

# CHAPTER-I

## INTRODUCTION

### 1.1 Background of the Study

Gold smith used to store people's goods and charge nominal rate against the deposit. At that time, people deposited their gold and valuable goods for the security rather than earning. An efficient system of financial institution is obviously necessary not only for industrialization but also help for optimum utilization of financial resources of the community and economic prosperity.

In ordinary, word meaning of term, "Finance", is resource or revenue. It does not signify the coins and notes of the country. But in wider sense, the term finance also includes credit.

"Tejarath Adda" is the father of modern banking system in Nepal, which delivered a good service to government staffs and general public. In reality, the concept of modern banking was introduced when "Nepal Bank Limited" was established in 1984B.S. Since 1994 B.S, NBL carried out the functions as a commercial bank. The mobilization and implementation of efficient and effective monetary policy to upgrade the banking system was essential. For that Nepal Rastra Bank was established in 2013B.S. Since 2013BS, it has been functioning as a government's bank and has contributed to the growth of financial sector. Till this date 2012, 32 commercial bank, 87 development banks and 79 financial companies are providing service.

The open market and liberalization policies directly influence the world economy that creates the environment for the establishment, growth and development of the bank and financial institutions. Bank and financial institutions are the specialized firms that facilitate the transfer of funds from savers to borrowers. They act as a bridge between the savers and users. They collect scattered deposits and give loans to maximize their wealth. The financial institutions in Nepal can be broadly classified into four parts: 'A' class commercial banks, 'B' class development banks, 'C' class finance companies and 'D' class micro-credit development banks and cooperatives institutions ( Adhikari and Shrestha, 2063)

Finance companies are the 'C' class financial institutions that tend to meet the various kinds of consumer credit needs. In a situation when the existing financial institutions, especially commercial banks are unable to decide credit facilities timely and carry capital market activities, undertake merchant banking functions and other allied functions. The present finance companies

are very helpful for those who do not have easy access to the bank. The special feature of finance companies is that they go to areas where commercial banks find difficult and not accessible to lend with risk. Most of the customers prefer finance companies with the notion that taking loan without passing too many procedures often that exist in commercial banks. They stress that the finance companies are the 'C' class financial institutions operating in the overall financial system of the economy. However, they serve as they act as the borrowing and lending financial institutions with additional financial risk taking management. Finance companies can be considered as quasi-banking intuitions. They collect deposit and mobilize, extend loans and advances to business, house, and hire-purchase etc sectors. The principal sources of fund of these institutions beside equity are term deposit collections and issuance of debentures. The resources thus collected and invested in government securities and bonds, issuing guarantee, which are approved by Nepal Rastra Bank for the finance companies. Therefore, finance companies can be considered as complementary to commercial banks to some extends. The growth of business activities necessitated the financial institutions because they are the institutions that supply capital required for business and fund for other purposes.

The groundwork for establishing finance companies was initiated in 2042(1985) with the enactment of Finance Company Act 2042 (1985). Despite the provisions of Act, private sectors were completely silent till 2049BS. On July 1992 with the major shares of public sectors, Nepal Housing Development Finance Company Limited was established under the Finance Company Act, 1985. In the private sector, Nepal Finance and Saving Company Ltd. pioneered in this field and started its transaction since April 1992.

Similarly, Fewa Finance Limited (FFL) was established under the Company Act 2053 and licensed by Nepal Rastra Bank in 2060 BS Baisakh 9 and came into operation in 2060 Baisakh 17 as a national level finance company in Pokhara. The main objective of the FFL is to provide financial support to different productive and needy sector by collecting the small and large saving all around the country for the overall development of the nation under the free economy policy of Neal government. It accumulated scattered saving and mobilized it to various planned sector of economy to support the economic prosperity of the country. Its future plan is to provide the service to all ethnic groups, all places and all kind of people and opening its branches in different parts of the country. It even planned to increase the paid up capital according to the direction of Rastra Bank of Nepal. FFL collected deposit under various deposit products and

invested it in different sectors like hire purchase, housing loan, business loan, industrial loan etc. The company has a very aggressive plan of expansion of branches with its service in future. The study will mainly focus on institution's performance in term of fund collection and lending structure in various sectors.

**Table : 1.1**  
**Types of Deposit Account**

Types of Account	Interest per Annum in %	Min. Balance
Normal Saving Account	9.5	Rs.1000
Fewa Special Saving Account	9.5	Rs.0
Easy Saving Account	9.5	Rs.1000
Shareholder Saving Account	9.5	Rs.0
Fewa Attractive Saving Account	9.5	Rs.1000
Corporate Saving Account	9.5	Rs.0
Shuva Laxmi Saving Account	9.5	Rs.1000
Ex-Army Saving Account	9.5	Rs.1000
Fewa Plus Saving Account	9.5	Rs.5000
Fewa Smart Saving Account	9.5 to 11.0	Rs.1000
Fwea Jestha Nagarik Saving Account	9.5	Rs.500
Fewa Nari Saving	9.5	Rs.100
Fewa Super Saving	9.5 to 11.0	Rs.20000
Fewa Children Saving	9.5	Rs.100
Fewa Utkrista Saving	9.5 to 11.0	Rs.0

*Source : Brochure of FFL, 066/67.*

**Table : 1.2**  
**Scheme on Fixed Deposits ( in %)**

Fixed Deposit	Monthly	Quarterly	Yearly	On Maturity
9 Months		12.5		
6 Months		11.5		
3 Months		11		
1 Year	13	13.5	13.6	13.6
5 Year	13.6	13	13.9	14.1
4 Year	13.5	13.7	13.8	13.9
3 Year	13.4	13.65	13.7	13.8
2 Year	13.25	13.6	13.62	13.7
Special One year fixed Deposit	13.10 to 13.60			

*Source : Brochure of FFL 066/67.*

**Table : 1.3**  
**Types of Loan provided by FFL**

S.NO	Type of Loans	S.No	Types of Loans
1	Hire Purchase	10	Social Loan
2	Home Loan	11	Foreign Employment Loan
3	Business Loan	12	Personal Loan
4	Industrial Loan	13	Medical Loan
5	Educational Loan	14	Real Estate Loan
6	Health Loan	15	Project Loan
7	Tourism Loan	16	Loan Against Fixed Deposit
8	Hydro Electricity Loan	17	Others
9	Agriculture Loan		

*Source : Brochure of FFL 066/67.*

FFL plays a vital role to combat all kind of difficulties and challenges including the people from low income to the capitalists and also to help strong than the economic status of the country. Not only in one particular area, Fewa Finance is also providing its services from six branches and in the future it is planning to facilitate in all the districts in Nepal. The promoters of Fewa Finance

include successful businessmen, traders, social workers and professionals having long experience in finance. Ongoing technological development in the world is the most challenging fact in every sector in the developing countries. But there is no other way to implement it because of its positive impacts. So Fewa Finance is also implementing the technology and providing the ATM facility for four different places.

Its head office is located at Chipledhunga, Pokhara, Kaski District, Gandaki Zone. This finance company is being handled by the 6 board of directors (BOD) and 12 founders who are well leading and reputed industrialists.

## **1.2 Statement of the Problem**

Financial institutions collect the deposit from the public and invest it in different sectors. There are many ways of collecting the fund. In this competitive age, every institution is adopting the attractive schemes and facilities to attract the depositors. The institution is responsible for the investment done. Not only for investment, institution is also equally responsible to refund the depositors collection as demanded. So, to manipulate the collected deposit and loan is major challenge to the institution.

**'Lending Policy of Fewa Finance Limited'** is the statement of this work. In this thesis following are the relevant matters to be investigated:

1. What are the sources of lending?
2. What are the major areas of lending and its priority sectors?
3. What is the loan recovery pattern of FFL?
4. What is the position of outstanding loan?

## **1.3 Objective of the Study**

The study of certain matter should centralize to achieve specific purpose. Without determination of specific objective, the study would be meaningless. The main objective of the study is to know the trend of deposit collection and lending of Fewa Finance Limited. However, the other specific objectives of the study are:

1. To analyze the sources of lending fund of FFL.

2. To analyze the lending portfolio of FFL and its priority.
3. To interpret the loan recovery of FFL.
4. To analyze the outstanding loan of FFL.

#### **1.4 Significance of Study**

It is the analysis of the institution based on the static data, which helps to lead the institution on the effective way. Report from the research is highly acceptable if all the tools are used properly and appropriately. The research is the clean mirror of the particular institution. SWOT (Strengths, Weaknesses, Opportunities, Threats) analysis of the institution is possible with the help of this research.. This dissertation is based on deposit collection and lending. So it states the policies implemented on collecting deposit and providing loan of the institution and even analysis of the strategy.

In the context of Nepal, very few studies and researches have been made related to loan disbursement and collection procedure of FFL. Out of this, there are some positive impacts of studies;

- ) To the company (FFL)
- ) To the interested entrepreneur and businesspersons.
- ) To the policy makers.
- ) To the interested persons and scholars.

#### **1.5 Organization of the Study**

The study will follow the research structure (format) prescribed by the university. The body of reports will be classified into five chapters. The title and the contents of each chapter of this study are briefly mentioned here;

- **Introduction:** It covers general background, statement of problem, objectives of the study, significance of the study, limitation of the study and general assumption about the study. This is the first chapter of the study.
- **Review of Literature:** It is the second chapter of the study devoted to review the conceptual framework for the study. The books, journals and available research documents have been reviewed and presented in this chapter.

- **Research Methodology:** It contains those methods which make the convenience for the comparison of the performance made. This chapter contents research design, population sample, method of data analysis and various financial and statistical tools and techniques applied.
- **Presentation and Analysis of Data:** It is devoted to the presentation, analysis of collected data. It also incorporates with the major findings. For this purpose, various analytical tools have been used.
- **Summary, Conclusion and Recommendations:** It covers the findings, summary and conclusion derived from the study. Lastly, depending upon the findings, recommendation for further improvement in future is prescribed.

Besides these, bibliography and appendices will also be present at the end of the project. Similarly, acknowledgement, table of contents, list of tables, list of diagrams, abbreviation will be presented in the front part of the project report.

## 1.6 Limitations of the Study

The study is based on case study of FFL, which may not represent the overall scenario of all financial institutions. The analysis of the study is based on its financial statements and annual reports. Reliability depends on the reliability of the data. Some of the limitations of the project are;

- ) Though there are 79 finance companies, this study considers only one finance. i.e. Fewa Finance Limited.
- ) The study covers the period of only five years. (2062/63 to 2066/67)
- ) The study focuses mainly on deposit collection and loan disbursement of FFL.
- ) The data used in the study is only secondary data based on the information provided by the company.

## **CHAPTER-II**

### **REVIEW OF LITERATURE**

Review of literature is the preliminary search that helps to generate and refine one's research idea on Lending Policy. Many researchers have conducted their research in the field of financial companies focusing on financial performance, fund mobilization etc which are helpful for the study. Some of the relevant studies, their objectives findings and theoretical review have been reviewed under this chapter. To ensure the precious, lucid and concrete view about the stated topic, the entire work is divided into different sub-headings, which is given below:

Review of Conceptual Framework

Review of Previous research

Conceptual review covers the concepts of basic terms used in the study and research review includes the reviews of International Journals, along with Master's Dissertations.

#### **2.1 Conceptual Review**

This sub-chapter presents the theoretical aspect of the study. It covers the historical development of the financial system and evolution of finance companies in Nepal, concept of finance companies, financial products and services and financial performance approaches.

##### **2.1.1 Evolution of Finance Companies in Nepal**

Nepal's formal financial system began in 1937AD. With the establishment of Nepal Bank Ltd. which was the first commercial bank in the country. Nepal Rastra Bank was established in 1956 A.D. under the NRB Act 1955 A.D., and the Rastriya Banijya Bank was set up in 1966 A.D. as the second commercial bank under the RBB Act with a view to expand activities in the banking sector and to provide better banking facilities to the people. In the developing stage of financial institution in Nepal, the establishment of Agriculture Development Bank was another significant achievement. It was established in 1968 A.D. under the ADBN Act 1967AD to address the needs



of Agriculture sector. (Shrestha and Bhandari, 2004)

The mid July 2010 bulletin published by Nepal Rastra Bank shows that there is a tremendous growth in the number of financial institutions in the last two decades. At the beginning of the 1980s when financial sector was not liberalized, there were only two commercial banks and two development banks performing banking activities in Nepal. There were no micro-credit development banks, financial companies, co-operatives and non-government organizations (NGOs) with limited banking transactions. After the liberalization of the financial sector, financial institutions have made a hallmark progress both in terms of the number of financial institutions and beneficiaries of financial services.

Economic Liberalization policy of the government has encouraged the establishment and growth of finance companies in Nepal within a short span of time. So, establishment of finance companies are the major outcomes of the economic liberalization. The groundwork for establishing finance companies was initiated in 1985AD. with the enactment of Finance Company Act 2042BS. Despite the provision of Act; private sectors were completely silent till 1992AD. On July, 1992AD. with the major shares of public sectors, named Nepal Housing Development Finance Company Limited was established under the Finance Company Act 1985. In the private sectors, Nepal Finance and Saving Company Ltd pioneered in this field and started its transaction since March 1992AD. (Pant, 2067)

### **2.1.2 Concept of Finance Companies**

As per NRB classification, Finance companies are the 'C' class financial institutions which borrow funds so as to profit on the difference between the rates paid on borrowed funds and those charged on loans. However, they act as the borrowing and lending financial institutions with additional financial risk taking management. They came into existence under the Finance Company Act, 1985 and now are being operated under Bank and Financial Institution Act, 2006. They are registered as limited companies at the office of the Company Registrar Office (Pant, 2067).

