PROFITABILITY ANALYSIS OF COMMERCIAL BANKS IN NEPAL

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RECOMMENDATION

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I, hereby, declare that, this thesis entitled “Profitability Analysis of Commercial Banks in Nepal” submitted to the Faculty of Management, Tribhuvan University, is my original work conducted in the form of partial fulfillment of the requirement for the Master’s Degree in Business Studies (M.B.S.).

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Bimala Piya

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LIST OF ABBREVIATIONS

AU	Assets Utilization
DPS	Dividend per share
EM	Equity Multiplier
EPS	Earning per share
FIs	Financial institutions
FY	Fiscal year
GDP	Gross domestic product
HBL	Himalayan Bank Limited
NABIL	Nabil Bank Limited
NBL	Nepal Bank Limited
NIDC	Nepal Industrial Development Corporation
PM	Profit Margin
RBB	Rastriya Banijya Bank
ROA	Return on Assets
ROE	Return on Equity
SCBNL	Standard Chartered Bank Nepal Limited

CHAPTER I

INTRODUCTION

1.1. Background of the study

Financial institutions play very important role in the process of economic growth of the developing country. Among the financial institutions, commercial banks are important enterprises that serve as primary means of institutions for financial resources mobilization. A developing country must maintain high and sustained rate of economic development. It must mobilize the available resources to support requisite high level of investment.

The commercial banks accept the demand and time deposits from business, industries, government corporations, non-government organizations and individuals. They give them interest against the deposits. They use funds deposited by the public and provide loans in the agricultural, commercial and industrial sectors with the objectives of profit maximization. The commercial banks also provide technical and administration assistance to industries, trade and business.

The mobilization of the resources in developing countries should focus on two main parts. First of all, developing countries should exert massive effort to increase the rate of domestic savings especially in the case of difficult access and harder term of commercial borrowing. The institutionalization of household savings is crucial for the rapid growth of saving. Secondly, developing countries should improve the efficiency of the investment to maximize the return on capital and yield highest possible economic benefit.

In Nepalese context, “The Tejarath Adda” (loan providing office) was established by the government in 1877 A.D. to provide the loans for general public and organizations at a low rate interest against the securities of the coins of gold, silvers and other ornaments. It is the first financial institution of Nepal for dealing on money and credit.

Later, Nepal Bank Limited (NBL) was established in 1994 B.S. as a semi-government bank. It had a share capital consisting 51% of the government and 49% of public. It had an initial authorized capital of NRs.10 million and paid up capital of NRs. 842 thousands. It was the first commercial bank of Nepal. The Nepal Bank Limited (NBL) is providing such banking services as to accept the deposits, to provide credit facilities for the promotion of trade, cottage industries and agricultural, and to provide customer services i.e. issue of bills of exchange, hundies, to invest in government bonds and securities. After 2055/056, Nepal Bank Limited has changed its share capital pattern with consisting is 40% of the government and 60% of the general public.

Meanwhile, Nepal Rastra Bank was established on April 26, 1956 A.D. as a central Bank with authorized capital of 10 million fully subscribed by the government with objectives of supervising, directing to the other commercial and development banking activities.

After that, Nepal Industrial Development Corporation (NIDC) was established in 1957 A.D. as a development bank. In 1966, Rastriya Banijya Bank (RBB) was established with 100% government ownership as a second commercial bank. The Agricultural Development Bank (ADB) was created in 1967 A.D. as an agricultural bank to provide loans in agricultural and non-agricultural sectors. After that, it started commercial banking activities from 1986 A.D. with similar activities of the Rastriya Banijya Bank.

Accordingly, from 1957 A.D. to 1977 A.D., small types of financial institutions were established and provided long term and short-term loans to agricultural and industrial sectors. But, they were not able to provide disburse loans and realize loans. Therefore, they could not run easily.

In 1984 A.D., Nepal Rastra Bank opened the financial institution’s door for joint-venture banking system in Nepal with participation of equity investment and technical assistance or collaboration from foreign financial institutions/banks. In this context, the researcher is going to analyze the position of resource mobilization of commercial banks in Nepal. The main analysis is especially concerned with the resource mobilization between three commercial banks; Standard Chartered Bank Nepal Limited, Nepal Arab Bank Limited and Himalayan Bank Limited.

1.2. Focus of the Study

The profitability of any financial institution can represent whether such institutions are running smoothly or not. The indicators concerned with the profitability directly represent the profit generating capacity of the institution. Since the major aim of commercial banks directly relate with earning of profit along with providing the financial services to the customer, this term ‘profitability’ might represent the actual scenario of the mentioned commercial banks for achieving their goals.

In this context, it is intended to have assessment of the concerned indicators of the profitability according to available information of the sample commercial banks. The study will show the trend of profitability and assess the financial strength and weakness in accordance with the ratio analysis.

1.3. Statement of the problem

The main target of a commercial bank is to maximize the profit. There are various financial institutions in Nepal. These are competing each other. The Nepal Rastra Bank has mandated the commercial banks to open one branch in rural area while opening branches in urban areas. However, this policy is not found implemented effectively. The joint-venture banks, which are concentrated in major cities of the country, are able to focus their activities around big industrialists, but small entrepreneurs have not been able to enjoy benefits from these commercial banks.

The challenge of the country is to direct these joint-venture commercial banks to provide services to small and middle class entrepreneurs.

Although, the rural branches of commercial banks are not able in resource mobilization and loan disbursement because in rural areas, most of the people are below the poverty line. They have no more income source and savings. Therefore, they can hardly save and deposit money in the bank. On the other hand, when nobody can deposit money in the bank, the bank can not be able to mobilize money/source. Also, there are not enough industries in the rural areas. In this way, the rural branches of the commercial banks can not earn profit easily.

According to the banking and financial statistics published by Nepal Rastra Bank, banking operation department, the ratio of the total deposit to Gross Domestic Product (GDP) is 32.2% in mid January, 33.7% in mid April and 35% in mid July 1998. The Credit GDP is 22.5% in mid January, 23.4% in mid April and 23.4% in mid July 1998 and productive sector 52.1% in mid January, 51.8% in mid April and 51.9%in mid July 1998. However, the ratio of the priority sector credit to total credit is 8% in mid January, 8.7% in mid April and 8.6% in mid July 1998.

Therefore, the competition is the burning issue of time in the country due to emergence of enough financial institutions. It has threatened all the banking institutions. It has warned to the commercial banks for improving and managing their financial activities and services.

The research study seeks to find out comparative efficiencies and weaknesses of the three commercial banks with analysis of these banks’ financial statements. The attempts will be made to sort out the answers for following questions:

a. What is the current position of banks' profitability?

b. What are strong and weak sides in performance of banks?

c. What measures bank managers have to take for improving profitability?

1.4. Objectives of the study

The study is to highlight the important activities and progresses of three commercial banks with justification. However, the researcher wants to be more specific in her study to reflect what objectives have guided to undertake the study. These banks can run easily and efficiently if they are able to mobilize the deposits in right sector and realize these amounts in time. Otherwise, it would be difficult to run their banking business in the competitive market. Therefore, the main objective of this study is to focus on how far the banks are able to fulfill this major purpose. The study will try to collect various opinions from various sectors, such as how to run the bank effectively? What should the management do to run the bank in the present competitive market? The specific objectives of the study are as follows:

a. To study the profitability trends of the banks for the last five years.
b. To assess the financial strength and weakness with help of ratio analysis, cash flow analysis and statistical technique.
c. To draw the conclusions and recommendation as to how the banks can be more successful in mobilizing the financial resources in the productive sectors.

1.5. Significance of the study

Apart from aiming to gain knowledge, research itself adds new analysis to the existing literature. The significance of this study lies mainly in identifying problem or deteriorating financial institutions (FIs), as well as for categorizing institution with deficiencies in particular component areas. Furthermore, it assists in following safety and soundness trends and in assessing the aggregate strength and soundness of the financial industry. The research is prepared in order to supplement present examination procedures applicable to financial institutions of Nepal. As such, the study assists the stakeholders in fulfilling their collective mission of maintaining stability and public confidence. It would be helpful for the senior management involved in day-to-day operations. The bankers, and examiners, alike can use this report to further their understanding of banks' financial condition. The profitability analysis is important for analyzing financial performance of any financial institution and its sustainability. This study will assist to analyze return on equity (ROE) framework through improving financial management under evaluating the strength and weaknesses of banks. It will be useful to the investors, shareholders and policy formulators of the institutions.

In addition, this study will provide a collective knowledge and analysis to the literature of financial institutions.

