economy. Nowadays the financial institutions are viewed as catalyst in the process of the economic growth. The mobilization of domestic resources is one of the key factors in the economic development of a country. Banking sector plays an important role in the economic development of the country. Commercial banks are one of the vital aspects of this sector, which deals with the process of channeling the available resources in the needed sector. It is the intermediary between the deficit and surplus of financial resources. Financial institutions like banks are necessity to collect scattered savings and put them into productive channels. In the absence of such institutions it is possible that the saving will not be safely and profitably utilized within the country.

Banks today are under great pressure to meet the objectives of their stockholders, employees, depositors and borrowing customers while somehow keeping government regulators satisfied that the bank’s policies, loans, and investments are sound. The majority of the needs of the stakeholders are related with the profitability of the banks. Thus, the foremost objective of the banks is the profit maximization. As other types of business entity, commercial banks are also inspired by the profit, in this age of great competition, only the profitable banks can sustain for a long time. Financial policies of any concern are directly or indirectly influenced by its profitability. Thus, it is a base for a banks survival, growth and expansion. So, this research studies about the profitability analysis of commercial banks in Nepal with reference to selective banks namely RBB and NBL.

Profitability analysis is one of the key tools for financial decision and assist in making plan before using sophisticated forecasting and budgeting procedure. The value of this approach is the quantitative relation, which can be used to diagnose strengths and weakness in a bank performance. Such analysis is considerable things for the bank's common stock holders, investors, bondholders and others. The objective of the study is to find out and analyze the profitability position in Nepalese Commercial Banks. To fulfill the main objectives following specific objectives are formulated.

- To evaluate the profitability and operating financial efficiency of Rastriya Banijya Bank and Nepal Bank Ltd
- To analyze the income and expenditure, cost and profit trends of the banks.
- To provide suggestions and recommendations for the improvements of the overall profitability of the banks and provide information to the stakeholders.

In the first chapter, brief introduction of profitability management, focus of the study, significance of the study, research objectives, brief introduction of the sampled banks, limitation of the study and research scheme are included.

In the second chapter, theoretical review has been made. Different theories, policies, rules and regulations about profitability management are reviewed. During the study different books, journals, previous studies, websites, reports are viewed and visited to different professionals to know the profitability management. During the literature review, it is found that there is a few research have been made on this topic.

Research design, population and sample and analysis tools are included in the third chapter. The data are collected from secondary source for the study. The secondary data are collected from annual papers of sampled banks, SEBON, and Nepal Rastra Bank. After collecting the data from different source, it is analyzed by using financial and statistical tools and techniques.

An attempt has been made to fulfill the objectives of the research work in chapter four. In this chapter all the secondary data are compiled, processed and tabulated as per the necessity and figures; diagrams are also used to present it clearly.

In the chapter five, the summary, conclusion and recommendations are included. The summary of the study, conclusion drawn from the study are presented and necessary suggestions are given to the concern authorities, sampled banks as well as Nepalese commercial banks for the betterment of Profitability management.

This study suffers from different limitations; it considers two banks for the sampled of total commercial banks in Nepal. Time and resources are the constraints of the study. Therefore, the study may not be generalized in all cases and accuracy depends upon the data collected and provided by the organizations and respondents.

5.2 Conclusion

To avoid the chances of duplication in the study and confirm whether the study is in accordance with the principles and doctrines, supportive text and the previous dissertation have been reviewed. For analyzing the financial data of the sampled banks the financial tools- ratio analysis, income and expenditure analysis and the statically tool average and trend analysis have been used. From the analysis and interpretation of the data, the investor arrives at following conclusion.