A finance company can accept deposits of the maturity of three months to maximum six years. They can also collect fund by saving nature called deposit and issuing debentures. Some of the

finance companies deal with leasing finance as well. They offer more attractive rates on deposit than the commercial banks.

The primary function of the finance companies is to make loan to both individuals and businesses. These companies are popular among low income and medium class people for financing hire purchases, vehicles, machinery, tools, equipments, durable household goods etc. They can also perform merchant banking activities with prior approval of NRB. They are willing to lend to riskier borrowers than commercial banks. They are free to fix interest rate on both deposit and loans. As per the NRB unified directives for banks and financial institution issue directives No8/2005/06(July 2006 AD.), there is no any restriction for finance companies to invest in government securities and Nepal Rastra Bank bonds. However they have to perform their activities as prescribed by the NRB directives. (Neupane, 1995) The finance companies in Nepal are established with the slow growth and traditional attitude of commercial banks in mobilizing financial resources, lack of financial innovations and growing interest of the public on Upahaar and Dhukuti programmes. (Upadhaya, 2004) Finance company is established with a view to provide easy access to fulfill individual credit needs, provide attractive return incentives and favorable terms on deposits, encourage consumers to strengthen their purchasing power. On the other hand, finance companies are the market maker, investigator and user of money market and capital market. Financial companies are those intermediaries, which link the savers and users of capital. They collect small and scattered saving of the individuals and mobilize it in the productive sectors in the form of investment or loan. (Upadhya, 2004).

### **2.1.3 Bank and Financial Institution Act, 2006**

Bank and financial activities are governed by rules and regulations which are reviewed from time to time to reflect the changing economic environment. Previously, Finance Company Act, 1985 used to govern finance companies in Nepal. Due to the absence of parliament, Bank and Financial Institutions Ordinance (BAFIO) came into existence in February 4, 2004. The ordinance is renewed in every six months. BAFIO governed all types of financial institutions. It aimed to ensure reliable and quality banking and financial intermediation services through healthy competition among banks and financial institutions safeguard and promote the interest of the depositors and people at large in the overall banking and financial system of the country. The

ordinance repealed and replaced all existing Acts related to Commercial Banks, Nepal Industrial Development Bank other Development Banks and Finance Companies which brought all such institutions under one single Act is known as Umbrella Act. As per the Umbrella Act, banks and financial institutions are to be classified as A,B,C and D class on the basis of minimum paid up capital. Accordingly, commercial banks are in the 'A' class and they are labeled as banks. Similarly development banks, finance companies and micro credit development banks are categorized into 'B', 'C' and 'D' respectively and they are called financial institutions (BAFI, 2006) Till the date 2012, there are 33 commercial banks, 87 development banks, 79 finance institutions, 21 micro credit development banks, 2876 saving and credit co-operatives and 38 NGOs which are providing financial services in Nepal.

For the proper and smooth operation of bank and finance institutions, an Umbrella Act named Bank and Financial Institution Act, 2063 has been enacted, which is effective since 30<sup>th</sup> July, 2006. As per the Act, well performing bank or financial institution may be upgraded if it has met capital requirement, has been in profit for the last 5 years in a row, total non-performing assets have remained within the NRB prescribed limit and all the prescribed conditions have been met. Similarly, NRB can downgrade any bank or financial institution from 'A' to 'B' or 'B' to 'C' class if its status of performance is found to have turned totally other way around against as prescribed. Subject to this Act, Class 'C' licensed institution may conduct the following types of financial transactions;

- ) Accept deposits with or without interest and refund such deposits, subject to the limit prescribed by the NRB.
- ) Supply credits other than hypothecation credit as prescribed.
- ) Supply credits for businesses relating to hire-purchase, leasing and housing, as well as for service enterprises.
- ) Engage in merchant banking business.
- ) Write off credit on the basis of co-financing by joining hands with other licensed institutions according to the agreement concluded for the purpose so as to divide the collateral pari passu.
- ) Supply credit against the guarantee provided by any bank or financial institution.
- ) Obtain credits by pledging its movable or immovable assets as collateral.

- ) Supply a fresh credit in a lump sum or in installment against the security of the same movable or immovable assets, which have already been pledged with it or with any other licensed institution to the extent covered by the total value of such security.
- ) Proper manage, sell or lease out its assets.
- ) Issue, accept, pay, discount or deal in bills of exchange, promissory notes, cheques, traveler's cheques, drafts or other financial instruments.
- ) Deal in Indian currency.
- ) Supply credits not exceeding the amount prescribed by the Rastra Bank to ensure the economic upliftment of the destitute class, low income families, victims of natural calamities and inhabitants of any area of the country with the provision of individual or collective guarantee.
- ) Exchange with the Rasta Bank or any other licensed institution particulars, information or notices regarding debtors or customers who have obtained credits or any other facility from it or any other licensed institution.
- ) Supply installment or hire-purchase credit to any individual, firm, company or institution for vehicles, machinery, tools, equipment, durable household goods or similar other movable property.
- ) Supply credit to any individual, firm, company or institution for the purchase or construction of residential house or go downs, or for the purchase of lands for the construction of such residential house or go downs.
- ) Supply credit (leasing-finance) to any individual, firm, company or institution for taking up vehicles, machinery, tools, equipment, durable household goods or similar other movable property on lease, or provide such movable property on lease.
- ) Prescribe condition according to need in order to protect its interests while supplying credit to any individual or institution or carrying out a transaction with him/her/it.
- ) Operate projects such as those relating to purchase of land and construction of building for land development and residential purposes, and sell or manage such lands and buildings, or make arrangements for doing so.
- ) Perform such other functions as are prescribed by the Rastra Bank.

This section deals with the meaning of various financial indicator of institution. Fewa Finance has always been committed to providing quality products and services for its customers. Even

the pricing of the product is done giving due consideration to the consumer segments and nature of the products. All the staff members are encouraged to provide new ideas and concepts on existing and new products of the institution. In order to make a product successful in the market, the structure of decision-making and service delivery across different levels need to be well designed.

Some of the financial indicator designed to suit the growing and ever changing needs of the institution are given below;

#### **2.1.4 Deposit**

Accepting deposits or borrowing from the public is one of the most important functions of a bank. Banks borrow funds from the public by means of different kinds of deposits such as current account, fixed deposits account, saving account etc. Nepal Rastra Bank has the power to fix interest rate on deposits in order to avoid unhealthy competition among different banks and no bank can pay interest on various deposits in excess of the rate prescribed by the NRB. Various deposits accounts are as follows;

##### **a) Saving Deposit Account:**

Saving bank accounts are monthly opened by households, lower and middle class people with the intention of saving the present income to meet their future demand and also to earn some interest at nominal rates. These are repayable on demand and money can also be withdrawn by cheque. Finance companies accept saving deposit from individuals and organization. The main purpose of saving deposit is to encourage the habit of saving among the common people and institutions. Depositors can deposit any amount in their accounts anytime. But they can withdraw their money up to a limited amount in certain period. Prior information is required incase of withdrawal beyond the restricted limit. Finance companies are allowed to accept saving deposits not exceeding 2.5times of their core capital. They provide interest on daily balance basis on saving deposit.

##### **b) Fixed Deposit Account:**

Fixed deposits are also known as time deposits or term deposits. They carry a fixed maturity. A penalty is charged for early withdrawal. Savers that do not need money for a stipulated period from 3 months to longer periods ranging up to 6years are encouraged to keep it in fixed deposit. This type of deposit offers higher interest rate than saving account. Longer the maturity period,

higher will be the rate of interest. However the depositor can take 90 percent loan from the finance companies against the security of fixed deposit receipt. The money on a fixed deposit is payable by the bank on the expiry of the period. The interest on the fixed deposit account is usually paid on maturity. But as per request of the depositor the institution may pay interest to every three or seven months or may even credit the amount of the interest to the current or saving account. But if the depositor has not withdrawn the money from the fixed deposits even after the maturity, the bank is not bound to pay interest on it. The bank shall allow interest on such deposits for the overdue period provided the deposit is renewed for a further period.

**c) Recurring Deposit Account:**

Various types of recurring deposit schemes are introduced by finance companies. The scheme of recurring deposit is designed in order to motivate the small savers to save regularly some amount. The rate of interest under this account varies according to the period for which the account has been opened. The person opening recurring deposit account has to deposit every month a fixed amount (usually in multiple of Rs.100 or Rs.1000) for the specified period. The period ranges for 1 to 10 years.

**d) Current Account**

Current accounts are also known as demand deposits because the deposits in current account are payable on demand. These accounts are opened by businessmen and traders and can be operated any number of times. Various services are provided by the bank to the current account holder, if sufficient amount of money is available in the account such as paying all cheques drawn, issuing drafts on behalf of the account holder etc.

**2.1.5 Loan**

Loan means the repayable liability that is brought by accepting. It means that loan is the repayable liability, which is to be repaid along with some additional amount that is gained in the present. In other words, loan distribution or investment means providing the credit facility of money to the people in mutual agreement to repay the amount along with some extra benefits and return in the future. It is financial asset resulting from the delivery of cash or other assets by a lender to a borrower in return for an obligation to repay on specified date or demand. The banks or financial institutions lend the fund as investment, which is called loan. Financial institutions do not keep cent percent reserve against deposit for meeting the demand of

depositors. The excess reserve than depositors is granted as loan investment from banks. So the term loan plays an important role in banking sector.

Banks make a wide variety of loans to a wide variety of customers for several different purposes. For customers, the cause of loan purchasing may be investment in business, purchasing automobiles, taking dream reactions, pursuing college education, constructing home and office building etc. On the basis of loan purposed; financial loan can be divided into seven broad categories

**a) Real Estate Loan**

It is the credit extended to purchase or improve real property, such as land building. Such loans are secured by real property land, building and other structure. Real estate loan includes long term loan to finance the purchase of farmland, houses, apartments, commercial structure and foreign properties. The interest rate will fluctuate according to economic condition and situations. It is issued in installment basis and repayment will also be in installment with interest.

**b) Financial Institution Loan**

It is the credit extended to financial institution and other financial service providers. Mostly, finance companies, insurance, companies credit banks, co-operative firms saving and credit firms are the customers of financial institution loan provided by the bank.

**c) Agriculture Loans**

Agriculture loan is the credit extended to support farm and branch operations. This loan is extended to assist in planting and harvesting crops, storing crops and marketing them. Agriculture loan also supports the feeding and care of livestock.

**d) Commercial and Industrial Loan**

These loans are extended to business firms to support the production and distribution of their products and services. Such express as purchasing inventories, paying taxes and meeting payrolls too.

**e) Individual Loans**

This is the loan extended to private individuals for private and household purpose. Generally, individual loans are extended to finance the purchase of automobiles, appliances (TV, computer set, washing machine, refrigerator etc). Customer can also use individual loans for medical care, personal expenses.

**f) Miscellaneous Loan**

All those loans which are not classified above are included in this category. Higher education loan, marriage loan, dreams tour loan can be included in miscellaneous loans.

#### **g) Lease Financing Receivables**

Financial institution can lend physical equipment to the customer, in addition to money lending. People do not buy the heavy and costly equipment that is seldom needed for them. For example; curser machine, pressing machine and other plants use for construction etc. They prefer to get them on pledge. Banks may provide such equipment and vehicles on lease to customers.

According to the NRB unified directives for Banks and Financial Institutions issue directives No 15/2005/06 ( July, 2006 AD.). Finance companies are free to fix interest rates on both the deposits they take and the loan they provide. So, the rate of interest on both the deposits and loans will vary from one finance company to another. (Pant, 2010)

#### **2.1.6 Deposit and Lending Trend**

Deposits are the main source of funds. By providing certain rate of interest, finance company calls deposit from the customer. Usually fixed deposits are used for lending the money to different sectors. The deposit will end to increase the working capital of the company. The finance company is authorized to receive deposit from the public and to transfer the economic upliftment of the country by offering loan and advances to the needed people. Finance company is that institution which receives the saving from the public usually in fixed deposit to pay some rate of interest. Therefore it draws money from the people who do not use it at the time and lend it to those who are in position to use it for productive purpose.

The investment or lending is one of the main functions of the company. Only the acceptance of deposit is not sufficient for the company but it should refund the deposit including certain rate of interest. So, it is a significant task of the company to utilize the deposit in the proper way where it can earn more profit. Without the proper utilization of deposit it will not be in position to return the money to the customer. But the investment or lending is not simple and easy rather it is very risky.

##### **2.1.6.1 Guiding Principles of lending Policy**

The lending business is very risky. Therefore, commercial banks should adopt sound policy regarding loans. The loans, which are provided by the commercial banks, involve several



considerations such as length of the time, types of borrowers, kinds of security etc. Generally a sound lending policy of bank is guided by three major principles. They are as following.

- a. Safety or security
- b. Liquidity
- c. Profitability

#### **a. Safety or Security**

The first principle of lending is safety or security. When commercial bank is going to lend some money to the borrower, direct attention must be given towards the security of the loan. For the safety or security of loan, bank examines the economic condition and capability of the party. Moreover, the bank demands for collaterals. Gold and silvers are readily acceptable collaterals. However, other goods are also taken as collaterals by the Commercial Banks. For such goods, the bank studies the prevailing market price first, then the bank grants loan to the lender. To minimize risk, Commercial bank advances the market value of the security. The value, which is reduced by the bank for the purpose of safety is called margin. (Nepal Rastra Bank fixes the margin rates according to the needs of the country). The margin rate depends on the nature and durability of goods and capacity and behavior of the party.

#### **b. Liquidity**

Liquidity generally means capacity to produce cash on demand for deposits. Bank provides loan from the deposit of depositors. The bank should return back depositor's money promptly if they demand. So, the bank has to maintain the capacity for payment as the demand of depositors. Over liquidity causes the lack of proper lending opportunities. On the contrary, under liquidity causes the less faith by depositors and shareholders upon the bank. So, the bank should maintain proper degree of liquidity. Generally, liquidity of a bank is measured by the ratio of loan to total deposits of the bank. The higher is the ratio the lower is the liquidity and vice-versa.