1.6. Limitations of the study

The limitation is another important aspect of the study. It is realized that the financial institutions including commercial banks are responsible for internal resource mobilization in the country. This study will be conducted simply for partial fulfillment of Masters on Business Studies, Second Year course. This study will be focused only on profitability analysis of selected commercial banks. Other limitations are as follows;

1. Time constraint

   This study is conducted and completed with in a short period. As a result, all the concerned areas might not be covered.

2. Reliability of the data

   This study is mainly based on the secondary data. Therefore, the accuracy of results and conclusions basically rely on the reliability of published secondary data. The published data of various agencies are not sometimes tallying. Therefore, the best estimates and more weightage are given to published data of the considered banks.

1.7. Organization of the study

The study report will contain the systematic presentation of the research design, analysis, and findings of the study. The study report is designed in five major chapters.

The beginning chapter of the study is introduction, which will serve for orientation to the readers to know about the basic information of the research area, various problems of the study, and objectives of the study, need or justification of the study. It assists for reporting, giving them the perspective they need to understand the detailed information about coming chapter.

The second chapter of the study will assure the readers that they are familiar with important research that has been carried out in similar area. It also establishes the study as link in a chain of research that is developing and emerging in the concerned field.

The third chapter will describe about the various sources of data related with study and various tools and techniques employed for presenting and analyzing the data.

The fourth chapter analyses the data related with the study and present the findings of the study and also comments briefly on them.

On the basis of the result from data analysis, conclusion will be presented from the study of the researcher concerned with the performance of the financial institutions in terms of job satisfaction and profitability. It will also provide important recommendations and suggestions for the concerned organizations for their better performance in future.

CHAPTER II

REVIEW OF LITERATURE

Many research works have been conducted by the various researchers on banking sectors. Several views and opinions have been expressed by the different researchers regarding commercial banks and their activities in magazines, journals, booklets, and other related important publications which have been published by various sectors.

Concerned research works by other researchers are also important to know for better guidelines and the feedback to serve purpose of this study. The relevant literatures related to the field of this study are traced below.

2.1 Functions of a bank

The banks are financial services from producing and selling the professional management of the public fund as well as performing many other roles in the economy. Their success and failure depend on their ability to identify the financial services as per public demands and production of those services efficiently and sell them at competitive price. The functions of banks can be listed as follows:

- Cash management function
- Credit function
- Trust function
- Saving function
- Investment function
- Payment function
- Investment banking function
- Insurance function
- Brokerage function

2.2 Types of banks

The modern economy demands various types of financial institutions. A single institution can not fulfill all the services demanded by the customers. Therefore, different types of banks also emerged in the banking industries as listed below:

a. Commercial banks:

The commercial banks are those banks, which perform all types of banking functions like accepting deposits, advancing loans, credit creation, and agency functions. They provide short-term loan, medium-term loan and long-term loan for trade and industries. They also operate off balance sheet functions such as issuing guarantee, bonds, and letter of credit. In Nepal, Nepal Bank Limited, Himalayan Bank Limited and Nabil Bank Limited are major commercial banks.

b. Development banks:

The development banks are those banks, whose aim is not to earn the profit. These banks can be categorized into two major types. The first type of development banks finance loan to the farmer and other agricultural sectors for short, medium and long term. On the other hand, the second type of development banks finance loan in the infrastructure development in the country. The first types of development banks in Nepal are Agricultural Development Bank and Rural Development Bank.

c. Exchange banks:

The exchange banks are those banks, which deal in foreign exchange and specialize in financing foreign trade. These banks supply the necessary foreign exchange required for settlement of transactions between traders engaged in the foreign trade. These banks also collect and supply information about the foreign customers and provide remittance facilities. The Rastriya Banijya Bank (RBB) is the exchange bank of Nepal.

d. Saving Banks:

The objectives of the saving banks are to mobilize the small savings and to promote savings in a country. In other words, these banks are specialized institutions that induce small income groups to save something out of their incomes and pool such savings. The postal saving scheme is one of the types of saving bank in Nepal.

e. Central Bank:

The central bank is the apex bank in a country that controls all monitory system and banking structure. It operates in the interest of the country and assists in the implementation of the economic policy of the government. It regulates and issues currency, performs agency and banking services to the government and manages the foreign currency reserve of the whole country. It also works as the lender of the last resort, clearing house and control. The NRB is the central bank in Nepal.

f. Industrial Bank:

The industrial banks are those banks, which provide short, medium and long term loans for the establishment of industries in the country like for the purpose of land and development, machinery and equipment. The NIDC works as the industrial bank in Nepal.

g. Co-operative Banks:

The co-operative banks are such banks which operate on the principle of co-operation. They collect small deposits, mobilize small savings and provide short-term and medium-term loans to their members.

h. Merchant Banks:

The Merchant banks accept the time deposit and finance in trade and industry. The main source of capital of these banks are the time deposits and by the issue of securities. The Nepal Sri-Lanka Merchant Bank is an example of this type of bank in Nepal. They assist business corporation to raise fund for long term capital requirement by issue of bonds.

i. Pension Fund:

The pension fund is also considered as a bank. They accept legitimate deposit from the employees of different organizations. They provide loans to different financial institution and sometime participate for the financing in trade and industry. In Nepal, Employees Provident Fund is working as a pension fund.

j. Housing Bank:

The housing banks are those banks that collect deposit, by deposits and selling securities in the capital markets whereas they finance in the development of houses in the country. In Nepal, Nepal Housing and Development Finance Company Limited is working as a housing bank.

2.3 Definition of the commercial bank

A commercial bank is a financial institution, which accepts the demand and time deposits from the business, institutions, and individuals and engages in both business and customer lending. It must use fund raised form the public deposit providing loans to agriculture, commerce and industries with the prime objectives of profit maximization. It also provides technical and administrative assistance to the industries, trade and business.

The commercial banks play the important role in directing the affairs of the economy in various ways. The size and composition of their transactions mirror the economic happenings in the country. For example, the mass failures of commercial banks during the 1930's reflected the phenomenon of reserve global depression in the world. The commercial banks have played a vital role in giving a direction financing the requirements of the trade and industry in the nations.

The commercial banks induce the savers in the community to hold their savings forming socially useful assets of which bank deposits constitute the most important element. The commercial banks draw the community savings into the organized sector, which can be allocated among the different economic activities according to the priority laid down by planning authorities in the country.

2.4.1 List of licensed commercial banks in Nepal (Till February, 2009)

- Nepal Bank Limited.
- Rastriya Banijya Bank

- Nabil Bank Limited
- Nepal Investment Bank Limited
- Standard Chartered Bank Nepal Limited
- Himalayan Bank Limited
- Nepal SBI Bank Limited
- Agriculture Development Bank Limited
- Nepal Bangladesh Bank Limited
- Everest Bank Limited
- Bank of Kathmandu Limited
- Nepal Credit and Commerce Bank Limited
- Lumbini Bank Limited
- Nepal Industrial and Commercial Bank Limited
- Machhapuchchhre Bank Limited
- Kumari Bank Limited
- Laxmi Bank Limited
- Siddhartha Bank Limited
- Global Bank Limited
- Citizen Bank International Limited
- Sunrise Bank Limited
- Prime Commercial Bank Limited
- Bank of Asia Nepal Limited
- Development Credit Bank Limited
- NMB Bank Limited

2.5 Conceptual review of commercial banks

The word ‘bank’ is derived from the Italian word ‘banco’ which means bench. Previously, bankers did their banking transactions by sitting on the bench on the open market. A bank is a kind of financial institution, which is established under the law and act for dealing with monetary transaction. Therefore, bank accepts deposit from general public and commercial organization. People can deposit their small saving amount into the bank and whenever required they can withdraw through cheques.

A commercial bank is a business organization that receives and holds deposits of funds from other, makes loan or extends credit and transfers funds by written order of depositors. From above meaning, it is obvious that a bank has two main functions; accepting deposits from public and performing transaction related to loan. Actually, modern banks perform all the required financial function and provide its service to needy people.

The commercial banks perform only commercial activities. Therefore, commercial banks are established for the purpose of earning profit. A commercial bank is one which exchanges money, deposits money, accepts deposits, grants loans and performs commercial banking functions. Principally, commercial banks accept deposits and provide loans, primarily to business firms thereby facilitating the transfer of funds in the economy. The American Institute of Banking has stated four functions of commercial banks, i.e. receiving and holding deposits, handling payments for its clients, granting loans for investment and creating money by extension of credit (American Institute of Banking, 1972).