- We can conclude that the Net Profit Margin, Return on Total Assets,Net Operating Margin of RBB is comparatively better than NBL. It also justifies that in an average the profit position of RBB is better than NBL over the study period.
- The Return on Equity and Return on Capital employed ratio of RBB is higher than NBL .It indicates the strength position of RBB in terms of equity mobilizing to generate profit.
- Operating Efficiency Position of RBB is better than NBL. It depicts the NBL is not able to generate profit from operation. The ratio shows that the NBL has high operating efficiency ratio than RBB which indicates the poor performance of NBL.
- The interest payout ratio of NBL is slightly better than RBB but in an average both banks are able to pay its interest cost.
- The balance sheet of both banks shows the proportion of loan and advance on deposit is very low so, they should utilize their deposits in profitable sector.
- Net Operating margin ratio of RBB is better than NBL, its shows RBB is able to use its assets in more profitable sector than NBL. In an average the ratio of NBL found negative due to its bad lending practice.
- Interest income to total income of both banks have found good, it shows the more contribution of interest in total profit of banks.
- Fee and commission income of both bank are not satisfactory so, both bank should adopt fee and commission based business to sustain in competitive market.

- It shows that RBB pays higher amount of total interest to their depositors than NBL but the interest expenses on their total operating expenses of NBL is better than RBB.
- The portion of staff expenses of both banks are very high so it helps to increase the total operating expenses and reduces the profitability of the bank.
- Office Operating Expenses to Total Expenses ratio of RBB is higher than NBL and trend of RBB is decreasing and NBL is increasing but in an average NBL seems better than RBB.
- In the statistical tool, trend analysis of Net Profit of both bank are found decreasing trend. The past and forecasted profit of RBB is higher than NBL so the profitability position of RBB seems better than NBL but decreasing trend of RBB is higher than NBL.

5.3 Recommendation

Suggestion is the output of the whole study. It helps to take corrective action on their activities in future. Different analyses are done to arrive at this step. Based on above analysis and findings of the study following suggestions and recommendations may be referred to overcome weakness, inefficiency to profitability management and for corrective action for the concern authorities and other researchers.

- Both the banks have high level of negative net worth. Therefore, a capital plan needs to be worked out and the shareholders of these banks need to employ the capital.
- Both banks have very high potential of earning high profit than profit than they are making in the recent years so both the banks should utilize its

resources more efficiently for generating more profit margins. If resources held idle, bank faces high cost and causes the low profit margin.

- The growth rate of net profit of both banks is decreasing trend. Due to their low profit margin, they have negative growth rate in EPS and DPS which will bring negative impact to different stakeholder. Since profit is a key of success of business they should increase net profit by launching different new product or investing in profitable sectors, this may occur due to highest retain of profit for future prospect.
- After the takeover of the new management team, it has been regulated in the recent year.
- RBB and NBL do not seem to utilize their assets more efficiently to generate profit so both banks should optimal utilize their assets and take necessary steps immediately to manage its assets for its existence in this competitive market.
- Both banks have not adopted any cost management strategy to have control over its cost of funding. The cost management strategy would be ideal to reduce the various costs and increase the profitability.
- The operating efficiency ratio of both the banks is very unfavorable during the study period due to the huge amount of operating expenses in compare to the operating income. Although, both the banks efficiency ratio has lowered in the recent year it has not come to the fair level. So both the banks need to improve its operating efficiency by reducing the non-interest costs especially, staff costs, wages and overhead costs.
- Both the banks have very high staff expenses related to the total operating expenses. This is mainly due to the over staffing of the bank. Under the FSRP, the bank have implemented VRS to cut down the number of staff and still both the banks have to rethink to maintain the appropriate level of

staff to minimize the staff expenses. Not over but required staff should be maintained.

- The staff of the banks must be empowered by providing training and knowledge about the bank so that customer will go better services.
- For the better mobilization of deposit and credit, both the banks must take the help of media. It means special publicity campaign should be lunched to provide exposure of its service, which will help to boost up the banking habits and confidence among the people upon the bank.
- NBL should move towards the modern banking facilities, prompt service in each branch, and provide new product to the customer to attract relative growth trend of deposit.
- NBL need to enhance the amount of loan and advance in total assets to rise the interest income.
- Both banks have very large network in the country, as the bank has to fulfill some social obligations to the rural areas and promoting the development of poor and disadvantage group. By using the large network, both banks should focused their business on commission based sector.
- So, both the banks need to re-look in managing their network throughout the country.
- As the banks are fully or partially owned by the government, there seems some political influence in both the banks. The banks should be free from political influence as it affects the overall activities of the bank. So government must be aware of this fact and policy must be developed to improve the current situation of NBL and RBB.
- Both the banks still lack scientific MIS. The IT platform needs to be installed as soon as possible. Only after computerization of the activities, the public will feel improvements in the banking operation. But the computerized system is limited to certain branches of the banks. They have

more than a million customers in rural and urban areas. So, banks must be aware and accountable to these people for the implementation of integrated banking package. So, these activities reduced operational costs.