#### **c. Profitability**

Only safety and liquidity are not sufficient for a sound and viable lending policy of a bank. Profitability is also equally important. Therefore the bank should give attention to profitability too. (The profit of a bank partially depends upon the volume of investment; the higher the

volume of investment the greater will be the rate of profit). The bank earns profit from the difference of interest rates between lending and deposits. Profit is necessary to sustain the bank.

Beside these, the bank should also consider other principles while lending.

- Principle of diversification
- Principle of marketability
- Principle of price stability
- Principle of tax facility
- Principle of national interest

### **2.1.7 Criteria for Providing Loan**

Set-up of well established criteria for disbursing advance and loan is the most essential to survive, thrive and enlargement of the bank. Loan should not be allowed to all demanding parties. Ergo well defined and setup criteria to grant loan which be must visible to the personnel.

#### **1. Personal Character**

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

#### **2. Capacity/Competency**

Whether the person is capable in making contract according to contract Act 2056 or not should be checked out at first considering the patent and expertise of persons in concerned field, decision about the flow of loan is to be taken.

#### **3. Capital**

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

#### **4. Security**

Priority should be given to readily marketable and handy collateral. Decision about the flow of

loan is made considering nature of business and types of securities proposed. Banks accept having securities above and near about and denies the loan proposal containing inferior quality security.

## **5. Credit Information**

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

## **6. External Environment**

External environment of industry of business shown by loan proponent needs to be evaluated on the eve of providing loan to know the facts about use of right business. It is pivotal to evaluate external environment of business where business origins, thrives and survives since modification of external environment is almost impossible in accordance with own motto and plight.

### **2.1.8 Loan Approval Process**

The approving authority approves loan only after being convinced that the loan will be repaid together with interest. There are many proceed involved to approve the loans which have been appended below.

#### **1. Application**

A borrower is normally required to submit an application to the bank along with required documents: project proposal, historical financial statements and documents pertaining to company's legal existence.

#### **2. Conducting the Interview**

The documents submitted give much information about the borrower, but collecting information by interviewing the borrower is of great importance. Normally, such an interview takes place at the bank premises. Many pertinent questions as possible should be asked during the initial interview. The questions should covered the following contains:

- ) Loan Purpose
- ) Loan Amount

- ) Repayment Sources
- ) Repayment schedule
- ) History of the business
- ) Banking relationship

### **3. The Credit Analysis**

There is a practice of analyzing five Cs of credit by the financial institutions. Except them, historical analysis is also conducted credit analysis. These five Cs are considered as below.

- Character: It refers to the personal traits ethics, honesty and integrity of borrowers, which is very important for lending decision.
- Capacity: It is being used in two sense
  - Legal capacity to borrow money
  - Capacity to generate enough income to repay loan or through liquidation of assets.
- Condition: It refers to the general economic condition beyond the control of the borrower that affects the business of the borrower.
- Collateral: Loan is given if the banker is satisfied that the borrower can repay money from the cash flow generated from operating activities. However, the banks want to ensure that their loan is repaid even in case of default. In such cases the bankers ask for additional securities. Collateral can be fixed in nature land, building, machinery or working capital like inventories and account receivables.
- Capital: It refers to net worth of the borrower. This is covered under capacity above while analyzing the leverage ratio.

### **4. Forecasting and Risk Rating system**

Based on the findings of historical analysis and in light of present and foreseeable future environment, the analyst has to forecast impending major risks. The analyst should also highlight to what extent inherent risks will be mitigated and how unmitigated risks can be covered.

### **5. Return**

The amount of loan has got inherent cost as it is obtained from either shareholder or depositor or creditor. The analysis should be made to calculate total return (interest, fee and commission) and

compare whether it meets bank's standard.

## **6. Liquidation**

The analyst should ascertain bank's ability to recover loan in case of liquidation of the borrower. If liquidation analysis reveals insufficient security, additional security may be asked for.

## **7. Creditworthiness and Debt Structure**

If the analyst finds the borrower creditworthy and decides to extend loan, he should structure the debt facility to be extended.

## **8. Preparation of Credit Report**

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

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

- ) Evaluation of loan proposal
- ) The types of loan
- ) Determination of necessary documentation

### **2.1.9 Terms and Conditions to Disburse Loan**

There are few reasons for inquiring various terms and conditions in extending loan to any firm or person in order to keep their loan safe and to be repaid in time. Different financial institutions have different terms and conditions to suit their own situations, which fulfill the purpose in the prevailing economic, social, political, and other environmental factor. With this view in mind, financial institutions should impose following terms and conditions (Basu, 1957).

#### **Amortization Period**

Every loan does have certain amortization period. Any sort of loan extended by company should be repaid within a stipulated time. The borrower should repay the loan within the amortization

period. Company takes some sort of action, if it delays the repayment for a longer period of time. The fixation of amortization period is very crucial task. Any kind of mistake in fixation of this period creates so many problems in making loan repayment. Therefore, while performing this delicate and vital task, the special attention should be taken by the company. However, the amortization period is fixed on the basis of expected earning of the firm/person as revealed by the financial statement like cost, sales and profitability statements.

### **Interest Rate**

As much as loan delays in making repayment of principle dues, so much will be movement. The longer the delay in making repayment of principle dues, higher will be movement in the total amount of interest to be paid along with the principle amount. If the borrower can repay the loan earlier, their amount of interest to be paid will be decreased.

Whether it is for the purpose of meeting various expenditure of the company or to meet shareholder obligation of to motivate quick, repayment interest rates should be set in accordance with cost of capita. The low rate of interest can be bread uneconomic project that are viable only because they are subsidized.

### **Security**

The first thing which company generally looks into is the safety of itsloans. Mostly company insists upon adequate security for the loans it provides. But security is not the only thing to go for rigidity of the finance companies should satisfy with various technical, managerial, economic and social factors of the project. If the project is supported on the basis of the security and not with proper care about above-mentioned factors, fails to run, then no doubt that the lender or financial company can realize the loan amount by selling the securities.

### **Legal authority of the borrower**

Such requirement will definitely avoid unsound, unproductive and uneconomic projects to come up. The breeding of uneconomic and unsound projects can be minimized by the way of legal authority to borrow from the related department of ministry of government. But the length and tedious process might cause uneasiness on the part of borrower to come up with genuine project.

### **Soundness of Project**

Technically, managerially and economically, sound projects are those, which deserve special interest of the development by finance company to extend necessary financial help. No finance company wishes to waste its resource in an unsound project. It is always as a condition that any

business or industrial venture applying for loan with the finance company must be sound enough to contribute to the economic development. Every financial institution or company looks at the first hand that whether the particular project is technically, managerially and economically sound or not. That's makes easy to the loan repayment timely.

### **Repayment Capacity**

Repayment capacity can also be taken as a condition for extending loans. It is considered that the repayment of loan is the ultimate evidence of the right allocation of fund by financial company and the source or industrial venture. So the finance company always thinks about the repayment capacity of the borrower before granting loans.

In this way, we see that the finance companies of any country impose several terms and conditions in order to keep their loan safe and to make it properly utilized and ultimately to get them return in time.

## **Regulation Relating to Loan Classification and Loan Loss Provisioning**

### **1. Classification of Loans**

Effective from FY 2062/63, banks should classify outstanding principal amount of loans and advances on the basis of aging. Loans and advances should be classified into the following four categories.

#### **Pass**

Loans and advances whose principal amounts are not past due and past due for a period up to 3 months should be included in this category. These are classified and defined as performing loans. For this type of loan, minimum 1% of provision for loan loss should be maintained.

#### **Sub -Standard**

All loans and advances that are past due for a period of 3 months to 6 months should be included in this category. For such loans, 25% of loan loss provision should be maintained.

#### **Doubtful**

All loans and advances that are past due for a period of 6 months to 1 year should be included in this category. Minimum 50% of loan loss provision should be maintained for such loans.

## **Loss**

All loans and advances which are past due for a period of more than 1 year as well as advances which have least possibility of recovery or considered unrecoverable and those having thin possibility of even partial recovery in future should be included in this category. 100% provision of loan loss provision should be maintained.

### **2.1.10 Priority Sector Lending**

Thus, with the objectives of mitigating the unemployment, poverty, economic inequality, etc and thus upgrading the deprived and low income people, the project of national development and priority, micro and small enterprises were declared priority sector and the lending to such sector has been categorized as priority sector loan.

With a view to make bank credit available to small agricultural, industrial and services sector and promote income and employment opportunities, the NRB has directed the Commercial Bank to extend a certain percentage (ranging from 7.25 percent to 10 percent) of their total outstanding loans to the priority sector.

## **2.2 Review from Journals and Articles**

The book “Banking Management” explains how well a bank performs its lending function has a great deal with the economic health of the country because bank loans supports the growth of new business and jobs within bank’s territory and promote its economic activity (Vaidya, 1999).

Karki, in her article, “Challenges of non-performing loan management in Nepal”, the course of increasing trend of non-performing loan. She identifies the major courses such as poor loan analysis, guarantee oriented loan system, desire platoon of values assets, misuse of loan, lack of regular supervision of loan (Karki, 2059).

Shrestha, in his article “A study on deposit and credit of commercial banks in Nepal” concluded that the credit deposit ratio would be 51.30% other thing remaining the same. In Nepal that was the lowest under the period of review. Therefore, he has strongly recommended that joint venture should try to give more credit entering into new fields as far as possible, otherwise they might not be able to absorb even the total expenses.

Pradhan (2009) wrote in his article “An Article on Loans” that rural area have poverty. The state and the financial institution must think about the rural people and offer them financial loans. The



rural people need small capital and they cannot borrow it from the conventional banks because they do not have sufficient collateral. It's a good sign that many banks are reaching to the rural area but the delivery mechanism has to be efficient. He believes that micro credit can play a pivotal role in alleviating poverty in our country.

### **2.3 Review of Thesis**

There are various dissertations about loan management of banks written by various researchers in the past years. Some of the dissertations are about the loan disbursement and collection of commercial banks but rarely are there about finance companies. However, there are several dissertations written in the past, which are close to the topic. Some of such dissertations are reviewed here.

Neetu Shrestha (2007) has submitted a thesis named “Deposit Collection and Loan Disbursement of Agricultural Development Bank of Nepal” to P.N Campus. The main objectives of the study are as follow;

- ) To measure the trend of deposit collection and loan position of ADBN.
- ) To assess the process of deposit and loan collection of ADBN.
- ) To analyze the portfolio of loan disbursement of ADBN.
- ) To analyze the main problems of bank in loan collection.

By making them the major objectives, the researcher found both the percentage change except in 060/61 and the contribution to total deposit of current deposit were declining in each and every year. The incremental trend of saving deposit to total deposit seems sound than the other deposits. The incremental trend of fixed deposit found diminishing. However, the contribution to total deposit was relatively stable throughout the study periods. The short term and medium term loan disbursement were found in increasing trend but long-term loan were in fluctuating state. The short and medium term loan collections were found in increasing trend but long term loan were in fluctuating state. The total loan outstanding is found increasing in each and every year. The main problems of loan collection are analyzed as miss-utilization of loan, lack of political sustainability, transfer of branches from remote, competitive environment, lack of reinvestment of loans etc.

Bir Bahadur Karki (2008) submitted his thesis “Deposit Collection, Loan Disbursement and Loan Recovery pattern of Fewa Finance Company Limited and the objectives of the study are as

follows;

- ) To analyze the type-wise deposit collection.
- ) To analyze the process of loan disbursement.
- ) To analyze the performance in terms of deposit collection, loan disbursement and loan recovery.
- ) To analyze the process of loan recovery.
- ) To analyze the main problem in deposit collection, loan disbursement and loan recovery.

The researcher found that Fewa Finance Company Limited has collected a total of Rs.563117 thousands deposit between fiscal year 059/60 to 063/64, increasing at an average growth of 114.81% per annum. In the past five years the deposit collection of Fewa Finance Company Limited continuously increased. The slope trend line obtained from least square trend line is positive which shows increasing trend of deposit collection during the study period. If other remains the same, the deposit collection of institution will increase. Saving deposit, fixed deposit and recurring deposit are types of deposit collection of the institutions. The company collects 35.12%, 64.44% and 0.44 % of deposit respectively form the total deposit collected. The percentage of Recurring Deposit has increased up to the fiscal year 062/63 then decreased and the percentage of fixed deposit has increased up to 061/62 then decreased. Increasing at an average growth rate 96.57% per annum, the institution has disbursed total of Rs.1301278 thousands loan between fiscal year 059-60 to 063/64. In the past five years the loan disbursement of the institution continuously increased. The slope of the trend line obtained from least square trend line is positive, which shows increasing trend of loan disbursement during the study period.

Bandana Paudel (2010) submitted a thesis on “An Analysis of Loan Disbursement and Repayment Pattern of Agricultural Development Bank Limited in Nepal. She made the objectives of her study as follows;

- ) To evaluate the projected and actual loan disbursement and repayment.
- ) To find out the rate of the growth of loan disbursement and repayment.
- ) To analyses the purpose-wise, region-wise, loan disbursement, repayment and outstanding.
- ) To give suggestions and recommendation.

The researcher found the loan repayment amount depends upon loan disbursement. The correlation co-efficient between these two variables is 0.99, which express strong positive relationship between these variables. The co-efficient of determination is 0.9980. There is a positive correlation between targeted loan disbursement and targeted loan repayment. Percentage of actual loan repayment over actual loan disbursement is in increasing trend every year and it is positively correlated. The targeted loan seems weak in Fiscal Year 2062/63 because actual loan disbursement was double than targeted loan disbursement. It was like imaginary situation.