2.6 Commercial bank in Nepal: a historical review

It is a fact that financial sector plays a vital role for the economic development of a country. Even before the establishment of a banking system in Nepal, financial transaction was in practice as undertaken by some moneylenders like sahu-mahajans, jamindars, relatives, friends, and few informal organization limited to ethnic group. Borrowing from the other peoples and the informal organizations were limited and based on personal understanding. At that time, people used to deposit their gold, silver, and valuable goods for the sake of security.

However the private money lenders supported the economic development of a country, the transaction undertaken by them was totally based on their personal understanding. No legal restrictions were against them and their monopoly in transaction was the reason for covering the interest in exploiting the people. Thus, it was realized to establish financial intermediaries in supporting the economic development of a country.

Nepal has been ruled over by many rulers as Kirats, Lichhavi, Malla, Baaise Rajas, Rana and Shah. Mostly, Kirats, Lichhavi, and Malla ruled in Nepal. At that period neither the people nor the government was interested to think about the economic development of the country.

After long time, during the Rana regime, only some prime ministers thought about the economic development of the country. They established some offices in 1993 Bikram Sambat (B.S.). No financial institutions were established over a long period due to political reasons. To fulfill the growing need of economy in Nepal, banking activities were performed only after the establishment of ‘Nepal Bank Limited’ in 1994 B.S. as the first commercial bank of Nepal. This bank was established under Nepal Bank Act 1994.

At the beginning, 49% of the ownership belonged to the promoters as well as general public and remaining belonged to the government. The incorporation of Nepal Bank Limited was the real starting of the banking institution in Nepal. Nepal Bank Limited started the act of consolidating the scattered capital since its establishment functioned to mobilize it in productive sector. It developed a systematic tradition in culture of modern banking system in Nepal. Such system could be able to establish a strong base for the improvement of national economy. Besides, it also acted as central bank for more than three decades.

As the central bank of Nepal, Nepal Rastra Bank (NRB) was established in Baisakh 14, 2013 B.S (1956 A.D.) under Nepal Rastra Bank Act 2012. It is totally owned by government. Besides the commercial banking functions, NRB is heavily assisting for the development of whole economy. It is providing timely directives to all financial institutions operated and conducted in all over the country.

The government introduced Commercial Bank Act in Nepal in 2003 B.S. to cover their vast field of financial sector. This act has helped to emerge number of commercial banks with a view to maintain the economic interest in comfort of the public in general facilitating to provide loan for agriculture, industry and trade and make available banking services to the country and people (Commercial Bank Act, 1974).

Along vacuum in the banking sector got some rays of hope only when the government forwarded the economic liberalization policy in 2039 B.S. and decided to allow foreign banks to operate their activities in Nepal in “joint-venture model”. The joint-venture banks can be defined as an association of two or more parties having common objective and goal so as to get maximum satisfaction. Basically at that time, it was envisioned that joint venture banks (JVBS) would support the country in various ways (Singh and Khadka, 1999).

In Nepalese context, the main purpose of joint-venture is to develop economic forces in order to achieve distinguished results, which the partners separately could not achieve. Nowadays, JVBS are playing dynamic and vital role in economic development of the country.

The Nabil Bank Limited is the first joint-venture bank established in 2041 B.S. and started its operation with modern banking services. Similarly, Nepal Indosuez Bank (at present Nepal Investment Bank), is the second joint venture bank established in 2042 B.S. with an objective to encourage efficient banking services and facilities. Likewise, Nepal Grindlays Bank Limited (Now, Standard Chartered Bank) is operated under their direction of Australian and New Zealand banking group (ANZ).

With the satisfactory result of joint-venture banks, Nepalese promoters are highly encouraged and as a result, commercial banks are introduced with higher percentage of domestic investment. At present, Nepal Industrial and Commercial Bank (NIC Bank), Lumbini Bank Limited, Machhapuchchhre Bank Limited, Kumari Bank Limited, Laxmi Bank Limited and Siddhartha Bank Limited came into operation with fully domestic investment by Nepalese promoters which are the plus point of development of banking history of Nepal. Now, there is a strong competition between commercial banks for their existence, so that the growing needs of the customers can easily be achieved.

2.7 Concept of profitability

A company should earn profits to survive and grow over a long period of time. It is fact that profits are essential and sufficient profits must be earned to sustain the operation of the business to be able for obtaining funds from investors for expansion and growth that contribute towards the social overheads for the welfare of the society.

Profit is the difference between revenues and expenses over a period of time. It is the ultimate output of the company, and a company will have no future if that fails to make sufficient profits. Therefore, the financial manager should continuously evaluate the efficiency of its company in term of profit.

Profitability generally refers the capacity to generate profit. It is a measurement of operating efficiency of the company. It measures how efficiently the company has managed their funds to earn profit. Besides the profitability of the firm, creditors want to get interest and repayment on their principal amount. Owners want to get a reasonable return on their investment. All these are possible only when the company earns sufficient profits.

The shareholders, bankers, government, tax-collectors, employees and all bodies concerned with the company are generally concerned with the profitability of the company whereas the shareholders are interested with the rate of return, employees in the future prospectus of the company, government in the company's tax payment capacity and in the prosperity of the company.

The profitability is a measure of efficiency and it providers incentive to achieve efficiency. It also indicates public acceptance of the product and shows that the firm can reduce competitively. Moreover, profits provide the company of repaying the debt, incurred to finance the project, and resources for the internal financing expansion. The profitability of a firm can be measured by its profitability retained. (Pandey, 1995)

The company having the capacity of earning profits, methods of earning profits, skilled bodies to operate it, can easily compete with other companies and may be a leader of the market. The profitability reflects the staying capacity of the company in the market. The company that is able to face the present market situation can generally exist and sustain in the market.

There are various problems faced by the company to exist in the present market situation. Skillful handling of the problem is the indication of profit increment. The internal as well as the external variables influence the profitability of the company. The internal variables arise from the internal sources of the organization whereas the external variable arises from the external source. Therefore, internal variables, locating within the organization can be controlled or manipulated by the company. That means the organization should face the external variables.

The company, which is skillfully facing the internal as well as external variables, can exist in the market. Those companies can easily earn the sufficient profits. For achieving the success, following factors are to be considered seriously; good management of human resources, encouragement of manpower, improved salary, good working condition, team work, good behavior to employees, good relationship between employees and customer, low absenteeism and turnover of employees, morality, consumer service, improved employee commitment, reward system, employee positive attitude towards their job, their rewards and their management. These factors are required for increasing the profitability of the company.

2.8 Factors required for profitability of commercial banks

Generally, characteristics, financial structure, and macro economic indicators of banks have impact on net interest margins and profitability of commercial bank. High net interest margin and profitability tend to be associated with bank that hold a relatively high amount, and with large overheads. Other important internal determinant of interest margins of bank is bank loan that has a positive and significant impact on company performance.

Macro-economic indicators such as inflation and growth rates have impact on bank's interest margins and profitability and stock market development has a positive effect on bank profitability.

2.9 Determinants of profitability of commercial bank

The determinants of commercial banks' profitability can be divided into two main categories: management controllable and that are beyond the control of management. Those factors, which are management controllable, are classified as internal determinants. Moreover, those which are beyond the control of management are referred to as external determinants. The management controllable internal determinants considered in this study are similar to those considered in research on bank profitability by Bourke (1989), Molyneux, Williams and Thornton (1994). The internal determinants include capital ratios, liquidity ratios, assets and liability portfolio mix and overhead experiences.

The external determinants for profitability of commercial banks can be further subdivided into environment related factors and firm specific factors. The environment related factors considered by Short (1979), Spinlock (1985), Bourke (1989) and Monyneux and Thornton (1992), include market structure, regulation, inflation, interest rate and market growth.

The companies have various functional areas such as production and operation department, finance and accounting department, marketing department, search department, human resource department, and selling and distribution department. Each department plays a vital role for achieving the success of companies. However, there is equally importance of all the departments for success of the business.

Human resource also plays a vital role for profitability. Improper utilization of human resources directly affects the profitability of the company. Therefore, human resource management (HRM) should seriously be considered. It is a management function that helps mangers to recruit, select, train and develops members for an organization. Obviously, HRM is concerned with the people's dimensions in organization. Therefore, HRM is the management and operations of the people in organization.

HR indicates the people involved in organization. Therefore, the involved (employed) peoples play a great role in the profitability of any company. If the employees involved in the organization are motivated, satisfied and competent, high degree of profitability may be achieved.