- Both the banks should introduce major programs as per the customers demand these days such as consumer banking, home loans ,study loan, vehicle loans, credit card facilities, online banking, internet banking, sms banking, mobile banking, branchless banking, ATM card etc. These facilities are provided by the foreign and joint venture banks, which made RBB and NBL to lag behind.

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Appendix I

Nepal Bank Limited

BALANCE SHEET

For the period from 17th July, 2007/08 to 16th July, 2011/12Rs.in ‘000

Capital and Liabilities	**2007/08**	**2008/09**	**2009/10**	**2010/11**	**2011/12**
Share Capital	380,383	380,383	380,383	380,383	1772828
Reserve and Fund	(6,388,684)	(5,234,694)	(5232200)	(4,604,661)	(4450239)
Debenture and Bond	-	-	-	-	
Borrowings	1820089	1970675	2125100	1842410	2153794
Deposits	41,829,391	45,194,232	42,129900	46,804,206	56042591
Bills Payable	52,342	12,016	47100	-	-
Pro. &Divi. Payable	2,067	2,065	2,000	-	-
Income Tax Liabilities	-	-	130600		-
Other liabilities	4357856	5,234,433	3,490,800	8,178,866	2159969
Total Liabilities	**42,053,444**	**47,559,110**	**43,073,700**	**52,601,204**	**57678943**
Assets					
Cash balance	1,181,792	1,515,655	1,573,700	10,837,966	11991877
Balance with NRB	4,430,641	6,619,700	7,450,200		
Balance with Banks	1,004559	1,036,435	1,044,700		
Money at Call and Short Notice	-	400,000	-	400,000	-
Investment	16,570,755	13,397,559	5,815,800	7,577,702	8391726
Loan Advance and Bills Purchase	13,251,963	17,614,899	23,546,800	26,709,883	29698857
Fixed Assets	207,528	249,393	327,900	308,188	361919
Non Banking Assets			435300	381,065	309445
Other Assets	5,406,206	6,725,469	2,979,300	6,386,400	6925119
Total Assets	**42,053,444**	**47,559,110**	**43,073,700**	**52,601,204**	**57,678,943**

Appendix II

Rastriya Banijya Bank

BALANCE SHEET

For the period from 17th July, 2007/08 to 16th July, 2011/12Rs.in '000

Capital and Liabilities	**2007/08**	**2008/09**	**2009/10**	**2010/11**	**2011/12**
Share Capital	1,172,300	1,172,300	1,172,300	1,172,300	5497610
Reserve and Fund	(16,632,278)	(13,133,193)	(9,789,377)	(9,377,570)	(8294989)
Debenture	-	-	-	-	-
Borrowings	2517009	3873598	4039791	4,812,803	2923127
Deposits	64340951	68160927	68,623,160	73924079	87775031
Bills Payable	68180	68605	31360	-	
Pro. & payable div	55090	62960	86687	-	
Tax Liabilities	-	-	29186	-	
Other liabilities	1,783,670	8,509,150	19,904,757	10691581	12659244
Total Liabilities	**53,304,922**	**68,714,347**	**84,097,864**	**81,223,193**	**100560023**
Assets					
Cash balance	8640723	2014077	1674650	6907305	
Balance with NRB	3708616	8412752			19262919
Balance with Banks	197157	1344468			
Money at Call	550000			83250	512300
Investment	14443378	15416020	12989463	15333163	26501130
Loan Advance	21202987	26187931	30254069	36866104	40448863
Fixed Assets	465553	452209	890805	946815	1060414
Non Banking Assets	51453	23317	199077	145013	126126
Other Assets	7950828	14863573	28177001	20941543	12648270
Total Assets	**53304922**	**68714347**	**84097864**	**81223193**	**100560023**