Dhana Prasad Gurung studied on the topic of “Lending services provided by finance companies”: A comparative study of Annapurna and Pokhara Finance company. This has following objectives:

- To analyze the different types of loan provided to customers by Annapurna and Pokhara Finance Ltd.
- To analyze the weighted ratio of different types of loan out of total loan/total assets.
- To analyze the situation of income from lending services.

After analyzing the data using various financial and statistical tools, he has concluded that:

- Both the finance companies are providing various types of loan such as hire purchase, housing, term loan and loan fixed deposit.
- Both Annapurna and Pokhara finance company have granted maximum loan in term loan. But Pokhara Finance term loan lending higher than Annapurna Finance co. Ltd.
- Since the function of finance company is leasing and factoring as well, but it is known through the study that they are not performing such types of activities by Annapurna Finance Ltd. and Pokhara Finance Ltd. being insufficient paid up capital.(Gurung 2005)

Mr. Lal Bahadur Pun in his dissertation entitled “Lending Services Provided by Joint Venture Banks of Nepal” ( A case study of Nabil, Himalayan and Everest Bank Limited) attempted to fulfill the objective of analyzing and interpreting the different types of lending services provided by the joint venture banks and also interpreting the lending practices adopted by those banks in Nepal. He came up with the following finding:

- Out of three joint venture banks, the total deposit of Himalayan Bank Limited has the highest ratio and Everest Bank Limited has the least ratio.
- The loan and advance by all the banks are in increasing trend. Himalayan Bank has the

highest mean ratio with least degree of variation whereas Nabil Bank has moderate and Everest Bank has the least mean with high degree of variation.

- Everest Bank has developed the highest portion of its total deposits in earning activities and the ratio is significantly higher than that of other two banks.

Trend analysis revealed the outstanding performance of Himalayan Bank in all the case experimented except in earning per share. The high degree of growth in loans and advance has put Himalayan Bank in the best position in the lending function of commercial banks. (Pun, 2009)

Mr. Kul Bahadur Khatri, studied in his topic " Investment Policy of Nabil Bank Limited" This has following objectives:

- To analyze the profitability of the bank in the study period
- To verify the NRB directives towards Nabil Bank Limited.
- To analyze the investment composition and its effect.
- To analyze the trend value of different variable related to investment.

Mr. Khatri, analyzed that the profitability position of the return on total assets ratio of the bank has fluctuated every year. But bank's net profit has positive figure in every year. The overall trend of total deposit is increasing. Nabil Bank has been successful in capturing the deposit from the market during the study period. The bank interest income shows the great future of the bank. Investment trend was satisfactory. Nabil Bank invests its fund in government security and non-government security. Out of total investment, highest percentage of investment is in government security. So, its investment is secured investment.

### **Research Gap**

This thesis is based on loan disbursement based on deposit collection. It tries to analyzed and interpretation the relation between the total collected deposit on various schemes and the disbursed loan on different title by the Fewa Finance Limited. It suggests the company in various aspects on loan disbursement. Similarly it advises company the better and effective schemes of deposit collection. This thesis helps the internal and external stakeholder to make decision on investment and policy formation. That is why this is interesting matter to enjoy with this topic.

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

Research methodology is the process of arriving at the solution of problems through a planned and systematic dealing with the collecting analysis and interpretation of the facts and figures. Research is a systematic method of finding out solution to a problem where a research methodology refers to the various sequential steps to adopt by a researcher as in studying the problems with certain objectives in view. Research methodology helps to find out accuracy, validity and stability of research. The justification in the present study can't be obtained without help of proper research methodology.

The main purpose of this chapter is to focus in different research methods and conditions, which are used while conducting the study. To deal with the problem, this chapter focuses on research design, sources of data, population and sample, data collecting procedures and methods of empirical analysis.

#### **3.2 Research Design**

A Research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure.

Research design is the plan, structure and strategy of investigation conceived so as to obtain answer to research questions and to control variances. It is the arrangement of condition for collection and analysis of data.

Research design is an organized approach unrelated part. It is an integrated system that guides

the researcher in formulation, implementing and controlling the study. Useful research design can produce the answer to the proposed research questions. The research design is thus an integrated frame that guides the researcher in planning and executing the research works.

Research design is the plan, structure and strategy of investigation conceived so as to obtain answer to research questions and to control variances. The plan is the overall scheme or program of research. To achieve the goal of the study, the project will apply the descriptive and statistical research design. It describes how the institution collects deposit, what are the strategies applied by the institution in this process. Similarly it describes what are the major sectors selected by the institution for lending, what are the methods and process to get a loan from the institution on the basis of collected data. On the other hand, the research will analysis what are the trend of deposit collection and loan disbursement (lending policy) in the previous five years and also analysis whether the relation between loan disbursement and deposit collection are relevant or not? Basically this project will study the lending policy of NBL, so far that purpose of the study it will apply descriptive and statistical method.

- **Descriptive Method:** It involves the systematic collection and presentation of data to give a clear picture of a particular situation. It is a fact-finding investigation with adequate interpretation of the current situation. This studies attempt to obtain a complete and an accurate description of a situation. To fulfill the objective this study, it identify the various characteristics of the NBL and the various problems on various sectors on lending policy.
- **Statistical tools used:** It is a method which concerns with the question how many items and to observe and how the information and the data items are to be analyzed. This process analysis is adopted to see the trend situation of lending policy of NBL form the F/Y 2062/63 to F/Y2066/67 BS.

### **3.3 Nature and Source of Data**

The data used in present study is secondary data which have been taken mainly form the annual report of the selected bank. Besides these the following sources of data are also considered.

- a. NRB reports and directives.
- b. Various publications dealing in the subject matter of the study.

- c. Various articles published in the newspaper.
- d. Unpublished dissertations of previous years.
- e. Annual reports of FFL: (2062/63 to 2066/67).
- f. Official Website of FFL and Different websites related to the study etc.

### **3.4 Methods of Data Collection**

In this research the secondary data have been used. In order to collect the data, the researcher has used the journals and annual reports published by the finance company.

### **3.5 Population and Sample**

A small portion chosen from the population for studying its properties is called sample and the number of units in the sample is known as the sample size. The method of selecting for study a small portion of the population to draw conclusion about characteristics of the population is known as sampling. Sampling is defined as the selection on part of the population on the basis of which a judgment or inference about the universe is made.

The population refers to the industries of the same nature and its services and products in general. Thus the total no. of financial institutions in Nepal is the population of the study. Among them only Fewa Finance Limited is taken as sample by adapting convenience sampling method. Total number of finance companies is the population of this research.

### **3.6 Analysis of Data**

First of all raw information have been received. After collection of raw information, the processing has been done. Then all collected data have been grouped accordingly to their nature in their tabular and chart by selecting relevant data. The collected data are presented and refined for the propose of the study. This processing procedure is required for sequential analysis of data to meet the objectives of this research

Before they are analyzed, data should be processed. So data processing is an intermediary stage of work between data collection and data analysis. After the collection of data, data analysis is

performed. For the purpose of data analysis, statistical tools are used to make the analysis more effective, convenient, reliable and authentic. To evaluate the financial condition and solve the problem the analytical tools can be used. For the purpose of the study, all collected secondary data are arranged, scanned, tabulated under various heads and then descriptive and statistical analysis have been carried out to enlighten the study. The various steps in processing of data may be stated as:

- ) Identifying the data structures
- ) Editing the data
- ) Coding and classifying the data
- ) Transcription of data
- ) Tabulation of data

There are various tools for data analysis. Depending upon the project spirit, the tools that are effective for comparison are required. The following tools are required for this project.

- ) Measures of Central Tendency
- ) Correlation Analysis
- ) Trend analysis
- ) Graphs, charts and diagrams etc

### **3.7 Tools and techniques employed**

To meet the objectives of the study, data are analyzed by using financial tools such as ration analysis, percentage etc. Graph chart and table were used to support analysis. Similarly some data are analyzed through software package for social studies version. Statistical tools such as mean, correlation coefficient and probable error are also used for data analysis.

#### **Statistical tools**

For supporting the study statistical tools such as central tendency, correlation analysis, trend analysis, tables, diagrams etc have been used under it.

- **Measure of Central Tendency:** Graphical representation is a good way to represent summarized data. However, graphs provide us only an overview and this may not be used for further analysis. Hence, we use summary statistics like computing averages



to analyze the data. Mass data, which is collected, classified, tabulated and presented systematically, is analyzed further to bring its size to a single representative figure. This single figure is the measure, which can be found at central part of the range of all values. It is the one, which represents the entire data set. Hence, this is called the measure of central tendency. The tendency of data to cluster around a figure, which is in central location, is known as central tendency. Measure of central tendency or average of first order describes the concentration of large numbers around a particular value. It is a single value which represents all units (Statistics for Management, 2010)

**Average:** A simple arithmetic average is used to summarize the data as a representation of mass data. A simple arithmetic average is a value obtained by dividing the sum of the values by their numbers (Kothari, 1994). Thus, average is expressed as:

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

Where,

$\bar{X}$  = Simple Arithmetic Mean

$\sum$  = Symbol for summation

n = Total number of Observation

During the analysis of data, mean is calculated by using the statistical formula 'Average' on excels data sheet on computer.

- **Correlation Analysis:** When two or more variables move in sympathy with other, then they are said to be correlated. If both variables move in the same direction then they are said to be positively correlated. If the variables move in opposite direction then they are said to be negatively correlated. If they move haphazardly then there is no correlation between them. Correlation analysis deals with the following.
  - Measuring the relationship between variables
  - Testing the relationship for its significance.
  - Giving confidence interval for population correlation measure.

In this research, Karl Pearson's correlation is used. It is simply denoted by the symbol 'r'.

The correlation between two variables is examined applying following formula;

$$r = \frac{N \sum XY - \sum X \sum Y}{\sqrt{N \sum X^2 - (\sum X)^2} \sqrt{N \sum Y^2 - (\sum Y)^2}}$$

Where :

X and Y are two variables

r = coefficient of variations

N = No. of observation

Properties of Karl Pearson's correlation coefficient

\* Its value always lies between -1 and 1.

\* It is not affected by change of origin or change of scale.

\* It is a relative measure. It does not have any unit attached to it.

- **Tables :** A table is presentation of data in row and column form. The presentation of table is concerned with labeling techniques to make the context clear. The raw data collected should be tabulated so that it will be revealing. The better the organization and sequencing of that data, the better it will be revealing. If the data is displayed in table form, it becomes easier for its analysis.

**Figure :** The term figure usually includes graphs and charts. These presentations help clarify and understand the data at a glance. In other word, figure assists to the reader in understanding the subject.

## **CHAPTER IV**

### **PRESENTATION AND DATA ANALYSIS**

#### **4.1 Data Presentation and Analysis**

This chapter is analytical and important part of the study. According to design and methodology various data are collected and tabulated then analyses are made as per necessary. The variables of loan effectiveness are analyzed on this chapter. For this, type wise deposit collection, purpose-wise outstanding loan, loan disbursement are given.

##### **4.1.1 Interest Rate on Loan of FFL**

The company charges certain rates on various kinds of loan, which is called interest rate. The company charges interest rates by providing loan to the customer. So, it is one of the major profit sources of the company. The loan, which is provided to the customer is highly affected by the interest rate and the loan and advances. If the interest rate charged by the company is very high, the demand for loans and advances will be low and vice-versa. When the company charges the interest rate, it should cover:

1. The cost of fund loan.
2. The cost of service for different kinds of loans.
3. A reasonable margin of profit.

##### **4.1.2 Security and Major Requirements**

FFL wants that, its loan to firm/person are adequately secured. It requires a liquidable mortgage on land, building, vehicle and fixed securities. Loans are secured by fixed securities and assets of individual borrowers. The volume of such security is determined by the company according to the prevailing market price and keeps a minimum margin of thirty percent (30%) on loans. The policy of FFL is admirable. Even the margin of thirty percentage on loan is justifiable because the price of security may go up and down (during the loan period ) within the repayment period.

##### **4.1.3 Loan Disbursement Procedure**

It requires guarantee of repayment by parties. There is no uniform rate of interest. It varies with circumstance, size or risk, type of loan etc. Loan and advances are the main source of earning

profit of the company. If any parties want to take the loan, first of all application should be given with full particulars eg: applicant's name, occupation, address, period and purpose for which the loan is required, amount required, how payment is possible.

The company from the client wishing to obtain loan recovers statements of movable and immovable property and of liabilities and record in the application for loan received register book. The manager endorses the intimation of such effect to the loan application after receiving a favorable report from the credit department regarding the confidential inquiries made by it. It lends money on the basis of three fundamental points:

1. What is the money wanted for?
2. How long it wanted for?
3. What is the source of repayment? After then the company can ask for security available or not?

Decision has to be made for the sake of providing loan to whom and under what circumstances it should lend. The lending officer must have knowledge about the nature of customer and its position.

The company disburses loan for various purposes and purpose-wise. Such as for new and second hand car, van, bus, minibus, tractors etc purchase. It gives housing loan for personal and institutional building and ware housing construction, repair, maintenance, land and building purchase. Agricultural loans are also provided for the development of agro-industry. Business and industrial loans are provided for working capital and fixed capital, which helps for the expansion of business and industry. It also gives education loans for higher education within the country and outside too, such as MBBS, CA, Nursing etc. Tourism loans are also provided for the development of tourism sector such as expansion of hotel, lodge, restaurant and travel agencies. It also gives other loan for social work such as Wedding, Bratabandha, Pasni etc. Loan against fixed deposit are also provided.