2.10 Concept of ROE framework

In recent years, the commercial banking industry has experienced a period of record profits, quite a change from the late 1980s and early 1990s when banks were falling in record numbers. Despite record profits, many banks have weak and inefficient areas that still need to be addressed. One way to identify weaknesses and problem areas is by analyzing financial statements. In particular, an analysis of selected accounting ratios (i.e. ratio analysis) allows a bank manager to evaluate the bank's current performance over a period of time (time series analysis of ratios over a period of time) and its performance relative to that of competitor banks (cross-sectional analysis ratios across a group of firms). A tool available to assist in cross-sectional analysis is the Uniform Bank Performance Report (UBPR) maintained by the Federal Financial Institution Examination Council (FFIEC). The UBPR summarizes performance of the banks for various peer groups, and by state.

The ROE (Return on Equity) framework starts with the most frequently used measures of profitability, ROE, and it breaks down to identify strengths and weaknesses in a bank's performance. The resulting breakdown provides a convenient and systematic method of identify strengths and weaknesses of a bank's profitability. Identification of strengths and weaknesses, and the reasons for them provides an excellent tool for bank managers as they look for ways to improve profitability (Saunders *et* al., 2004).

2.10.1 ROE and its components

‘Return on Equity’ is the numerical relationship between net incomes after taxes to total equity of a bank. It measures the amount of net income after taxes earned for each rupee of equity capital contributed by the bank's stockholders.

Breakdown of ROE into Various Financial Ratios

- **Return on Equity (ROE)**: Net income / Total Equity Capital
  - **Return on Assets**: Net Income / Total Assets
    - **Profit Margin**: Net income / Total Operating Income
      - Interest Expenses / Total Operating Income (Component)
      - Provision for Loan Loss / Total Operating Income
      - Non-interest Expenses / Total Operating Income (Component)
      - Total Taxes / Total Operating Income
    - **Assets Utilization**: Total Operating Income / Total Assets
      - Interest Income / Total Assets (Component)
      - Non-interest Income / Total Assets (Component)
  - **Equity Multiplier**: Total Assets / Total Equity Capital

Source: Saunders and Marcia, 2004

2.11 Profile of commercial banks under study

The establishment of commercial banks has given a new horizon to the financial sector of Nepal. The economic liberalization policy of government has provided a better opportunity for investors and consequently commercial banks and financial institutions have been incorporating rapidly. Three commercial banks selected namely Standard Chartered Bank Nepal Limited, Nabil Bank Limited and Himalayan Bank Limited is the field of study in this context.

2.11.1 Standard Chartered Bank Nepal Limited (SCBNL)

Standard Chartered Bank Nepal Limited has come from Nepal Grindlays Bank Limited (NGBL) on July 16, 2001 that was established in 1986 as a foreign joint-venture bank. It is executed under the direction of Australian and New Zealand banking group (ANZ). The ANZ Grindlays bank is the foreign joint-venture partner with 50 percent of investment. The ANZ Grindlays bank is managing under joint-venture and technical services agreement signed between ANZ Grindlays bank and Nepalese promoters. The SCBNL strives to secure the future of Nepalese entrepreneurs with the required services and know how to prosper in the new global order. It is the brainchild of leading Nepalese entrepreneurs with dream of framing the ultimate in modern merchant banking and financial services.

2.11.2 Nabil Bank Limited (NABIL)

The NBL is the first foreign joint-venture commercial bank of Nepal which was incorporated under the company act 1964. The Dubai Bank Limited was the initial foreign joint-venture partner with 50 percent equity investment. The shares owned by Dubai Bank Limited (DBL) were transferred to Emirates Bank International Limited, Dubai by virtue of its annexation with the later. Later on, Emirates Bank Limited, Dubai sold its 50 percent equity holding to National Bank Limited, Ireland. The bank is managed in accordance with the joint-venture and technical services agreement between Nepalese promoters and National Bank Limited, Ireland.

The objectives of the bank are to accept the deposits, to provide loans to agriculture, commerce and industry and to provide modern banking services to the people. The NBL has provided the services as a modern banking facility like tale-banking to the businessman, credit-master card and visa card, trade and project finance, housing loan, vehicle loan, vista electron debit branch banking service facility.

2.11.3 Himalayan Bank Limited (HBL)

The Himalayan bank limited is a joint-venture bank with Habib Bank of Pakistan. It was established in 1992 under company Act 1964. This is the first joint-venture bank managed by Nepalese chief executive. The operation of the bank started since February 1993.

The main objectives of the bank are to provide modern banking facilities like tale-banking to the businessman, industrialists, and other professionals and to provide loans on agriculture, commerce and industrial sectors. The HBL provides the services such as extension of branch, housing loan, hire-purchase loan for doctors, engineers, lawyer, chartered accountant, education loan , foreign remittance, ATM facility, vehicle loan, premium saving, debit card, internet banking, locker facility, any branch banking service facility, training for employees for skill development, and other various service facilities.

2.12 Raising the profitability of commercial banks

The banking sector in the Nepal has undergone a period of transformation and should be able to effectively fulfill the role of a main mediator of resources in the economy. The stability of the banking sector is conditional upon macro-economic conditions as well as the level of an individual bank’s management. These factors are mutually interconnected. A specific feature of a bank’s management is the fact that a bank as an enterprise, in comparison with other enterprises, is characterized by a high degree of dependence on the macro–economic development and its profit, to a large extent, is determined by the situation on the financial market, domestic as well as foreign. A further specific feature is that the success of a bank also depends on its ability to foresee and avoid risks, possibly cover losses brought about by risks arisen. In connection with a bank’s management there are often used the terms, such as: risk management, profitability management and balance-sheet structure management.

The profit is the essential prerequisite of competitive banking institution and the cheapest source of funds. It is necessary to see it not merely as a result, but also as a key for successful banking in a period of growing competition on financial markets. These facts together are the reason of bank profitability. Many problems and areas are negatively influencing bank's effectiveness. It is necessary to manage their assets and liabilities in aiming to achieve a profit and highlight areas where it might be possible to find room for raising bank's profitability.

2.13 Review of related studies and papers

2.13.1 Review of related books and articles

According to Weston & Brigham (2001), risk return trade off is one of the major financial function. They believe that the maximization of the value of the firm can be achieved through maximization of return in one hand and minimization of risk in the other hand. The relationship between the expected future state of the economy and the performance of individual firms enables a relationship to be set forth between the state of the economy and the return from investment in firms.

An article of Mr. Gyanwali (2055) on deposit mobilization refers to the collection of small and scattered savings of the people and directing them for investment in the productive purposes thereby contributing to the further increases of saving through improvement of the income level of the savers.

"A Comparative Performance Study of Rastriya Banijya Bank" by Mr. Bajracharya (2047), concluded that deposits growth of commercial bank is not so consistent; there is low growth in local/ non-joint venture banks than that in joint-venture banks. It is better on credit deposit ratio in joint-venture banks than the non-joint venture banks/local banks. Non-performing loan was greater in non-joint venture banks and profitability was greater in joint-venture bank. The local banks are forced to open their branches at the rural areas but joint-venture banks are not forced in this rule. Therefore, the competition among the local banks and joint- venture banks is not healthy.

Another article of Mr. Bajracharya (2047) on " Monitory Policy and Deposit Mobilization in Nepal", from "Rajat Jayanti Smarika”, opines that mobilization of domestic saving is one of the prime objectives of the most active financial intermediary for generating resources in the forms of the private sector and providing credit to the investors in different sectors of the economy.

Next article of Mr. Shrestha (2047) on "Commercial Banks’ Performance Evaluation" concluded that joint-venture banks are operationally more efficient having superior performance while comparing with non joint-venture banks. Better performance of joint-venture banks is due to their sophisticated technology, modern banking method via computerization, prompt customer service and skills. The local banks are efficient. But, in rural sectors, these are having numbers of deficiencies. Therefore, local banks have to face growing constraint of social, economical, political system on one spectrum and that of issues and challenges of joint-venture banks commanding significant banking business on other spectrum.

In the same way, an article by Mr. Thakur (2052) on "Performance of Nepalese Commercial Banks," stated that the joint-venture banks are successful not in only penetrating the market but also consolidating their position over the year. It is due to its customer orientation and strong marketing strategy.

Mr. Shrestha (2045) made a study on "A Study on Deposits and Credits of Commercial Banks in Nepal", which revealed that in 2004 A.D., the credit deposit ratio would be 5:13, other things remaining the same, which was the lowest under the period of review. Therefore, he strongly suggested that the commercial banks should try to provide more credit facility lunching new banking product otherwise they could not be able to absorb its total expenses.