Appendix III

Nepal Bank Limited

PROFIT AND LOSS ACCOUNT

For the period from 17th July, 2007/08 to 16th July, 2011/12Rs.in ‘000

S.N	Particulars	2007/08	2008/09	2009/10	2010/11	2011/12
1	Interest Income	2,094,906	2,690,058	2,865,100	3,735,206	4050973
2	Interest Expenses	772,657	791,710	764,400	1,457,253	2194326
Net Interest Income		**1,322,249**	**1,898,348**	**2,100,700**	**2,277,953**	**1856647**
3	Commissions and Discount	229,724	237,106	220,700	241,673	264871
4	Other Operating Income	157,432	156,757	-	140,239	179445
5	Exchange Income	119,407	89,209	23,600	13,595	53699
Total Operating Income		**1,828,812**	**2,417,420**	**2,345,000**	**2,673,460**	**2354663**
6	Staff Expenses	1,346,824	1,640,565	2,566,100	2,055,393	1830982
7	Other Operating Expenses	259,786	297,015	255,100	361,139	396167
8	Exchange Loss		-	-	-	-
Operating Profit Before Provision for Possible Loss		**222,202**	**479,840**	**(476,200)**	**256,928**	**127514**
9	Provision for Posssible Loss	258,572	334,315	55,600	36,369	(250356)
Operating Profit		**(36,370)**	**145,525**	**(531,800)**	**220,559**	**377869**
10	Non Operating Profit /Loss	67,942	57,526		35,735	54911
11	Loan Loss Provision written Back	134,362	676,372	748,700	54,056	71569

Profit from Ordinary Activities		**165,934**	**879,423**	**216,900**	**310,350**	**504349**
12	Extra Ordinary Income /Expenses	179,996	165,144	213,900	198,578	91607
Net Profit including all Activities		**345,930**	**1,044,567**	**430,800**	**508,928**	**595956**
13	Staff Bonus Provision	31,448	94,960		46,266	54178
14	Tax Provision This Year	75,268	55,353	2,200	79,225	135051
	Up to previous Yrs					
	Net Profit /Loss	**239,214**	**894,254**	**428,600**	**383,437**	**406727**

Appendix IV

Rastriya Banijya Bank

PROFIT AND LOSS ACCOUNT

For the period from 17th July, 2007/08 to 16th July, 2011/12Rs.in ‘000

S.N	Particulars	2007/08	2008/09	2009/10	2010/11	2011/12
1	Interest Income	2708764	3444188	4207610	5027872	5399992
2	Interest Expenses	1025586	1067779	1386980	2424251	3045590
Net Interest Income		**1683178**	**2376409**	**2820630**	**2603621**	**2354402**
3	Commissions and Discount	430618	577560	608261	435001	427239
4	Other Operating Income	157070	195561	177270	188903	210706
5	Exchange Income	-	32098	53215	(28028)	100820

Total Operating Income		**2270866**	**3181628**	**3659376**	**3199497**	**3093167**
6	Staff Expenses	875656	1389012	1629244	1432706	1439593
7	Other Operating Expenses	329090	393316	417546	510873	599075
8	Exchange Loss	30484		13067		-
Operating Profit Before Provision Possible Loss		**1035636**	**1399300**	**1599519**	**1255918**	**1054499**
9	Provision for Posssible Loss	425542	481042	286546	419482	639248
Operating Profit		**610094**	**918258**	**1312973**	**836436**	**415252**
10	Non Operating Profit /Loss	13872	60887	97738	96200	75880
11	Loan Loss Provision written Back	1134290	1331959	1201493	760297	994873
Profit from Ordinary Activities		**1758256**	**2311104**	**2612204**	**1692933**	**1486004**
12	Extra Ordinary Income /Expenses	152018	138356	(2219)	207062	210455
Net Profit including all Activities		**1910274**	**2449460**	**2609985**	**1899995**	**1696459**
13	Staff Bonus Provision	141502	181441	193332	140740	125664
14	Tax Provision This Year Up to previous Year .This Year Deferred Tax	-	344337	405966		124575
Net Profit /Loss		**1768772**	**1923682**	**2010687**	**1759255**	**1446220**

