

ANALYSIS OF NON-PERFORMING ASSETS OF NEPALESE COMMERCIAL BANKS

**(With reference to Nepal Bank Limited, Rastriya Banijya Bank, Nabil Bank Limited,
Nepal Investment Bank Limited, Standard Chartered Bank Nepal Limited)**

By

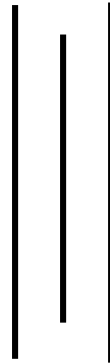
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**A Thesis Submitted to:
Office of the Dean
Faculty of Management
Tribhuvan University**



***In partial fulfillment of the requirements for the degree of
Masters of Business Studies (M.B.S.)***

Kathmandu, Nepal

September, 2011

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ANALYSIS OF NON-PERFORMING ASSETS OF NEPALESE COMMERCIAL BANKS

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Nepal Investment Bank Limited, Standard Chartered Bank Nepal Limited)**

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*And found the thesis to be the original work of the student and written
according to the prescribed format. We recommend the thesis to
be accepted as partial fulfillment of the requirement for*

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DECLARATION

I hereby declare that the work reported in this thesis entitled “**ANALYSIS OF NON-PERFORMING ASSETS OF NEPALESE COMMERCIAL BANKS (With reference to Nepal Bank Limited, Rastriya Banijya Bank, Nabil Bank Limited, Nepal Investment Bank Limited, Standard Chartered Bank Nepal Limited)** ” 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 Degree of Master of Business Studies (M.B.S.) under the supervision of Mr. Suresh Kumar Wagle of Saraswati Multiple Campus.

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ACKNOWLEDGEMENT

I am pleased to present this thesis titled “Analysis of Non-Performing Assets of Nepalese Commercial Banks” to the Office of the Dean, Faculty of Management, TU, in partial fulfillment of the requirements for the degree of Master of Business Studies (MBS). It’s like a dream come to complete this thesis work after the long committed efforts and dedication. I experienced a feeling of great relief and joy after completing this project.

Banking sector is the key player in the country's economic development. The issue of NPAs in Nepalese commercial banks has been a matter of serious concern in economic field. The main objective of this study is to find out the overall impact of NPA on the profitability of the commercial banks. I believe this thesis will be quite helpful to all the concerned to understand the status of NPAs of commercial banks.

This work would not have come out in its present shape without the cooperation, guidance and support provided by a number of people. In this respect, I would like to offer my particular thanks and gratitude to Mr. Suresh Kumar Wagle, my thesis supervisor and the senior lecturer of Saraswati Campus. His productive ideas, comments and friendly approach need special mention. Also, I am thankful to Mr. Shivraj Ghimire, lecturer of Saraswati Campus for his wonderful support. I must say thanks to the staffs of library and administration of Saraswati Campus and TU central library. I am thankful to all the staffs of NRB, especially Mr. Kiran Pandit for their support. Also, I must say thanks from the heart to all the staff members of NBL, RBB, NABIL, NIBL and SCBNL for their kind assistance.

I would like to give my special thanks to my dear parents Mr. Mukti Bahadur Pradhan and Mrs. Narmada Pradhan, wife Srijana Shrestha Pradhan, other family members and all friends and relatives for their constant encouragement, guidance and support, which are truly a source wonderful inspiration in completing this project.

To sum up, despite my painstaking efforts, there might be various shortcomings and limitations in this thesis work, which will be a lesson to me for my future endeavours.

Prakash Pradhan

September 2011

ABSTRACT

Banking sector plays a key role in the economic development of a nation. In the context of Nepal, as of Mid – July 2010 statistics of NRB, Commercial Banks hold more than 76 percent of the total assets and liabilities of the financial system. With the increasing number of banks and other financial institutions, the banking sector has to face numerous problems and challenges. One of the major problems the banking sector currently facing is the issue of non-performing asset (NPA). Proper management of NPA has always been a great challenge for the banks.

Non-performing assets are those assets which do not generate any income to the banks. The thesis titled “Analysis of Non –Performing Assets of Nepalese Commercial Banks” is conducted with the objective of evaluation of the proportion of non-performing loan and the level of NPA in total assets, total deposit and total lending; the analysis of the relationship between loan and loan loss provision; and the study of the trend of the non-performing assets, loan and advances, loan loss provision of the selected commercial banks. Also the study includes the analysis of overall impact of NPA on profitability of the banks, the causes of NPA and the measures to be adopted to control or reduce the NPA.

Various research methodologies were used for the study. Basically, research methodologies here signifies the research design, sources of data, population and sample of data, data collection procedure, data collection tools and techniques employed etc. Out of the total population of 30 commercial banks, five banks were taken as sample by using judgmental sampling method. Nepal Bank Limited (NBL) and Rastriya Banijya Bank (RBB) are selected from public sector banks and three major banks, Nabil Bank Limited (NABIL), Nepal Investment Bank Limited (NIBL) and Standard Chartered Bank Nepal Limited (SCBNL) were selected from private sector banks. Both primary and secondary data have been used in the study. The data collected from various sources are recorded systematically and presented in appropriate forms of tables and charts. Appropriate mathematical, statistical, financial, graphical tools have been applied to analyze the data. The data of five consecutive years of the five selected banks have been analyzed to meet the objective of the study. The researcher has tried to analyze the comparative position of bank in terms of non- performing asset and its impact.