2.13.2 Review of relevant dissertations

Prior to this, several thesis works have been conducted by various researchers regarding different aspects of commercial banks like financial performance, capital structure, investment policy, interest rate structure and resources mobilization. The excerpts from the findings of some of these research works are presented which are relevant for this study.

Mr. Joshi (1989 A.D.) studied the performance of commercial banks and concluded that the liquidity position of commercial banks was sound. But debt equity ratio of commercial or non-joint venture banks was higher than the joint-venture banks. He also said that the commercial banks had low profit margin but satisfactory return on net worth.

Similarly Mr. Dhungana (1994 A.D.) conducted "A Study of the Joint Venture Banks' Profitability" covering the period of five years from 1987/88 to 1991/92 with the main objectives of accessing the profitability of joint venture banks in Nepal. His study concluded that the interest income of Nepal Grindlays Banks Limited (present Standard Chartered Bank Nepal Limited) was highest than the other joint venture banks, Nepal Indosuez Bank Limited's (present Nepal Investment Bank Limited) commission and discount earning and foreign exchange income were higher than both Nepal Grindlays Bank Limited (NGBL) and Nepal Arab Bank Limited (NABIL). The NABIL's other operating income was appeared higher than the other banks. The NGBL had the highest earning per share and cash dividend per share in an average.

Mr. Kaini (1997 A.D.) has done a comparative study of financial performance of Nepal Arab Bank Limited (at present Nabil Bank Limited) and Nepal Grindlays Bank Limited (at present Standard Chartered Bank Nepal Limited) with the help of primary and secondary data . He concluded that liquidity ratio of both banks were below the normal standard though profitability ratios of both banks were able to maintain the standard.

Mrs. Shrestha (1990 A.D.) conducted a research work on portfolio behavior for commercial banks in Nepal. She concluded the debt to equity ratio of commercial banks highly leveraged and was with high risk. Furthermore, the researcher argued that the capital adequacy ratio explains the strength of the capital base of commercial banks. The higher the capital adequacy ratio, higher is its internal sources and vice versa.

Mr. Bohara (1992 A.D.) conducted a study on financial performance of Nepal Arab Bank Limited (NABIL) and Nepal Indosuez Bank Limited (NIBL) with main objectives of evaluating the comparative financial performance of NABIL and NIBL. Different ratios: liquidity, activity, coverage, leverage, profitability and other indicators like earning per share, dividend per share, market value to book value ratio were used to evaluate the performance of NABIL and NIBL and finally, concluded that performance of NABIL is better than that of NIBL.

Mr. Adhikari (1993 A.D.) studied on evaluation of the financial performance of Nepal Bank Limited with main objective of the research to evaluate the financial performance of bank. The major indicators of financial performance used were financial ratios- current, loan to deposit, return on capital, return in net worth , return on total assets, earning per share, dividend per share, pay out and net worth per share versus market price per share. Finally, the researcher concluded that the bank had not managed investment portfolio efficiently. The operational efficiency was not satisfactory. During the study period, except liquidity position, all other financial indicators were not satisfactory.

Mr. Joshi (1993 A.D.) has done a study on commercial banks of Nepal with reference to financial analysis of Rastriya Banijya Bank. The objective of this study was to provide conceptual framework of commercial banks, and to analyze and interpret these financial variables of Rastriya Banijya Bank (RBB) on qualitative and quantitative performance basis. The study was based on the financial data of Fiscal Year 2042 B.S. through 2046 B.S. Researcher has used various financial ratios like: current liquidity, funded debt to total capitalization and funded debt to equity in this study. The researcher had drawn the conclusion that performance of RBB was not satisfactory during the study period. Further, the researcher concluded that bank had not been managed in true professional approach but had managed in bureaucratic approach to sustain with political environment rather than commercial environment.

Mr. Shakya (1995 A.D.) performed a study on financial analysis of joint- venture banks in Nepal. The objective of this study was to carry out the comparative financial performance evaluation of Nepal Arab Bank Limited (at present NBL) and Nepal Grindlays Bank Limited (at present SCBNL). The researcher has found that in spite of the increase in loans and deposits of both banks, their performance measured in terms of deposit utilization rate is not satisfactory. Again, the study concluded that financial performance of NBL was better than that of NGBL.

Mr. Gurung (1995 A.D.) conducted a research on financial study of joint- venture banks in Nepal. The objective of this study was to examine the financial strengths and weaknesses of NGBL and NIBL. The researcher has, on the basis of different financial indicators; found that performance of NGBL was better than that of NIBL.

Likewise, Mr. Deoja (2001 A.D.) conducted study entitled "A Comparative Study of the Financial Performance between Nepal State Bank of India Limited (NSIBL) and Nepal Bangladesh Bank Limited (NBBL)." The researcher's main objective of study was to evaluate the trend of deposits and loan and advances of NSBIL and NBBL and to evaluate the liquidity, profitability, capital structure, turnover and capital adequacy position of NSBIL and NBBL. Through research, he found that the cash and bank balance to current assets, saving deposit to total deposit of NSBIL are higher while fixed deposit to total deposits, loans and advances to current assets of NBBL are higher. Similarly NBBL has better turnover than NSBIL in terms of loan and advances to total deposits ratio and loan and advances to fixed deposit ratio. Through the study of the different ratios, he has concluded that both banks are highly leveraged.

Furthermore, Mr. Bhandari (2006 A.D.) used descriptive analysis in his research work of evaluating financial performance of Himalayan Bank in the framework of CAMEL. The analysis revealed adequate capital of the bank. The non-performing loan though in decreasing trend is still a matter of concern. The bank is still with better ROE however it is in decreasing trend. The decreasing trend of net interest margin shows management slack monitoring over the bank's earning assets. The liquid funds to total deposit ratio is above the industrial average ratio. NRB balance and cash in vault to total deposit ratios are below the industrial average ratio during the study period.

In the same way, Mr. Chand (2006 A.D.) conducted “A Financial Performance Analysis of Nabil Bank Limited in the frameworks of CAMELS” with main objectives of evaluating capital adequacy, assets quality, management efficiency, earning quality, liquidity and sensitivity to market risks and concluded that NBL has maintained the capital adequacy with NRB boundaries. The assets composition of NBL is mainly focused on loan and advances. The earning efficiency of the bank is sound and in case of liquidity the bank has not followed the NRB norms effectively.

Similarly, Mr. Poudyal (2000 A.D.) studied the financial performance of Annapurna Finance Company Limited with working capital management. The objective of his study was to analyze the working capital management with reference to the liquidity and the profitability position of the company with the help of the secondary data. He concluded that the company was improving its liquidity condition and the working capital was satisfactory. .

Mr Basnet (2007) conducted a research work on diagnosis of financial health of Nepal Investment Bank Limited (NIBL). The objective of this study was to find out the financial health of NIBL in the framework of CAMELS. Her study has covered only six fiscal years from 2000/01 to 2005/06. This research has mainly focused on financial aspects of NIBL and was based on secondary data. He concluded that supplementary capital of the bank is sufficient to meet the banking operation as per the NRB standard.

Again, Mr. Sharma (2007) conducted the study on financial performance analysis of Nepal SBI Bank Limited. The basic objective of this study was to analyze the financial performance of NSBL in the CAMELS framework. This study has covered data from 2001 to 2006. His research based on secondary data. He concluded that NSBL has maintained the adequate total capital fund prescribed by NRB. The quality of loan of the bank was strong except in year 2001. The bank has satisfactory level of income as compared to the total asset of the bank. The bank maintained an average of 2.58 % liquidity in vault which is supposed to be adequate. The bank has not made sufficient provision for the sub-standard loan as prescribed by NRB.

CHAPTER III
RESEARCH METHODOLOGY

This chapter includes research design, population and sample, nature and sources of data, methods of data collection, data analysis tools and limitations of methodology. The above research procedures are adopted comprehensively to accomplish the objectives set in Chapter 1.`

3.1 Research design

The evaluation of the performance is designed to reflect an assessment of the profitability status of the three banks based on the ROE framework prescribed by Federal Financial Institutions Examination Council. Hence, the research is conducted on a historical and analytical case study basis. Therefore, a descriptive-cum analytical research methodology has been followed, to achieve the desired objectives. In order to evaluate the financial performance of selected banks, some financial and statistical tools and descriptive techniques are applied.