Appendix V

Income analysis of NBL From F/Y 2007/08 to 2011/12 (Rs. in '000)

Sources of Income	2007/08	2008/09	2009/10	2010/11	2011/12
Interest Earned	2,094,906	2,690,058	2,865,100	3,735,206	4050973
Commission & Discount	229,724	273,106	220,700	241,673	264871
Exchange Fluctuation Income	119,407	89,209	23,600	13,595	53699
Other Operating Income	157,432	156,757	58,709	140,239	179445
Non Operating Income	67,942	57,526	-	35,735	54911
Loan Loss provision written Back	134,362	676,372	748,700	54,056	71569
Profit/Loss from extra ordinary activities	179,996	165,144	213,900	198,578	91607
Total Income	**2,983,769**	**4,108,172**	**4,130,709**	**4,419,082**	**4767075**

Appendix VI

Expenses Analysis of NBL from F/Y 2007/08 to 2011/12 (Rs. in '000)

Expenses head	2007/08	2008/09	2009/10	2010/11	2011/12
Interest Paid	772,657	791,710	764400	1,457,253	2194326
Staff Expenses	1346,824	1,640,565	2566100	2,055,393	1830982
Office Operating exp	259,786	297015	255100	36,1139	396167
Exchange Fluctuation Loss	-	-	-	-	
Provision for Loan Loss	258,572	334,315	55600	36,369	(250356)
Provision for staff Bonus	31,448	94,960	-	46,266	54178
Total Expenses	**2,669,287**	**3,158,565**	**3,641,200**	**3,956,420**	**4225297**

Appendix VII

Income analysis of RBB From F/Y 2007/08 to 2011/12 (Rs. in '000)

Sources of Income	2007/08	2008/09	2009/10	2010/11	2011/12
Interest Earned	2708764	3444188	4207610	5027872	5399992
Commission & Discount	430618	577560	608261	435001	427239
Exchange Fluctuation Income		32098	53215	(28028)	100820
Other Operating Income	157070	195561	177270	188903	210706
Non Operating Income	13872	60887	97738	96200	75880
Loan Loss provision written Back	1134290	1331959	1201493	760297	994873
Profit/Loss from extra ordinary activities	152018	138356	(2219)	207062	210455
Total Income	**4,596,632**	**5,780,609**	**6,343,368**	**6,687,307**	**7419965**

Appendix VIII

Expenses Analysis of RBB from F/Y 2007/08 to 2011/12 (Rs. in ‘000)

Expenses head	2007/08	2008/09	2009/10	2010/11	2011/12
Interest Paid	1025586	1067779	1386980	2424251	3045590
Staff Expenses	875656	1389012	1629244	1432706	1439593
Office Operating exp	329090	393316	417546	510873	599075
Exchange Fluctu Loss	30484	-	13067	-	-
Provision for Loan Loss	425542	481042	286546	419482	639248
Provision for staff Bonus	141502	181441	193332	140740	125664
Total Expenses	**2827860**	**3512590**	**3926715**	**4928052**	**5849170**

Appendix IX

Summary of Financial Transaction of RBB'000'						
Particular	**Ref**	**2007/08**	**2008/09**	**2009/10**	**20010/11**	**2011/12**
Total Operating Income	A	2270866	3181628	3659376	3199497	3093167
Net Profit	B	1768772	1923682	2010687	1759255	1446220
Total Assets	C	53304922	68714347	84097864	81223193	100560023
Shareholder Equity	D	1172300	1172300	1172300	1172300	5497610
Total Operating Exp.	E	1204746	1782328	2046790	1943579	2038668
Interest Income	F	2708764	3444188	4207610	5027872	5399992
Interest Expenses	G	1025586	1067779	1386980	2424251	3045590
Total Income	H	4596632	5780609	6343368	6687307	7419965
Fee & Commission Income	I	430618	577560	608261	435001	264871
Staff Exp.	J	875656	1389012	1629244	1432706	1439593
Operating Profit	K	610094	918258	1312973	836436	415252
office expenses	L	329090	393316	417546	510873	599075
Total Expenses	M	2827860	3512590	3926715	4928052	5849170