NIBL has the highest proportion of the loans and advances in the total asset structure followed by NABIL, RBB and NBL. SCBNL has the lowest loans and advances in the total asset structure. The credit deposit ratio also shows almost the same result. This indicates the attitude of the management of SCBNL which is risk adverse. There is higher proportion of non-performing loan (asset) in the total loans and advances of RBB, which comes around 22.25% on average, which is very much higher than the acceptable standard of minimum 10%. This forces the bank to increase the loan loss provision. But the positive sign is that non-performing loan of RBB is in the decreasing trend. The non-performing loan in total loans and advances of NABIL, NIBL and SCBNL are 0.84%, 1.37% and 1.21% respectively which is quite less than the acceptable standard of 10%. This is the result of proper and effective management of NPL by these banks. The ratio of provision held to NPL of NABIL is the highest followed by SCBNL, NIBL, NBL and then RBB.

Although, NBL, NABIL and NIBL have used the higher portion of their investment in the most income-generating asset i.e. loans and advances, the banks are unsuccessful in generating anticipated returns as per investment. Most of the loans of these banks have become non-performing and hence it is not generating any income, instead demanded high provision for probable loss. On the other hand, NABIL and RBB have higher rate of return on investment due to proper lending and monitoring function with low cost of fund, high fee based income etc.

The correlation between loans and advances and deposit shows the positive relationship in all the sampled banks. It means that when the deposit amount increases the loan and advances also increases. There is negative correlation between LLP and loans and advances in NBL, RBB and SCBNL but shows the positive correlation in case of NABIL and NIBL. The correlation coefficients are negative as the loans and advances are increasing but LLP is decreasing. The positive correlation in NABIL and NIBL is due to decrement of non-performing loan of NBL. Amount to be provisioned depends upon the non-performing loan and its quality. Higher LLP provision has to be made for higher NPL. The correlation between NPA and net profit shows the positive correlation in all the sampled banks except NBL.

The trend analysis of loans and advances shows increasing trend in all the five sampled banks. The trend analysis of non-performing assets shows decreasing trend in all the five sampled banks. The trend analysis of loan loss provision in NBL, RBB and SCBNL shows the decreasing trend in the coming years. This is due to bank's recovery efforts towards reducing NPL through

establishment of Recovery cell. But NABIL and NIBL have increasing trend of loan loss provision in coming years. The trend analysis of net profit exhibits that all the sampled banks except NBL have increasing trend of profit in coming year.

As per the NRB directives regarding loan classification and provisioning, loans and advances have to be categorized into four types namely pass, substandard, doubtful and loss with respective provisioning of 1%, 25%, 50% and 100%. The loan falling under pass category is regarded as performing loan and that which falls under remaining three categories is regarded as non-performing loan. It was found that none of the sampled banks maintained the provision exactly as per the directives. They have maintained higher than requirement for one type of loan whereas lower for another class of loan category. Though the loan loss provision made by banks were not perfectly as per the directives, this was not highly unsatisfactory and was not the serious matter, only little attention is needed to manage LLP of each loan category. In the same way, effective supervisory role of NRB is essential in this matter. Regular supervision and control over the Nepalese commercial bank by NRB, whether they are implementing NRB's directive perfectly or not, is very important.

The NPA has inverse relation with profitability and performance of the banks. Today's banking industry is severely affected by the setback of NPA. In Nepal, the increase in NPA is especially due to the willful defaulters. Ironically big house and big companies are the major source of NPA of commercial banks. They take loan misusing their reputation, connection to political parties and make unhealthy influence. The political instability and the political pressure for sanction of loan are also major causes. Lack of proper law and the lack of willingness in the Government has been the main barrier in taking action against defaulters. Government unwillingness to punish defaulters also plays vital role in increase of NPA in Nepal and the political interference is making the acting government bodies helpless, which is one of the major causes of this problem.

It should, however, be kept in mind that NPAs are an integral part of the business financial sector and the players are in as they are in the business of taking risk and their earnings reflect the risk they take. They operate in an environment, where there would be defaults as well as deterioration in portfolio value, as market movements can never be predicted with certainty. It is in this context, that countries have adopted regulatory measures and the guiding structure has been provided by the Basel guidelines.

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ABBREVIATIONS

| | | |
|-------|---|---------------------------------------|
| AD | : | Anno Domini |
| AMC | : | Assets Management Company |
| AGM | : | Annual General Meeting |
| AMC | : | Assets Management Company |
| BS | : | Bikram Sambat |
| C.V. | : | Coefficient of variation |
| CIB | : | Credit Information Bureau |
| DRT | : | Debt Recovery Tribunal |
| E.Pra | : | Ejajat Parta |
| i.e | : | That is |
| LLP | : | Loan Loss Provision |
| Ltd | : | Limited |
| NABIL | : | Nabil Bank Limited |
| NBL | : | Nepal Bank Limited |
| NIBL | : | Nepal Investment Bank Limited |
| No. | : | Number |
| NPA | : | Non-Performing Asset |
| NBA | : | Non Banking Asset |
| NPL | : | Non-Performing Loan |
| NRB | : | Nepal Rastra Bank |
| PE | : | Probable Error |
| r | : | Correlation Coefficient |
| RBB | : | Rastriya Banijya Bank |
| Rs. | : | Rupees |
| SCBNL | : | Standard Chartered Bank Nepal Limited |
| S.D. | : | Standard Deviation |
| S.N | : | Serial Number |
| T.U. | : | Tribhuvan University |
| UA | : | Unutilized Asset |