3.2 Population and sample

There are many financial institutions in Nepal, however this study concerns with some commercial banks operating in Nepalese banking industry. The population of the study is the total number of commercial banks operating banking business in Nepal. And three samples are taken from total population of 25 commercial banks on convenient sampling basis.

The population of the present study is listed in *Appendix I*, the commercial banks operating in the banking industry of Nepal. From such population, three samples (SCBNL, NBL and HBL) were considered for analysis. Being leading commercial banks in Nepal, these banks are considered as samples in this study.

3.3 Nature and sources of data

Basically, the research is based on secondary information data. The annual reports of the banks form the major sources of data. The regulatory data were collected from NRB directives and reports. The information related to the past and current works conducted in the research field were collected from the following sources:

- NRB reports and bulletins and its official website
- Various research papers and dissertations
- Various articles published in journals and financial magazines
- Nepal Stock Exchange reports
- Official websites of banks

Formal and informal discussions with the senior staff of the banks were held which was helpful in understanding and obtaining the additional information.

3.4 Data collection procedure

The required information was collected by conducting visit to the branch office of each bank at Pokhara, consulting library at P.N. Campus and Pokhara College of Management, internet browsing and related text books. The annual reports of the selected banks for the study period were obtained from their Pokhara branch through personal approach and internet surfing to the banks' official websites. The NRB regulatory directives, Statistics of the Commercial Banks of Nepal and other related publication were obtained through internet surfing to NRB’s official website and periodicals. Existing literature on the subject matter was collected from various research papers placed in Western Regional Library (T.U.), Pokhara. Likewise, the review of working papers conducted by various scholars on the related matter was done through internet surfing to various websites.

3.5 Data processing

The financial data from the published documents and audited financial statements were manually extracted into the computer files of Microsoft Excel program which acted as master database file. The data was refined further into spreadsheets to carry out financial ratio calculation and graphical illustrations through mathematical functions and Chart program of the Excel program.

3.6 Data analysis tools

Financial ratios were the major tools used for the descriptive analysis of the study. In addition to the financial tools, simple statistical tools were also used.

3.6.1 Financial Ratio Analysis Tools

Financial ratio analysis tools were used to determine the profitability of the banks in the framework of ROE components. These ratios were categorized in accordance of the ROE components. Following category of key ratios were used to analyze the relevant components in terms of ROE:

1) **Return on Equity (ROE):** Return on Equity is the numerical relationship between net incomes after taxes to total equity of a bank. It measures the amount of net income after taxes earned for each rupee of equity capital contributed by the bank's stockholders, which is determined in the following way:

$$\text{Return on Equity (ROE)} = \frac{\text{Net Income}}{\text{Total Equity Capital}} \text{x100}$$

2) **Return on Assets (ROA):** Return on assets is the numerical relationship between net incomes after taxes to total assets of a bank. It is primarily an indicator of the quality of assets, managerial efficiency to utilize the institution's assets into net earnings (Rose, 1999). Higher the ROA, higher is the quality of assets and efficient asset utilization. It is calculated by using the following model.

$$\text{Return on Assets (ROA)} = \frac{\text{Net Income (after tax)}}{\text{Total Assets}} \text{x100}$$

3) **Equity Multiplier (EM):** Equity multiplier measures the extent to which assets of the banks and financial institutions are funded with equity to debt, which is calculated by using the following model.

$$\text{Equity Multiplier (EM)} = \frac{\text{Total Assets}}{\text{Total Equity}}$$

4) Profit Margin (PM): Profit Margin measures the ability to pay expenses and generate net income from interest and non-interest income, which is calculated by using the following model.

$$\text{Profit Margin (PM)} = \frac{\text{Net Income}}{\text{Total Operating Income}} \times 100$$

5) Assets Utilization (AU): Assets Utilization is the numerical relationship between interest income and non-interest income to total assets of a banks and financial institutions. It measures the amount of interest income and non-interest income generated per rupee of total assets, which is calculated by using the following model.

$$\text{Assets Utilization (AU)} = \frac{\text{Total Operatin Income}}{\text{Total Assets}} \times 100$$

3.6.2 Statistical tools

- **Average (**X**):** 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, 1989). Thus, the average is expressed as:

$$\mathbf{X} = \frac{\Sigma x}{N}$$

Where, $\mathbf{X}$ = Mean of the values, N = Number of pairs of observation.

During the analysis of data, mean is calculated by using the statistical formula average on excel data sheet on computer.

- **Standard Deviation (**σ**):** Standard deviation is the absolute measure of dispersion of the values and shows the deviation or dispersion in absolute term (Kothari, 1989). Here, the standard deviation is used to find out the deviation in absolute term. Standard deviation is determined in the following way:

$$|\exists = \sqrt{\left(\frac{(x-X)^2}{n}\right)}$$

Here, n = Number of observations

x = Individual value, **X** = Simple Arithmetic mean

During the analysis of data, standard deviation is calculated by using the statistical function 'stdev' of Excel data sheet on computer.

- **Coefficient of Variation (CV):** Coefficient of variation is the relative measure of dispersion based on the standard deviation (Kothari, 1989). It is most commonly used to measure the variation of data and more useful for the comparative study of variability in two or more series or graphs or distribution. Symbolically, the coefficient of variation is defined as:

$$CV = \frac{\sigma^2}{X}$$

Here, σ = standard deviation, X = Sample mean,

CV = Coefficient of variation

3.7 Limitations of the methodology

The research is conducted to fulfill the academic requirement of Master in Business Studies degree. It is focused on the financial analysis of the selected banks in the framework of ROE and is based on reliable disclosure of audited financial reports the banks during the period 2002/03 to 2006/07. Since the research work on ROE framework has been conducted to some extent done in Nepalese environment, the study may not reveal reliability and validity in every field. The basic limiting conditions, within which the research work is conducted, are:

1. The evaluation is made herein of three sample units of SCBNL, NABIL and HBL only, hence can not be reasoned for similar condition of the whole industry. However, it gives a particular direction to the industry.

2. The study remains largely in the realms of Offsite Monitoring System. Hence, qualitative assessment may not be reflected by the study. However, the proxy financial tools are helpful to give a close picture of such factors.

3. The quarterly financial reports of the banks are not publicly available or if available not adequate whereas the effectiveness of ROE assessment requires quarterly financial reports.

The data figures from different other sources may not be congruent with the bank's published data. However, audited data published by the banks are treated as authentic. The study is carried out within the framework of case study research design. Therefore, it is difficult to eliminate the limitations of the case study research design, in which the study as well as the methodology is bounded. Only a single unit is taken for the study, therefore, the study may not be able to represent the whole banking industry.

CHAPTER IV

DATA PRESENTATION AND ANALYSIS

This chapter deals with the presentation of data collected and its analysis focused on the ROE framework. The major findings from the analysis are shown following the presentation. The data collected from different sources have been refined and documented in Excel tables, which are further processed to analyze and arrive at the findings on the Profitability Analysis of three Nepalese commercial banks in terms of ROE framework.

4.1 The ROE Framework

The profitability generally measures the efficiency of commercial organizations. A good profitability situation refers their good position or efficiency of organization while low profitability saturation is the indication of the lower efficiency of the organization. It also indicates the financial condition of an income and expenditure of the organization.Net profit is a very basic indicator of an organization's profitability. Besides earning per share (EPS), dividend paid per share (DPS), resource utilization and mobilization capacity, investment capacity are the other important indicators of profitability.

The ROE Frame work starts with the most frequently used measures of profitability, ROE, and then beaks it down to identify strengths and weaknesses in a bank's performance. The resulting breakdown provides a convenient and systematic method of identify strengths and weaknesses of a bank's profitability. Identification of strengths and weaknesses, and the reasons for them provides an excellent tool for bank managers as they look for ways to improve profitability. Under the ROE framework, five financial ratios were been analyzed for the study; which are Return on Equity (ROE), Return on Assets (ROA), Equity Multiplier (EM), Profit Margin (PM) and Assets Utilization (AU).

4.1.1 Return on Equity Ratio (ROE)

The term 'ROE' is measure of the rate of return flowing to the bank's shareholders. The ROE is the profit as a percentage return on the owner's stake in a firm. The level of profit depends on the ROE i.e. the profit per dollar invested (Meir, 1999).