Appendix X

Summary of Financial Transaction of NBL '000'						
Particular	**Ref**	**2007/08**	**2008/09**	**2009/10**	**2010/11**	**2011/12**
Total Operating Income	A	1828812	2417420	2345000	2673460	2354663
Net Profit	B	239214	894254	428600	383437	406727
Total Assets	C	42053444	47559110	43073700	52601204	57678943
Shareholder Equity	D	380383	380383	380383	380383	1772828
Total Operating Exp.	E	1606610	1937580	2821200	2416532	2227149
Interest Income	F	2094906	2690058	2865100	3735206	4050973

Interest Expenses	G	772657	791710	764400	1457253	2194326
Total Income	H	2,983,769	4,108,172	4,130,709	4,419,082	4767075
Fee & Comm. Income	I	229724	273106	220700	241673	264871
Staff Exp.	J	1346824	1640565	2566100	2055393	1830982
Operating Profit	K	-36370	145525	-531800	220559	377869
Office Expenses	L	259,786	297,015	255,100	361,139	396167
Total expenses	M	2,669,287	3,158,565	3,641,200	3,956,420	4225297

Appendix XI

Calculation of Ratio Analysis of RBB						
Particular	**Ref**	**2007/08**	**2008/09**	**2009/10**	**2010/11**	**2011/12**
Net profit Margin	b/a	77.89	60.46	54.95	54.99	46.76
Return on Total Assets	b/c	3.318	2.8	2.391	2.166	1.44
Return on Equity	b/d	150.88	164.09	171.52	150.07	26.30
Operating efficiency Ratio	e/a	53.05	56.02	55.93	60.75	65.91
Interest Payout Ratio	g/f	37.86	31	32.96	48.22	56.40
Interest Income to Total Income	f/h	58.93	59.58	66.33	75.19	72.77
Fee & Com. Income to Total Income	i/h	9.368	9.991	9.589	6.505	3.57
Interest exp. To Total Operating Exp.	g/e	85.13	59.91	67.76	124.7	149.39
Staff Exp. To Total Operating Exp.	j/e	72.68	77.93	79.6	73.71	70.61
Net Operating Margin	k/c	1.145	1.336	1.561	1.03	0.41
Office exp to Total Expenses	l/m	11.64	11.2	10.63	10.37	10.24

Appendix XII

Calculation of Ratio Analysis of NBL						
Particular	**Ref**	**2007/08**	**2008/09**	**2009/10**	**2010/11**	**2011/12**
Net profit Margin	B/A	13.08	36.99	18.28	14.34	17.27
Return on Total Assets	B/C	0.569	1.88	0.995	0.729	0.70
Return on Equity	B/D	62.89	235.09	112.68	100.80	22.94
Operating efficiency Ratio	E/A	87.85	80.15	120.3	90.39	94.58
Interest Payout Ratio	G/F	36.88	29.43	26.68	39.01	98.52
Interest Income to Total Income	F/H	70.21	65.48	69.36	84.52	84.98
Fee & Commission Income to Total Income	I/H	7.699	6.648	5.343	5.469	5.55
Interest exp. To Total Operating Exp.	G/E	48.09	40.86	27.09	60.3	98.52
staff Exp. To Total Operating Exp.	J/E	83.83	84.67	90.96	85.06	82.21
Net Operating Margin	K/C	-0.09	0.306	-1.23	0.419	0.65
Office exp to Total Expenses	L/M	9.732	9.403	7.006	9.128	9.37

Appendix XIII

Trend Analysis of Net Profit of RBB'000'

Year	Time Period (x)	Net Profit (y)	x^2	Xy
2007/08	1	1768772	1	1768772
2008/09	2	1923682	4	3847364
2009/10	3	2010687	9	6032061
2010/11	4	1759255	16	7037020
2011/12	5	1446220	25	7231100
	$\sum x=15$	**$\sum y=8908616$**	**$\sum x^2=55$**	**$\sum xy=25916317$**