In hire-purchase loan, company demands a quotation from the vehicle suppliers for the new vehicle and photocopy of blue book for the old vehicle and other necessary document such as photocopy of citizenship of applicant and guaranteed person, income source paper, passport size photograph of applicant and guaranteed person. The company provides loan maximum of 80% of quotation price for new vehicle and 70% of valuation amount for old vehicle. It provides 70% of quotation price or valuation amount for old commercial vehicle and 80% of quotation price of

valuation amount for private vehicle.

In housing loan, company requires building's map, acceptance letter from municipality, passport size photograph and citizenship certificate of a applicant, income-source paper, photocopy of certificate of the land ownership ( Red-Book ), receives of land revenue payment and blue print (map) of land etc. The company provides loan maximum 80% of building construction and repair maintenances cost.

#### **4.1.4 Loan Recovery Procedure and Policy of FFL**

Loan is defined as the amount expected to be repaid with interest. In each loan modalities for repayment is mentioned which is affected by the nature of debt. In case of term loan, housing loan and hire purchase loan, payment is received in the form of installments as per pre-fixed monthly schedule while in working capital, interest is paid monthly while principle is paid at any time before expiry of the facility. In case of part payment interest is paid first and remaining amount is utilized to reduce principle outstanding.

In loan recovery system, company has implemented the principle of prize and penalty. Generally the laborious and efficient customer are supposed to be winner and the inefficient customer who neglect their occupation is penalized. As a result, the first category of customer will work in their business with heart and soul. The provision of prize and penalty system leads to competition among the customer to utilize the amount of loan in most effective manner.

All the customers of company are not good, so the loan classification is based only on overdue loan of previous year and to overdue of this year. From the classification of loan following are the action to be taken.

**a) First Reminder Letter:**

After one month of the due date, a reminder letter is sent and offered him to pay the loan as soon as possible.

**b) Second Reminder Letter:**

From the classification of loan this type of loan is overdue and after a month, letter is sent again to the customer to pay the overdue loan immediately and retain good relation.

**c) 'Notice of 35 Days' Publish on Newspaper:**

After the above actins, if the loan cannot repayment, the company publishes the notice in newspaper for the collection of loan within 35 days. But an information letter should be

sent before the notice published or after 60 days of second reminder letter. A copy of newspaper should be sent to the loan holder and the receipt letter should keep in his file. If the loan holder pays satisfactory amount within 35 days, the company can stop the further process.

**d) Auction of Collateral:**

After 35 days of the notice if the loan holder is unable to pay the amount of the company, the auction process begins. In a field office there is a loan committee representing by manager, chief of loan and account. First of all, the collateral which was secured by loan is revalued and the project also inspected. From the report of revolution and inspection, the loan committee of office makes decision to auction the collateral. After the decision, the process is run to central level auction of collateral committee. The committee fixes the date of auction and decision to auction the collateral. After the decision the information of the decision should be sent to the loan holder or his family within three days. Company publishes the notice of auction in national newspaper after seven days of decision giving the information about auction place, date, time and collateral.

If the revaluation of collateral on auction time is less than the loan amount, only collateral revalued amount of loan is processed for auction and other rest loan is collected from other process.

If the loan cannot be repaid by the effort of company, the company can appeal the case to the Loan Collection Court of the justice, which is established by Nepal Government with three members from the Law, Banking and Accountancy. The application should be given for overdue loan before this Act within three years and after the act within three years from overdue date. The company should pay 0.25% of claimed amount for loan collection charge with the application. Within 15 days from application the court of justice declares the case. After the order received from court, the loan collection officer should collect the loan from loan holder and pays to the bank or FI. For this he could adopt the following procedures;

- i) Adopting or auctioning the pledge secured or other fixed or current assets of proprietor.
- ii) Adopting or auctioning the fixed or current assets of guaranteed person.
- iii) To arrest and keep in jail to the loan holder or guaranteed person according to law.

After receiving the loan amount, the company should pay 1% of loan to the court of

justice as a loan collection charge.

#### 4.1.5 Deposit Collection of FFL by Type-wise

Deposit collection is one of the major functions of finance companies and it is the primary source of fund. Finance companies collect deposit of public in different forms like saving deposit, fixed deposit, recurring deposit, etc. Recurring deposit is one of the deposit scheme on which customers deposit fixed amount monthly till fixed period ( i.e. two or three years) and repayment with interest after fixed maturity period.

Deposit collection is to be well managed since it is the liability of the finance company and there is involvement of cost in term of interest earned which is to be paid to the depositors.

**Table : 4.1**  
**Annual Growth of Type-Wise Deposit Collection**  
**(Source of fund) Rs in '000'**

	062/63	063/64	064/65	065/66	066/67	Average
Saving Deposit	113344	199654	374736	732468	783745	53.26%
Growth Rate	-	76.15%	87.69%	95.46%	7.01%	
Fixed Deposit	272101	361029	464858	471987	905544	30.96%
Growth Rate	--	32.68%	28.75%	1.53%	91.86%	
Recurring Deposit	2748	2434	2888	--	--	--
Growth Rate	--	-11.43%	--	--	--	
Total	388193	563117	842482	1204455	1689289	44.47%
	--	45.06%	49.61%	42.96%	40.25%	

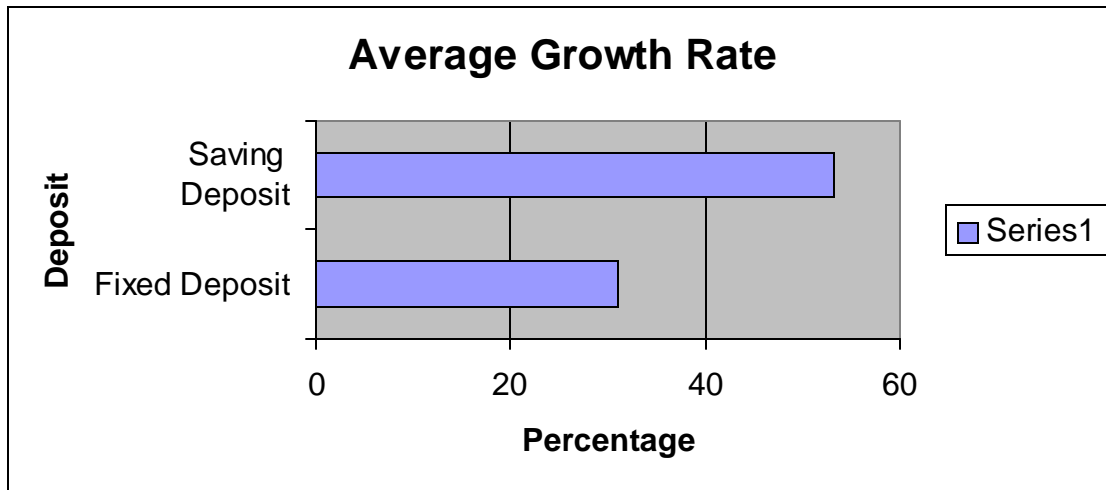
*Source : Fewa Finance Limited*

As Shown in the Table 4.1, FFL has categorized its deposit portfolio into three types. Because of the technical circumstances, FFL closed its Recurring Deposit scheme from the FY 065/66. The average growth rate of saving deposit in these five year is 53.26.57% and fixed deposit is 30.96% .

In the FY 063/64 saving deposit is increasing in increasing rate of 76.15% and continuously it is

increased in the same direction up to the FY065/66. In the FY 066/67 it is increased in the diminishing marginal rate, i.e. 7.01%. Similarly, the fixed deposit is increased by 32.68% in the FY 063/64 and increased in the diminishing marginal rate up to 065/66 and increased in increasing rate at the year 066/67. It is the highest increment of Fixed Deposit in these five years. FFL total deposit collection reached to Rs.1689289 thousands in the FY 066/67 from Rs.388193 thousands in the FY 062/63 Which is shown in the average growth rate of 44.47% per annum.

**Figure : 4.1**  
**Average Growth Rate of Type-wise Deposit Collection**



**4.1.6 Trend of Deposit Collection**

The trend of the total amount of deposit every year has been made by using trend analysis technique. The following trend line shows the trend of the total amount deposit of FFL.

**Figure : 4.2**  
**Trend of Deposit Collection**  
**(062/63-066/67)**

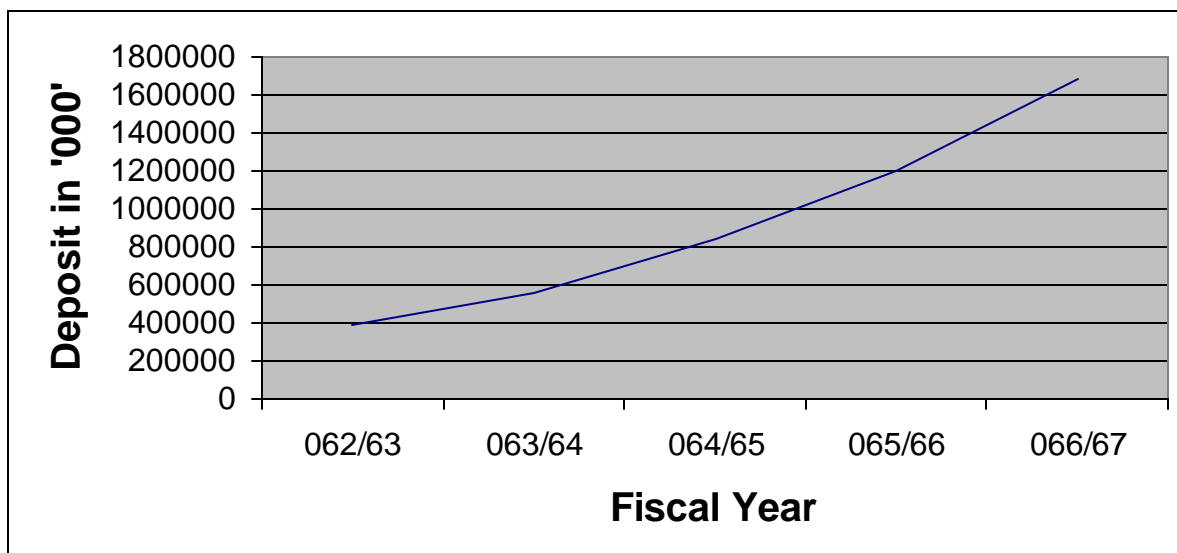




Figure 4.2 shows the trend of Deposit collection of FF from FY062/63 to FY 066/67. It is clear from the figure that the deposit collection of FFL is increasing in the increasing rate up to the FY 064/65 and it increases in the diminishing marginal rate in the next two years.

**Table : 4.2**  
**Portfolio of Deposit**

	062/63	063/64	064/65	065/66	066/67	Average
Saving Deposit	113344	199654	374736	732468	783745	43.27%
Percentage	29.20%	35.45%	44.48%	60.82%	46.40%	
Fixed Deposit	272101	361029	464858	471987	905544	56.73%
Percentage	70.80%	64.55%	55.52%	39.18%	53.60%	
Total	388193	563117	842482	1204455	1689289	100.00%
	100%	100%	100%	100%	100%	100.00%

*Source : Fewa Finance Limited.*

As shown in the table 4.2, FFL has categorized its deposit portfolio mostly in two types. The Fixed Deposit of FFL remaining at the higher position in most of the FY during the study periods but it edged in second position in the FY 065/66. Similarly, Fixed Deposit remained at the second position in most of the years of the study period but in higher position in the FY 065/66. Fixed deposit shown in table (i.e. 56.73%) is more appropriate for lending because it is not withdrawal before the expiry date. So the company can mobilize the amount of Fixed Deposit into productive sector and gain more profit. The company should improve their increasing percentage of fixed deposit to total deposit, which shows the decreasing percentage from 062/63 to 065/66.

**Figure : 4.2**  
**Deposit Portfolio Share Percentage**  
**(62/63 to 066/67)**

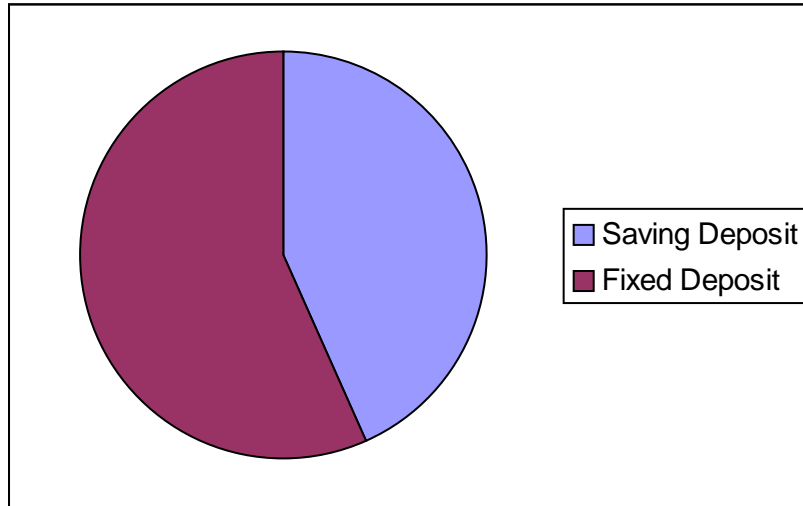


Figure 4.2 shows the composition of deposit collection made by FFL between the period of 062/63 to 066/67. From figure it is clear that fixed deposit got the higher proportion of deposit. FFL should try to maintain its proportion to 60-40 ( i.e. 60% fixed deposit and 40% saving deposit) for the best performance.

#### **4.1.7 Purpose-wise Loan Disbursement of FFL**

FFL has implemented the loan investment program to help its member in investing in different types of productive and profitable works. FFL has collected the deposit from the people and provided to the needy ones who help a lot in the economic development of the nation by providing loans under different sectors.