Table 4.1: Return on Equity Ratio (ROE)

Standard Chartered Bank Nepal Limited (SCBNL)			
Fiscal Year	**Net Income (Million)**	**Total Equity (Million)**	**Return on Equity (ROE) %**
2002/03 (059/60)	479	1435	33.38%
2003/04 (060/61)	507	1465	34.61%
2004/05 (061/62)	538	1560	34.49%
2005/06 (062/63)	536	1664	32.21%
2006/07 (063/64)	659	1844	35.74%
Average	**543.8**	**1593.6**	**34.08%**

Nabil Bank Limited (NABIL)			
Fiscal Year	**Net Income (Million)**	**Total Equity (Million)**	**Return on Equity (ROE) %**
2002/03 (059/60)	416	1314	31.66%
2003/04 (060/61)	455	1482	30.70%
2004/05 (061/62)	520	1658	31.36%
2005/06 (062/63)	635	1875	33.87%
2006/07 (063/64)	674	2057	32.77%
Average	**540**	**1677.2**	**32.07%**

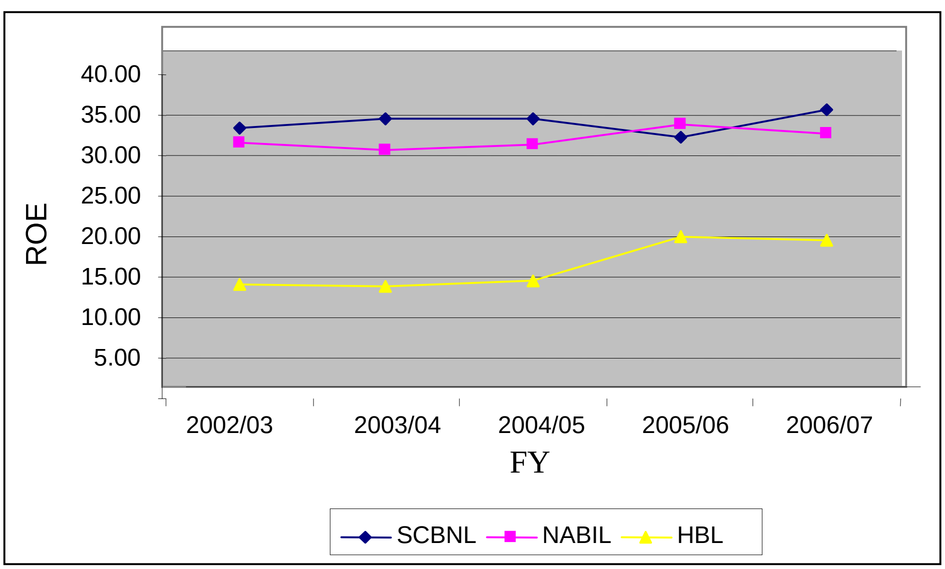
Himalayan Bank Limited (HBL)			
Fiscal Year	**Net Income (Million)**	**Total Equity (Million)**	**Return on Equity (ROE) %**
2002/03 (059/60)	212	1502	14.11%
2003/04 (060/61)	263	1906	13.80%
2004/05 (061/62)	308	2126	14.49%
2005/06 (062/63)	457	2292	19.94%
2006/07 (063/64)	492	2506	19.63%
Average	**346.4**	**2,066.40**	**16.39%**

Source: Annual Reports, 2002-2006

Computed as the ratio of net income to the equity, it reflects the income earned from its internal sources. The ROE measures the book return to the owners of the firm. It is a 'bottom line ratio' in that sense (Weston and Copeland, 1991). The return on equity reveals how well the bank uses the resources of owners. The higher ratio represents sound management and efficient mobilization of the owner's equity and vice- versa. The ROE of 15% is treated as a standard and banking industry are desired to have higher value than this (World Bank, 1996).

As shown in Table 4.1, the ROE of SCBNL of 32.21% was the minimum in 2005/06 and maximum of 35.74% in 2006/07. The ratio fluctuated between 32.21% in the year of 2005/06 and 35.74% of the final period of 2006/07. The average ROE of the bank was 34.08%. In all years of the review period and obviously the average ROE ratio was above the 15% benchmark. Hence, the bank's ROE ratio was sound. On the other hand, ROE of NABIL was maximum with 33.87% in the FY 2005/06 and minimum of 30.70% in FY 2003/04. The average ROE ratio of the bank is 32.07%. The average ROE ratio above the 15% benchmark showed that the bank also seemed to have sound profitability. Similarly, the ROE of HBL was maximum with 19.94% in the year of 2005/06 and minimum with 13.80% in the year of 2003/04. The average ROE of the bank was 16.39% which is above the 15% benchmark. This indicated the bank's ROE ratio to have in good range.

Figure 4.1: Return on Equity Ratio (ROE)



As shown in Figure 4.1, the ROE ratio of SCBNL slightly decreased in 2005/06 and finally increased in 2006/07. The slope of the curve was positive which indicated the upward trend in ratio of bank during the period of five years. The average ROE ratio was also above the benchmark. The increasing trend of ratios implied that earning quality of the bank was getting better. Similarly, the slope of the ratio of NABIL was also positive. This indicated the upward trend in the ratio of bank during the periods. The observed values of the ratio of both banks were slightly fluctuating over the study period. Comparatively, the ratio of HBL was found to be in very low position. However, the slope of the ratio was positive. In first three years the ratios were below the benchmark of 15%, which indicates the poor earning quality of the bank. In the last two fiscal years, slope of the ratio was above 15%. This showed the improvement in the earning quality of the bank.

4.1.2 Return on Assets Ratio (ROA)

The 'ROA' determines the net income produced per dollar of assets. It is a measure of profitability linked to the asset size of the bank (Saunders and Cornett, 2004). It is primarily an indicator of managerial efficiency indicating how efficiently the management of the bank has been converting the institution's assets into net earnings (Rose, 1999). The ROA is a popular tool to measure how well its asset is utilized in generating profit. It measures the profit earning capacity by utilizing available resources (i.e. total assets).

The return will be higher if the bank's resources are well managed and efficiently utilized. Generally, the return on assets ratio should be 1% and higher is desired to the banking industry (World Bank, 1996).

The ROA is the numerical relationship between net incomes after taxes to total assets of a bank. It is primarily an indicator of the quality of assets, managerial efficiency to utilize the institution's assets into net earnings. Higher the ROA, higher is the quality of assets and efficient asset utilization.

As shown in Table 4.2, the return on asset ratio of SCBNL was minimum in FY 2004/05 with 2.28% and maximum in FY 2002/03 with 2.60 %. The overall ratio of the bank during study period was slightly fluctuating. The average ratio of the bank was 2.46 %. The return on asset ratio of NABIL was minimum in 2006/07 with 2.47% and maximum in 2004/05 with 3.05 %. The overall ROA ratio of the bank also was slightly fluctuating during the study period. The average ROA ratio of the bank was 2.73%.

Table 4.2: Return on Assets ratio (ROA)

Standard Chartered Bank Nepal Limited (SCBNL)			
Fiscal Year	**Net Income (Million)**	**Total Assets (Million)**	**Return on Assets (ROA) %**
2002/03 (059/60)	479	18443	2.60%
2003/04 (060/61)	507	20911	2.42%
2004/05 (061/62)	538	23642	2.28%
2005/06 (062/63)	536	21782	2.46%
2006/07 (063/64)	659	25776	2.56%
Average	**543.8**	**22110.8**	**2.46%**

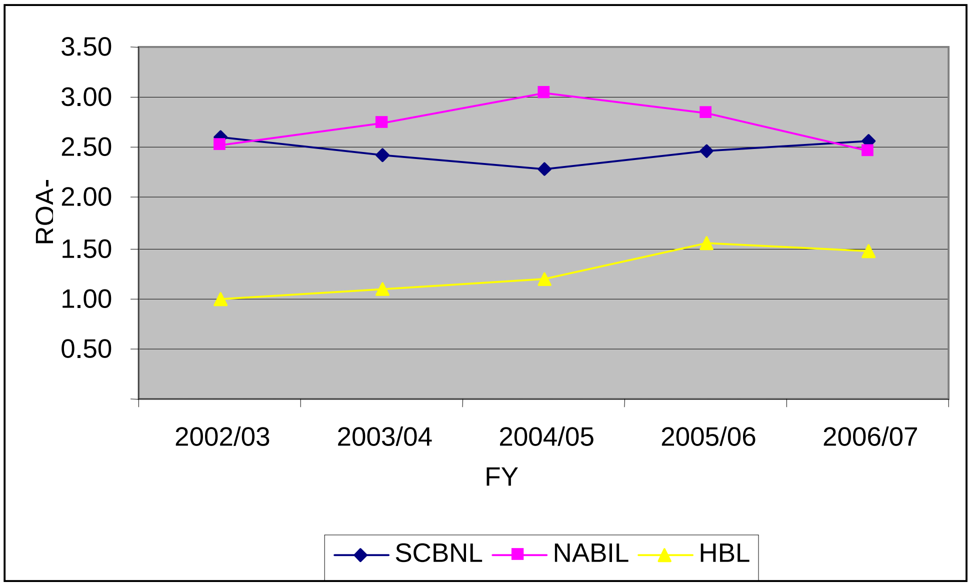
Nabil Bank Limited (NABIL)			
Fiscal Year	**Net Income (Million)**	**Total Assets (Million)**	**Return on Assets (ROA) %**
2002/03 (059/60)	416	16437	2.53%
2003/04 (060/61)	455	16633	2.74%
2004/05 (061/62)	520	17064	3.05%
2005/06 (062/63)	635	22330	2.84%
2006/07 (063/64)	674	27253	2.47%
Average	**540**	**19943.4**	**2.73%**