For this method we have a equation

y= a+ bx…………….(i)

Where,

y= net profit

x= time period

n= 5(number of years)

a and b= constant parameters which are to be estimated. The parameter b gives the measure of annual increase in sales. The unknown parameter a and b are estimated by solving the following two equation based on the principle of least square.

$$\Sigma y = na + b\Sigma x \text{------ii}$$

$$\Sigma xy = a\Sigma x + b\Sigma x^2 \text{ ----iii}$$

Substituting the value in eqn. ii and iii We have,

8908616= 5a + 15b -------------iv

$25916317 = 15a + 55b$ -----------v

Multiplying equation iv by 3 and solve them

$$\begin{array}{lll} 26725848 & 15a & 45b \\ \underline{25916317} & \underline{15a} & \underline{55b} \\ 809531 & & -10b \end{array}$$

Or, $-10b = 809531$

Or, $b = -80953.10$

Substituting the value of b in equation iv.

$8908616 = 5a + 15b$

Or, $8908616 = 5a + 15 * -80953.10$

Or, $8908616 = 5a + -(1214296.50)$

Or, $a = 2024582.50$

Now substituting value of constant a & b in equation (i) we get

$y = 2024582.50 – 80953.10x$

From the equation, now we can obtain the forecast of the net profit for next five year.

Forecast for next 5 years profit			
Year	**Time Period(X)**	**Y=a+bx**	**Forecasted Net Profit**
2012/13	6	y=2024582.50-80953.10*6	1538863.9
2013/14	7	y=2024582.50-80953.10*7	1457910.8
2014/15	8	y=2024582.50-80953.10*8	1376957.7
2015/16	9	y=2024582.50-80953.10*9	1296004.6
2016/17	10	y=2024582.50-80953.10*10	1215051.5

Appendix XIV

Trend Analysis of Net Profit of NBL'000'

Year	Time Period (x)	Net Profit(y)	x^2	Xy
2007/08	1	239214	1	239214
2008/09	2	894254	4	1788508
2009/10	3	428600	9	1285800
2010/11	4	383437	16	1533748
2011/12	5	406727	25	2033635
	$\sum x=15$	**$\sum y=2352232$**	**$\sum x^2=55$**	**$\sum xy=6880905$**

For this method we have a equation

$y= a+ bx$…………….(i)

Where,

y= net profit

x= time period

n= 5(number of years)

a and b= constant parameters which are to be estimated. The parameter b gives the measure of annual increase in sales. The unknown parameter a and b are estimated by solving the following two equation based on the principle of least square.

$$\Sigma y = na + b\Sigma x \text{------ii}$$

$$\Sigma xy = a\Sigma x + b\Sigma x^2 \text{ ----iii}$$

Substituting the value in eqn. ii and iii We have,

$$2352232= 5a + 15b \text{ -------------iv}$$

$$6880905=15a + 55b \text{ -----------v}$$

Multiplying equation iv by 3 and solve them

$$\begin{array}{lll} 7056696 & 15a & 45b \\ \underline{6880905} & \underline{15a} & \underline{55b} \\ 175791 & & -10b \end{array}$$

Or, $-10b = 175791$

Or, $b=-17579.10$

Substituting the value of b in equation iv.

$2352232 = 5a + 15b$

Or, $2352232 = 5a + 15 \times -(17579.10)$

Or, $2352232 = 5a + -(263686.5)$

Or, $a = 523183.7$

Now substituting value of constant a & b in equation (i) we get

$y= 523183.7 -17579.10x$

From the equation, now we can obtain the forecast of the net profit for next five year.

Forecast for next 5 years profit			
Year	**Time Period (x)**	**Y=a+bx**	**Forecasted Net Profit**
2012/13	6	y=523183.7-17579.10*6	417709.1
2013/14	7	y=523183.7-17579.10*7	400130
2014/15	8	y=523183.7-17579.10*8	382550.9
2015/16	9	y=523183.7-17579.10*9	364971.8
2016/17	10	y=523183.7-17579.10*10	347392.7