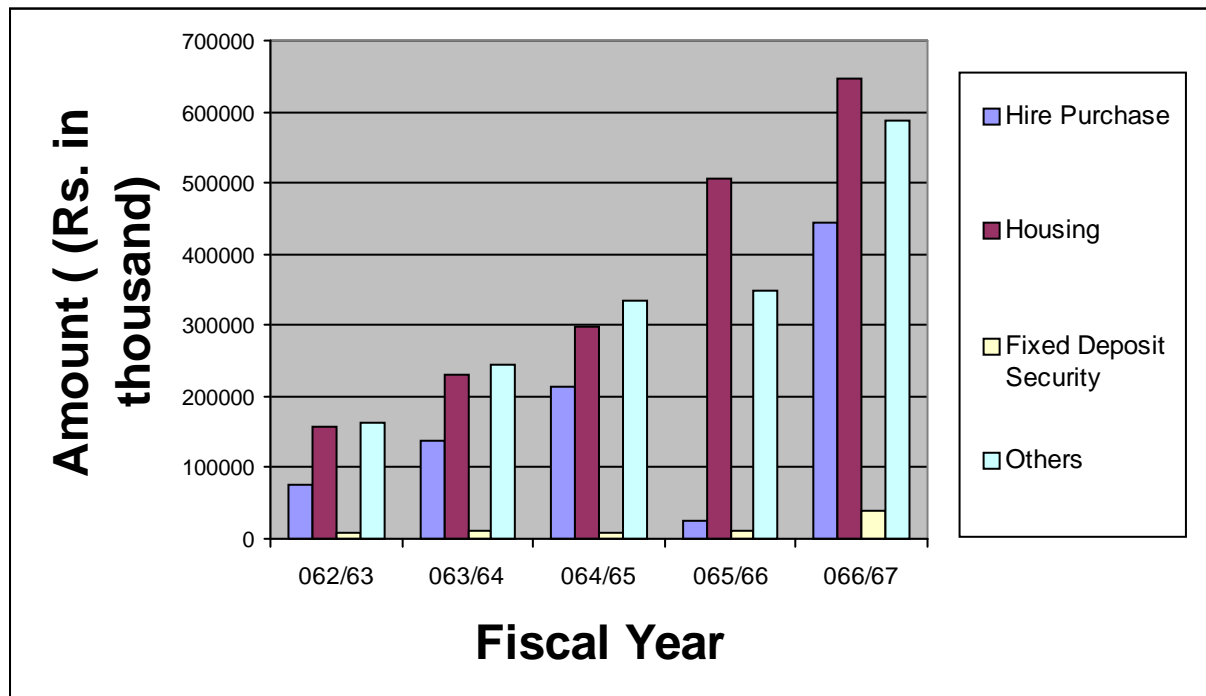
**Table : 4.3**  
**Purpose-wise Loan Disbursement of FFL**

( Rs. in Thousand)

S.No	Purpose	062/63	063/64	064/65	065/66	066/67	Average
1	Hire Purchase	77102.38	137377.02	213623.75	25850.021	442866.33	23.12
		19%	22%	25%	23%	26.60%	
2	Housing	158262.78	231043.17	299073.25	505767.15	647483.89	38.98
		39%	37%	35%	45%	38.89%	
3	Fixed Deposit	8116.04	12488.82	8544.95	11239.27	38126.47	1.65
	Security	2%	1%	1%	1%	2.29%	
4	Others	162320.8	243531.99	333253.05	348417.37	586381.66	36.84
		40%	39%	39%	31%	35.22%	
	<b>Total</b>	<b>405802</b>	<b>624441</b>	<b>854495</b>	<b>1123927</b>	<b>1664911</b>	

*Source : Annual Reports of FFL ( FY 062/63 to 066/67)*

**Figure : 4.3**  
**Purpose-wise Loan Disbursement**



The data presented in the above table 4.3 shows the loan-disbursed position of FFL.

In FY 062/63, the company has provided 19% in hire purchase, 39% on housing, 2% on fixed deposit security and 40% in other sectors. In most of the FY, company provided the loan highly on other sector and housing in the second position. In the FY 063/64 also the ratio of lending is similar to previous year, only hire purchase loan is increased by 3%. Similarly, in FY 064/65, hire purchase is increased but housing and fixed deposit security is decreased even the whole ratio is the same of previous years (i.e. other sector is in first position, housing is in second and hire purchase sector is in third position.)

There is a slight change in the lending ratio in the FY 065/66. Organization invests the huge amount on housing sector than before and this sector is in first position and other is in second position. In the FY 066/67, housing is decreased and reached on 38.89% of the total lending amount of the company. It shows that, there was the high demand of housing loan on the FY 065/66. Because of this loan, economic condition of the whole nation is disturbed, so NRB controlled that situation by increasing the interest rate provided by the banks and financial institutions and it came down in the next year.

**Figure : 4.4**  
**Average Loan Disbursed**

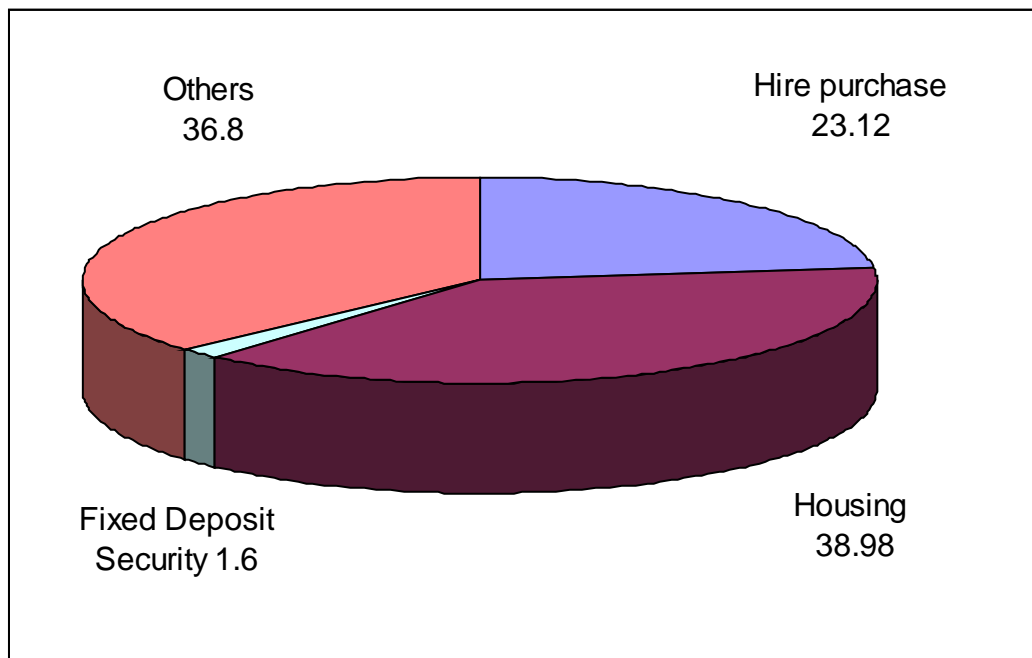


Figure 4.4 shows the percentage of loan disbursed by FFL in various sector during the study periods. (i.e. FY 062/63 to 066/67) FFL invested high amount on housing sector, which is 38.98% of the total investment. Similarly other sectors, hire purchase and fixed deposit security are in second, third and fourth position respectively.

**Table : 4.4**  
**Annual Growth of Disbursed Loan**

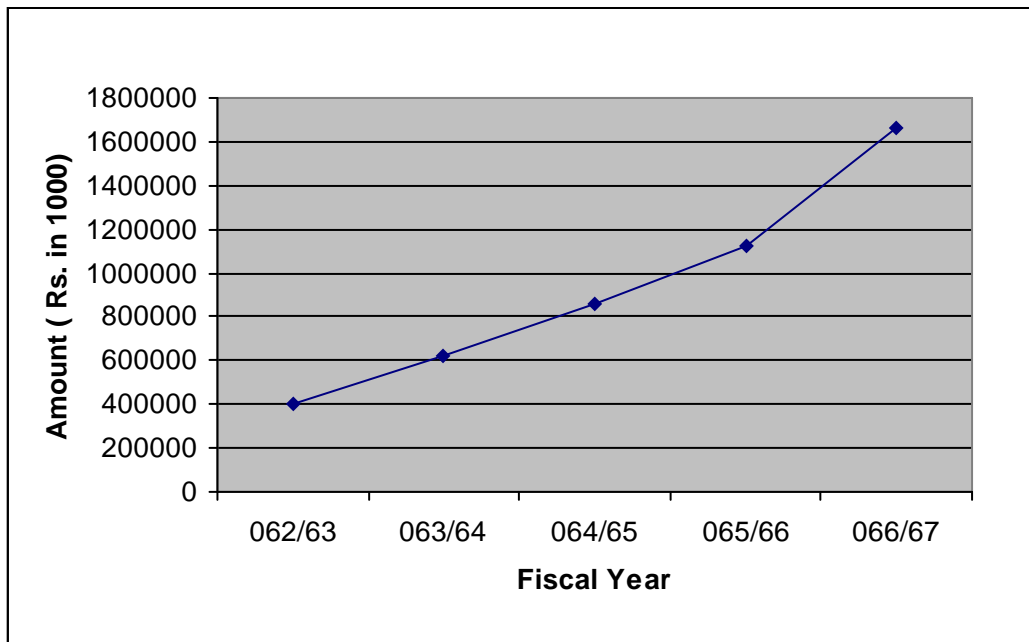
(Rs. in Thousand)

S.No	Fiscal Year	Disbursed Loan (Rs)	Annual Growth %
1	062/63	405802	-
2	063/64	624441	53.88
3	064/65	854495	36.85
4	065/66	1123927	31.54
5	066/67	1664911	48.13
	Average Growth Rate Per Annum		42.6

*Source : AGM Reports of FFL*

Table 4.4 shows that FFL's total loan disbursement increased from 405802 thousands in FY 062/63 to 1664911 thousands in FY 066/67. And the average growth rate per annum of FFL is 42.6 percent.

**Figure : 4.5**  
**Movement of Loan Disbursement of FFL**



The data of Table 4.4 are plotted in figure 4.5 with loan disbursement on the vertical axis and Fiscal Year on horizontal axis. From the figure, it is clear that the annual growth rate of each year is increasing. Between the fiscal year 062/63 to 066/67, growth rate of loan disbursement varied from a lowest 31.54% in the fiscal year 065/66. It was highest 53.88% in the fiscal year 063/64. Then it was increasing in the diminishing marginal rate up to 065/66, finally it was increased in increasing rate with 48.13 % in the fiscal year 066/67.

#### 4.1.8 Loan Recovery of FFL by Period

Finance companies' ability to provide continual credit services depends upon the capacity and loan recovery. Satisfactory recovery of loan is important for the smooth functioning of the entire credit machinery. The collection of due loan in time is an important aspect of the company which determines the further expansion of company's activities but repayment of not due loan before the time is not good aspect of the company. Therefore it is necessary to analyze the recovery of the loan on the basis of period.

**Table : 4.5**  
**Annual Growth of Recovery Loan**

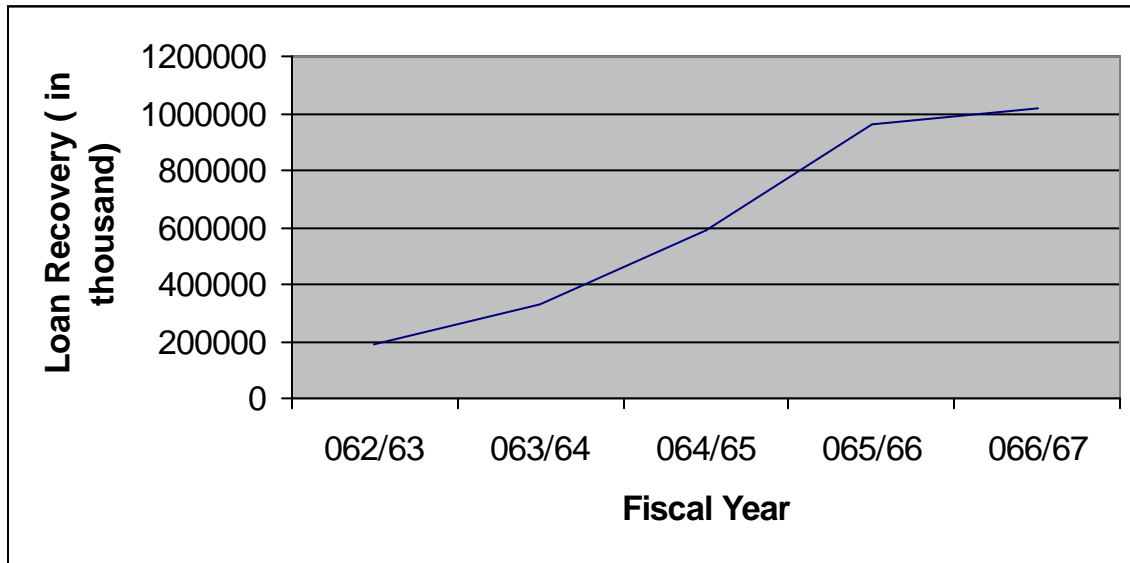
(Rs. In thousand)

S.No	Fiscal Year	Loan Recovery	Annual Growth
1	2062/063	191379	-
2	2063/064	329167	71.99
3	2064/065	590935	79.52
4	2065/066	958913	62.28
5	2066/067	1019624	6.34
Annual Growth Rate Per Annum			44.03

*Source : AGM Reports of FFL*

As shown in the table 4.5, FFL's total loan recovery increased from Rs.191379 thousands in Fiscal Year 062/63 to Rs.1019624 thousands in the Fiscal Year 066/67, which shows the average recovery growth rate of these five years is 44.03%.

**Figure : 4.6**  
**Movement of Loan Recovery of FFL**  
**(2062/63-066/67)**



The data of Table 4.5 are plotted in figure 4.7 with loan recovery on the vertical axis and fiscal year on the horizontal axis. From the figure it is clear that the annual growth rate of each year is increasing. Between the FY 062/63 to 066/67 the growth rate of loan recovery varied from a lower growth rate 6.34% on FY 066/67 to highest rate 79.52% in the FY064/65. Thereafter, it increased in the diminishing marginal rate simultaneously.

#### **4.1.9 Outstanding Loan of FFL**

A loan that cannot be recovered during the year is outstanding loans. It is difference between loans disbursed and recovered amount of loan. The increase in bad outstanding loan may cause to create hands of the company to remain idle in various loans but increase in proper outstanding loan is good for the company because it earns interest regularly.

**Table : 4.6**  
**Annual Growth of Outstanding Loan**  
**(2062/63-066/67)**

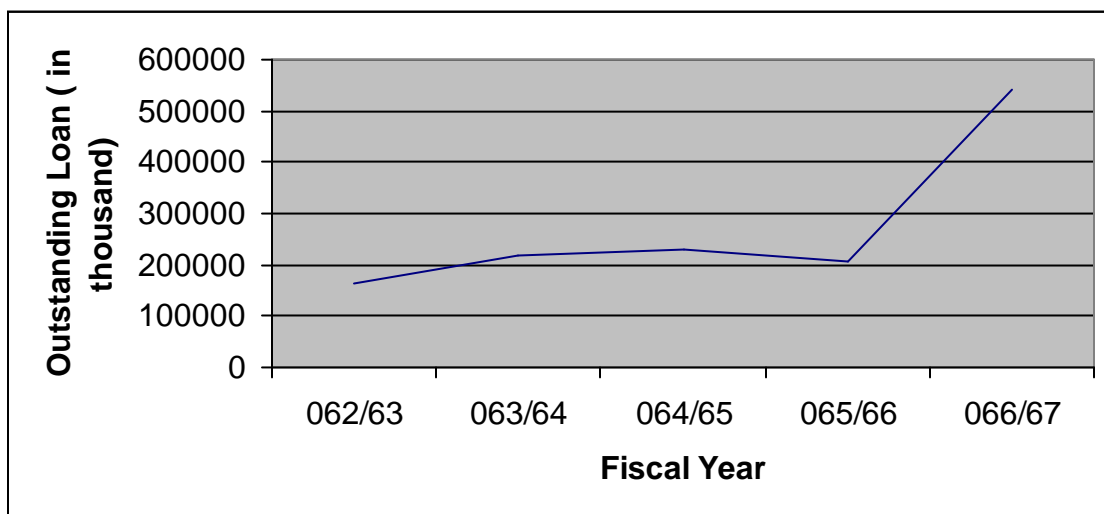
(Rs. In thousands)

S.No	Fiscal Year	Outstanding Loan	Annual Growth
1	2062/063	164820	-
2	2063/064	218639	32.66 %
3	2064/065	230054	5.23 %
4	2065/066	206693	-10.16 %
5	2066/067	540984	161.74 %
Annual Growth Rate Per Annum			37.89 %

*Source : Fewa Finance Limited*

Table 4.6 shows that FFL's total outstanding loan increased from Rs.164820 thousands in the FY 062/63 to Rs.540984 thousands in the FY 066/67. Its annual growth in FY063/64 is 32.66% and it is increased in decreasing order in the next year. i.e. 5.23%. It is decreased by -10.16% in the fiscal year 065/66 then it is again increased in increasing order in the next fiscal year 066/67. i.e. 161.74%. This table shows the average growth rate of outstanding loan in these five years is 37.89%.

**Figure : 4.7**  
**Movement of Outstanding Loan of FFL**  
**(2063/63-2066/67)**





The data of Table 4.6 are plotted in figure with Outstanding Loan in the vertical axis and Fiscal Years in the horizontal axis. From the figure, It is clear that the annual growth of each year is in increasing order except in the fiscal year 065/66. It is slightly increased up to the FY 065/66 and decreased in 065/66, then it is increased in high rate. i.e.161.74 in the FY 066/67.

#### **4.1.10 Analysis of the relation between Loan Disbursement, Loan Recovery and Outstanding Loan of FFL.**

Bank and Financial Institutions not only collect deposit but also disburse the loan. Without disbursement or investment the bank cannot earn any thing. From that we can say deposit collection is the main source of loan disbursement. But disbursement is not only sufficient. A good take care of disbursed loan and critical analysis is also required. So the relation between disbursed loan and recovered loan should be interpreted.

##### **a) Comparison between Loan Disbursement and Recovery**

A banks major income source is loan disbursement. In order to earn profit from the interest of loan, bank should provide various kinds of loan to various sectors. Short-term loan and long-term loan are the loans provided by the bank to customers. Their maturity periods are varied from there purpose. Some loans are matured within one year and some are extended for few years more. It is not possible and necessary that a bank or FI should recover all loans that are distributed in the same year. The more the disbursed amount will remain to recover the more the bank is getting interest.

In the following table the relation between the disbursed loan and recovered loan has be shown.

**Table : 4.7**

#### **Comparative Study of Loan Disbursement and Recovery**

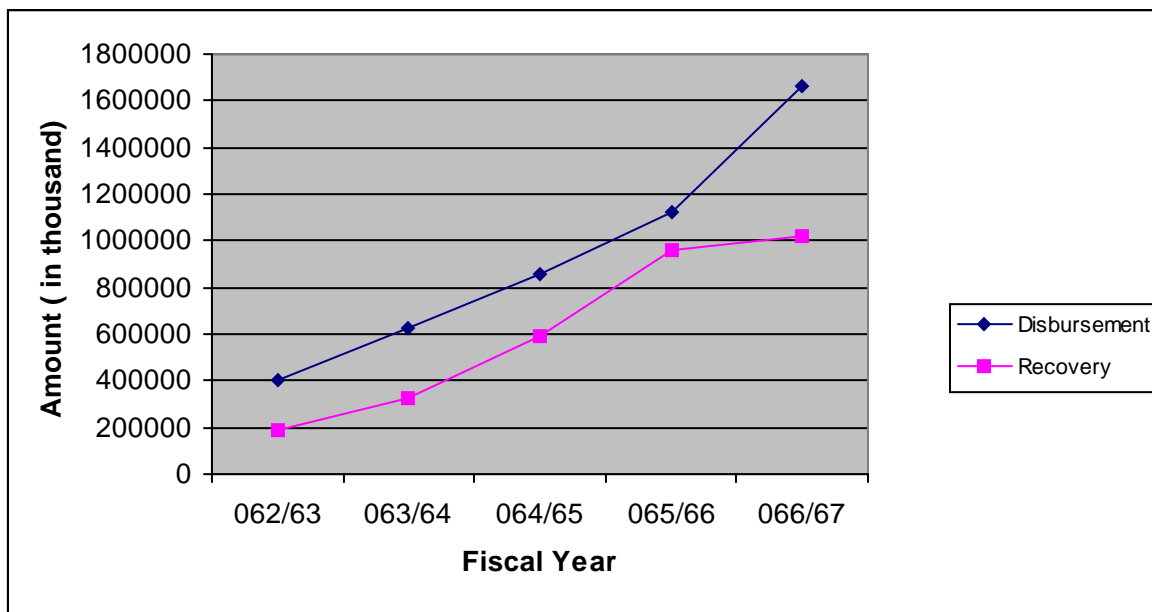
<b>Fiscal Year</b>	<b>Amount of Disbursement</b>	<b>Amount of Loan Recovery</b>	<b>% of Recovery on Disbursement</b>
2062/063	405802	191379	47.17
2063/064	624441	329167	52.72
2064/065	854495	590935	69.16
2065/066	1123927	958913	85.31
2066/067	1664911	1019624	61.25

Source : Fewa Finance Limited

In the table 4.7, the change in amount of disbursement and recovery are shown during the study period of FY 062/63-066/67. The amount of disbursement is increased in the increasing order and the amount of recovery is also increased in the same pattern. In the FY 062/63, 47.17% of disbursement amount is recovered. Similarly 52.72%, 69.16%, 85.31% and 61.25% of amount is recovered in the FY 063/64 to 066/67 respectively.

Among the five years 47.17% in the FY 062/63 is the lowest percentage of recovered amount where as 85.31 % in the FY 065/66 is the highest amount percentage recovered.

Trend line of the amount of disbursement and the recovery also help in the comparison.



### b) Coefficient of Correlation between loan disbursement and loan recovery

The tool coefficient of correlation measures the degree of relationship between these two variables, loan disbursement and loan recovery. In this analysis loan disbursement is independent variable 'X' and recovery is dependent variable 'Y'. The main reason of finding out the coefficient of correlation between these two variables is to justify whether loan disbursement and loan recovery is significant or not.

FY	L. Recov. X	L. Disb. Y	X- $\bar{X}$ (dx)	Y- $\bar{Y}$ (dy)	(dx) <sup>2</sup>	(dy) <sup>2</sup>	dx*dy
062/63	1.91	4.05	-4.27	-5.29	18.24	27.98	22.58
063/64	3.29	6.24	-2.89	-3.1	8.36	9.61	8.95
064/65	5.90	8.54	-0.28	-0.8	0.08	0.64	0.23
065/66	9.58	11.23	3.4	1.89	11.56	3.57	6.42
066/67	10.19	16.64	4.01	7.3	16.08	53.29	29.27
Total	30.87	46.7			54.30	95.09	67.47

$$\bar{X} = \frac{\sum X}{n} = \frac{30.87}{5} = 6.18$$

$$\bar{Y} = \frac{\sum Y}{n} = \frac{46.7}{5} = 9.34$$

Now,

$$\begin{aligned} \text{Coefficient of Correlation (r)} &= \frac{\sum (dx \cdot dy)}{\sqrt{\sum dx^2 \cdot \sum dy^2}} \\ &= \frac{67.47}{\sqrt{54.30 \cdot 95.09}} = \frac{67.47}{71.85} = 0.93 \end{aligned}$$

$$P.Er = 0.6745 \cdot \frac{1 - r^2}{\sqrt{n}} = 0.6745 \cdot \frac{1 - 0.93^2}{\sqrt{5}} = 0.0423$$

$$\text{Again, } 6P.Er = 6 \cdot 0.0423 = 0.2538$$

### Coefficient of Correlation (r) > 6P.Er.

Loan recovery of the company seems to be directly proportional to the loan disbursement because both have shown movement in the same direction. Therefore to increase funds of loan, recovery is associated with similar trend of loan disbursement. The coefficient of correlation between loan disbursement and loan recovery of FFL has brought (r) = 0.93. It indicates that there is high degree of positive correlation between two variables, which is nearer to +1. Thus

higher the volume of loan recovery greater will be the loan disbursement.

The Probable error of the coefficient of correlation helps in interpretation. The value of probable error measures the reliability of the co-efficient of correlation. If the value of (r) is less than six times of probable error, there is no evidence of correlation i.e. the value of (r) is not at all significant. Since the value of (r) is greater than 6 P.Er. i.e.  $0.93 > 0.2538$ , the value of (r) is significant. In other word co-efficient of correlation between loan disbursement and loan recovery is significant.

### c) Comparison between Loan Disbursement and Outstanding Loan.

The loan which is not recovered within the same year is called outstanding loan. Investment only for one year is not that much beneficial for the institution. So FI used to lend in the various sector for several years according to the priority sector. It is a bit riskier to invest on such loan but interest is regularly gained by the FI. So it is important to analyses the relation between the loan disbursement and outstanding loan.

**Table : 4.8**

#### **Comparative Study of Loan Disbursement and Outstanding Loan**

Fiscal Year	Amount of Disbursement	Outstanding Loan	% change in Disbursement and Outstanding Loan
2062/063	405802	164820	40.61
2063/064	624441	218639	35.01
2064/065	854495	230054	26.92
2065/066	1123927	206693	11.39
2066/067	1664911	540984	32.49

*Source : Fewa Finance Limited*

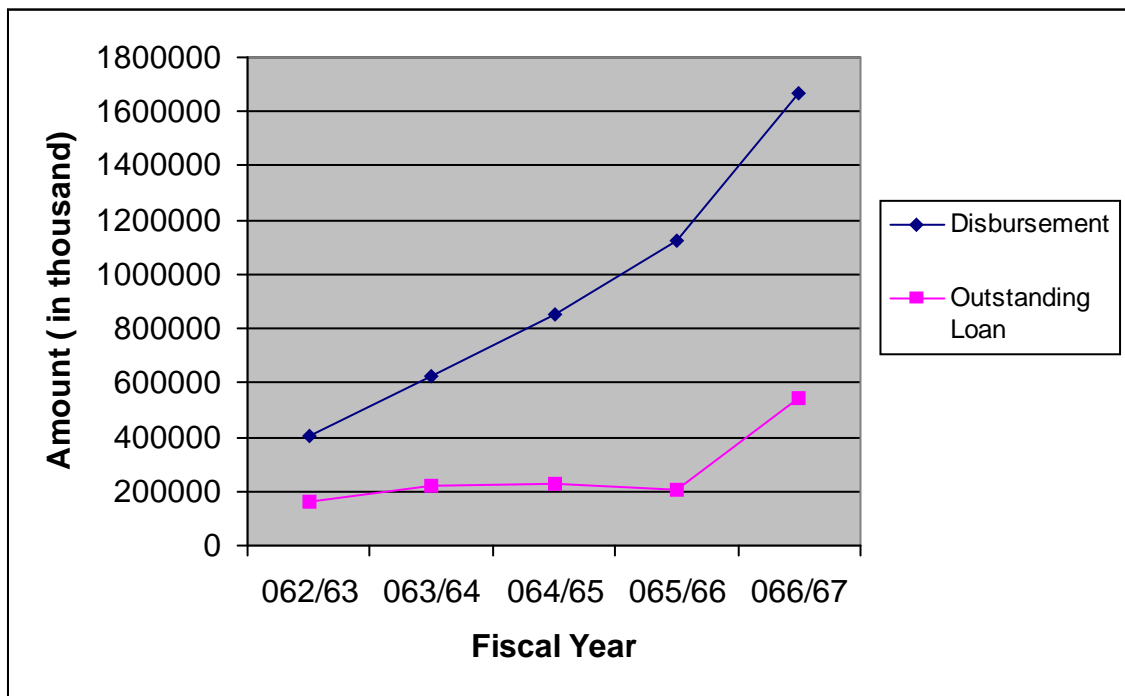
In the table 4.8, the change in amount of disbursement and outstanding loan are shown during the study period of FY 062/63-066/67. The amount of disbursement is increased in the increasing order and the amount of outstanding loan is also increased in the same pattern but the ratio of outstanding loan ratio is decreased. In the FY 062/63, 40.61% of disbursement amount is outstanding. Similarly 35.01%, 26.92%, 11.39 % and 32.49% of amount is outstanding in the FY 063/64 to 066/67 respectively.

Among the five years 11.39% in the FY 065/66 is the lowest percentage of outstanding loan

amount where as 40.61 % in the FY 062/63 is the highest amount percentage recovered.

Table 4.8 also shows Fewa Finance is investing in the increasing pattern; similarly it is enjoying earning interest from the outstanding loan too.

Trend line of the amount of disbursement and the outstanding loan also help in the comparison.



**d) Coefficient of Correlation between loan disbursements and outstanding loan.**

In this analysis, loan disbursement is independent variable 'X' and outstanding loan is dependent variable 'Y'. The main reason of finding out the coefficient of correlation between these two variables is to justify whether loan disbursement and outstanding loan is significant or not.

FY	L. Recov. X	Outs. Loan Y	$X - \bar{X}$ (dx)	$Y - \bar{Y}$ (dy)	$(dx)^2$	$(dy)^2$	dx*dy
062/63	1.91	1.64	-4.27	-1.07	18.23	1.15	4.56

063/64	3.29	2.18	-2.89	-0.53	8.35	0.29	1.53
064/65	5.90	2.30	-0.28	-0.41	0.07	0.17	0.11
065/66	9.58	2.06	3.4	-0.65	11.56	0.43	-2.21
066/67	10.19	5.40	4.01	2.69	16.08	7.24	10.78
Total	30.87	13.58			54.30	9.26	14.79

$$\bar{X} = \frac{\sum X}{n} = \frac{30.87}{5} = 6.18$$

$$\bar{Y} = \frac{\sum Y}{n} = \frac{13.58}{5} = 2.71$$

Now,

$$\text{Coefficient of Correlation (r)} = \frac{\sum (dx \mid dy)}{\sqrt{\sum dx^2 \mid \sum dy^2}}$$

$$= \frac{14.79}{\sqrt{54.30 \mid 9.26}} = \frac{14.79}{22.42} = 0.6596$$

$$\text{P.Er} = 0.6745 \mid \frac{1}{\sqrt{n}} \sum r^2 = 0.6745 \mid 0.2533 = 1.0248$$

$$\text{Again, } 6\text{P.Er} = 6 \times 0.1708 = 1.0248$$

### **Coefficient of Correlation (r) < 6P.Er.**

The coefficient of correlation between loan disbursement and outstanding loan of FFL has brought (r) = 0.6596. It indicates that there is a positive correlation between two variables.

The Probable error of the coefficient of correlation helps in interpretation. The value of probable error measures the reliability of the co-efficient of correlation. If the value of (r) is less than six times of probable error, there is no evidence of correlation i.e. the value of (r) is not at all significant. Since the value of (r) is smaller than 6 P.Er. i.e.  $0.6596 < 1.0248$ , the value of (r) is insignificant.

The nature of outstanding loan is different from the loan recovery and deposit collection. In comparison between loan recovery and loan disbursement there is the positive relation. i.e. higher the loan recovery higher the loan disbursement. But the major target of bank or financial

institution is not only to invest and collect it soon but also to earn profit by investing for long period time. i.e. more than one year. So bank or FI tries to invest for more than one year in the secure sector. The un-recovered loan is called outstanding loan. If all the loans are recovered within one year then bank cannot earn more interest, which is the major target of the financial institutions. Hence the negative relation (insignificant relation) between outstanding loan and loan disbursement is favorable to institutions for seeking interest if other things are remaining the same. Higher the outstanding loan higher the interest income.

## **4.2 Major Findings**

Most of the activities of the financial institutions are related with loan management. It plays the major role in profitability of the organization. It is highly complicated task in the bank and financial institution. Loan management requires effective deposit collection because deposit is only the primary source of fund in the financial institution and effective loan disbursement. Here we discuss about the major findings of FFL during the study period regarding lending policy.

- FFL has collected deposit mainly on three schemes up to the year 064/65. After that it only collected deposit on two schemes, saving deposit and fixed deposit. During the study period FFL collected 43.27% of saving deposit and 56.73 % of fixed deposit. The average increment of total deposit collection during the study period is 44.47%.
- Trend of deposit collection is increased in increasing order, which is 45.06% in FY 063/64 and 49.61% in the year 064/65. In the year 065/66, deposit collection is increased in diminishing marginal rate i.e. 42.96%, which is less than the previous years and again it decreased and come to 40.25% in the FY 066/67, which is the lowest increment of deposit collection during the study periods.
- The sector-wise loan disbursement of FFL is divided into major four categories. Hire purchase, Housing, Fixed Deposit Security and other sectors are various sectors in which FFL lends its deposit. The uncategorized loan of FFL is included in other sector.
- The highest portion of the loan is disbursed into housing sector in average, which is 38.98% of the total disbursed amount during the study period. Similarly in other sector

FFL invested in second position i.e.36.84% and 23.12% on hire purchase. The institution provides least amount of loan in fixed deposit security. Only 1.65% of total amount is disbursed on it.

- The disbursed amount of FFL is increasing in diminishing marginal rate. The disbursed amount is increased by 53.38% in the FY 063/64 and regularly it increased in decreasing rate i.e.36.84%, 31.54% in the FY 064/65 and 065/66 respectively. But in the FY 066/67 it is increased by 32.49%, which shows the increasing rate than the previous year. The average growth rate of disbursed amount by FFL is 42.6%.
- The annual recovery increment of FFL during the study period is higher in 2064/65. i.e. 79.52% in comparison to the previous year. Similarly in the second position 71.99% in 2063/64. The smaller amount 6.34% annual increment is recovered in FY 066/67 in comparison to the previous year. The average annual growth rate of recovery loan of FFL is 44.03%.
- FFL's total outstanding loan increased form Rs.164820 thousands in the FY 062/63 to Rs.540984 thousands in the FY 066/67. Its annual growth in FY063/64 is 32.66% and it is increased in decreasing order in the next year. i.e. 5.23%. It is decreased by -10.16% in the fiscal year 065/66 then after it again increased in increasing order in the next fiscal year 066/67. i.e. 161.74%. The average growth rate of outstanding loan in these five years is 37.89%.
- The amount of disbursement increased in the increasing order and the amount of recovery is also increased in the same pattern. In the FY 062/63, 47.17% of disbursement amount is recovered. Similarly 52.72%, 69.16%, 85.31% and 61.25% of amount is recovered in the FY 063/64 to 066/67 respectively. Among the five years 47.17% in the FY 062/63 is the lowest percentage of recovered amount where as 85.31 % in the FY 065/66 is the highest amount percentage recovered.
- The amount of disbursement is increased in the increasing order and the amount of



outstanding loan is also increased in the same pattern but the ratio of outstanding loan is decreased. In the FY 062/63, 40.61% of disbursement amount is outstanding. Similarly 35.01%, 26.92%, 11.39 % and 32.49% of amount is outstanding in the FY 063/64 to 066/67 respectively.

Among the five years 11.39% in the FY 065/66 is the lowest percentage of outstanding loan amount where as 40.61 % in the FY 062/63 is the highest amount percentage recovered.

- By using the coefficient of correlation tool in comparative study between loan disbursement and recovery, coefficient of correlation( $r$ ) is found 0.93 and 6 P.Er is 0.2538. It indicated high degree of positive correlation between the two variables. Coefficient of Correlation ( $r$ ) > 6P.Er. It shows the significant relation between the two variables.
  
- In comparative study between loan disbursement and outstanding loan, coefficient of correlation ( $r$ ) is found 0.6596 and Probable Error (6P.Er) is 1.0248, which is greater than 1. Coefficient of Correlation ( $r$ ) < 6P.Er. It shows the insignificant relation between the loan disbursement and outstanding loan.

## **CHAPTER V**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

This chapter includes two aspects of the study; first aspect of the study is to focus on summarizing the fact found on the study and making conclusion upon them while second aspect of the study focuses on making some useful suggestions and recommendations based on findings of the study to increase the deposit collection and loan disbursement of FFL.

#### **5.1 Summary**

The study has been concluded with the objective of analyzing the lending policy of FFL. This study was conducted by using the secondary data and the collected data has been described. The study covers five years from 062/63 to 066/67. For this study analytical as well as descriptive methods have been adopted. To analyze the data, simple statistical analysis such as average, percentage, co-efficient correlation etc have been calculated. Moreover, to present the data moreover clearly and attractively bar graph, line graph, pie chart etc also have been used. The required data and information have been mainly collected from secondary sources.

For the development of any country, the growth and progress in the economic sector is the first condition. Economic liberalization policy of the government has encouraged the establishment and growth of finance companies in the country. As the current report of NRB, 79 finance companies are in operation throughout the country. Financial companies play a significant role in the collection and mobilization of fund through different sectors and can contribute in national development.

FFL is in operation in Pokhara. It is one of the important cities of Nepal. The city is famous for tourism. Besides tourism, Pokhara is also growing as an education, health and trading center of the country. Hence the need of finance company is obvious. FFL was established with authorized capital Rs.4,00,00,000 at Gandaki zone, Kaski district at Chipledhunga. It started its transaction from 2060 Baisakh 17 BS. It provides loan such as business, industrial, hire purchase, housing etc. FFL lending trend is increasing day by day.

FFL is confined by a number of regulations. FFL has involved in different activities among them, deposit mobilization, hire purchase loan, housing loan are important. This study has also analyzed by making relation between loan disbursed and recovery. Similarly it describes the

relation between the loan disbursement and outstanding loan too. Deposits owned are the major parts of liabilities of FFL. It is observed from the study that there remained gradual increase in each source. Housing loan, Hire purchase and other loans remained as the major credit flow of FFL during the study period. It remained regular increment in each year of the study period in the sectors mention above.

## **5.2 Conclusions**

Form the analysis of the main findings of the study, following conclusions can be drawn about the Lending Policy of FFL.

- Among the four lending sectors, FFL invest most in the housing sector and in the other sector. The undefined sectors of lending are adjusted into other sector by FFL, which play vital role to increase the profit ratio of the institution. Hire purchase remains in the third position and fixed deposit security remains in the last priority.
- The average growth rate of deposit collection and loan disbursement is relatively equal, however deposit collection is greater than loan disbursement.
- Average growth of deposit collection and loan disbursement is nearer to each other. This indicates that there is neither high liquidity nor low liquidity. So deposit collection and loan disbursement of FFL has satisfactory between the study periods.
- The total amount of deposit collection trend in increased and almost of the type-wise deposit collection also increased. Fixed deposit and saving deposit are the major schemes of FFL to collect deposit where fixed deposit has the more percentage in total.
- Annual Growth Rate of loan recovered by FFL is more than two third portion in total.. Then it is increased in the next year comes nearly eighty percentage which is the highest increment during the study periods. In the FY065/66 it is decreased and become only two third parts in total. Lowest increment of recovery loan of FFL in 066/67. The average annual growth rate recovered loan of FFL is 44.03%.
- Annual Growth Rate of outstanding loan of FFL is more than one third of total in the beginning year of the study period. Then it started to decrease in the next two fiscal years and once it goes to negative too. But in the last year of the study, it is highly increased and comes to more than hundred percentages. The average annual growth rate of

outstanding loan of FFL is 37.89%.

- FFL recovered the greatest percentage of disbursed loan during the fourth year of the study period. Similarly the lowest percentage of recovered loan to the disbursement in the first year of the study period.
- FFL's outstanding loan is highest in percentage to the disbursed amount in the first year of the study period. Similarly the lowest outstanding loan percentage to the disbursement in the last year of the study period.
- There is a high degree of positive correlation between loan disbursements with loan recovery. The correlation coefficient between these two variables is 0.93. Like this Probability Error and 6PE are 0.0423 and 0.2538 respectively. This shows the positive relationship between these two variables, loan disbursement and loan recovery. Hence the relation between the two variables is significant.

There is a positive correlation between loan disbursements with outstanding loan but their relation is insignificant. The correlation coefficient between these two variables is 0.6596. Like this Probability Error and 6PE are 0.1708 and 0.0248 respectively. Hence the relation between the two variables is significant though the relation between these two variables is positive.

### **5.3 Recommendations**

The following are the recommendations for the FFL based on the study carried out.

- FFL needs to manage its lending portfolio effectively. It is good to be managed under the dynamic implications of financial market.
- Growth rate of fixed deposit in the FY065/66 is highly fluctuating. It is good to maintain in the same ratio.
- There are various services provided by FFL for the customer. Among them, uses of fund towards hire purchase and housing financing must be shifted towards the business financing
- It is better to apply different development schemes such as deposit insurance scheme, workers saving schemes, women development schemes etc though which FFL can collect more deposit.

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