Himalayan Bank Limited (HBL)			
Fiscal Year	**Net Income (Million)**	**Total Assets (Million)**	**Return on Assets (ROA) %**
2002/03 (059/60)	212	21316	0.99%
2003/04 (060/61)	263	24198	1.09%
2004/05 (061/62)	308	25730	1.20%
2005/06 (062/63)	457	29460	1.55%
2006/07 (063/64)	492	33519	1.47%
Average	**346.4**	**26844.6**	**1.26%**

Source: Annual Reports, 2002-2006

The mean ratios of both banks' were two folds above the 1% benchmark, which showed the quality of assets and their efficiency to generate return was sound. Similarly, the ROA of HBL was minimum of 0.99% in FY 2002/03 and maximum of 1.55% in FY 2005/06. The bank's mean ROA ratio was 1.26%. Since the average ROA ratio of the bank was above the benchmark of 1%, the bank's ratio was better but with decreasing tendency.

Figure 4.2: Return on Assets Ratio (ROA)



The Figure 4.2 shows that the ROA ratio of SCBNL was in decreasing trend in the first 3 years and increasing trend in the remaining 2 years. On the contrary, the ROA of NABIL was in increasing trend in the first 3 years and decreasing trend in remaining 2 years. However, the ROA ratios of the both banks were above 1% benchmark in each FY. On the other hand, the ROA of HBL was in increasing trend till FY 2005/06 and finally decreased in FY 2006/07. The ROA ratio of the bank was above 1% benchmark except during initial year 2002/03.

4.1.3 Equity Multiplier (EM)

The 'Equity Multiplier (EM)' measures the extent to which assets of the banks and financial institutions are funded with equity to debt.

Table 4.3 tabulated the bank's Equity Multiplier during the review period. As tabulated, EM of SCBNL with 15.16 was maximum in FY 2004/05 and minimum with 12.85 in FY 2002/03. The average EM ratio of the bank was 13.87. This ratio of the bank was slightly fluctuating over the study period. Moreover, EM of NABIL with 13.25 was maximum

Table 4.3: Equity Multiplier

Standard Chartered Bank Nepal Limited (SCBNL)			
Fiscal Year	**Total Assets (Million)**	**Total Equity (Million)**	**Equity Multiplier (EM) %**
2002/03 (059/60)	18443	1435	12.85
2003/04 (060/61)	20911	1465	14.27
2004/05 (061/62)	23642	1560	15.16
2005/06 (062/63)	21782	1664	13.09
2006/07 (063/64)	25776	1844	13.98
Average	**22110.8**	**1593.6**	**13.87**

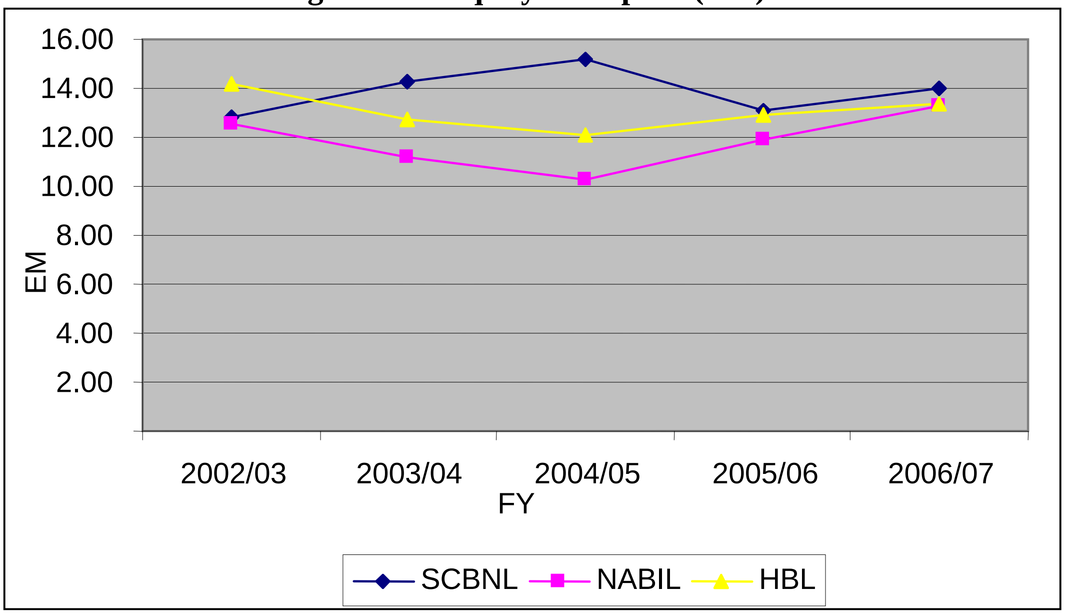
Nabil Bank Limited (NABIL)			
Fiscal Year	**Total Assets (Million)**	**Total Equity (Million)**	**Equity Multiplier (EM) %**
2002/03 (059/60)	16437	1314	12.51
2003/04 (060/61)	16633	1482	11.22
2004/05 (061/62)	17064	1658	10.29
2005/06 (062/63)	22330	1875	11.91
2006/07 (063/64)	27253	2057	13.25
Average	**19943.4**	**1677.2**	**11.84**

Himalayan Bank Limited (HBL)			
Fiscal Year	**Total Assets (Million)**	**Total Equity (Million)**	**Equity Multiplier (EM) %**
2002/03 (059/60)	21316	1502	14.19
2003/04 (060/61)	24198	1906	12.70
2004/05 (061/62)	25730	2126	12.10
2005/06 (062/63)	29460	2292	12.85
2006/07 (063/64)	33519	2506	13.38
Average	**26844.6**	**2066.4**	**13.04**

Source: Annual Reports, 2002-2006

in FY 2006/07 and minimum with 10.29 in FY 2004/05 and the mean EM ratio of the bank was 11.84. In the case of the HBL, EM ratio was maximum with 14.19 in FY 2002/03 and minimum with 12.10 in FY 2004/05 and the average EM ratio of the bank was 13.04 during the study period.

Figure 4.3: Equity Multiplier (EM)



The Figure 4.3 represented the data tabulated in Table 4.3. As shown in the chart, the EM value of SCBNL was in increasing trend in the first 3 fiscal year and decreased in FY 2005/06 and again increased in the final year. Whereas, the trend of ratio of NABIL and HBL was in decreasing order in the first 3 fiscal years and increasing in the remaining 2 fiscal years.

4.1.4 Profit Margin (PM)

The 'Profit Margin (PM)' measures the ability to pay expenses and generate net income from interest and non-interest income.

Table 4.4 presented the Profit Margin of the banks. Here, the PM value of SCBNL was maximum with 37.11% in FY 2006/07 and minimum with 33.10% in FY 2002/03. The average PM ratio of the bank was 34.37%. Similarly, the PM of NABIL was maximum with 46.69% in 2005/06 and minimum with 31.02% in FY 2002/03. The average Profit Margin ratio of the bank was 38.72% during study period.

Moreover, the profit margin of HBL was maximum with 35.32% in FY 2006/07 and minimum with 15.25% in FY 2002/03. The average Profit Margin ratio of the bank was 24.34%. The PM ratios of all banks were in increasing trend during the study period.

Table 4.4: Profit Margin (PM)

Standard Chartered Bank Nepal Limited (SCBNL)

Fiscal Year	Net Income (Million)	Total Operating Income (Million)	Profit Margin (PM) %
2002/03 (059/60)	479	1447	33.10%
2003/04 (060/61)	507	1505	33.69%
2004/05 (061/62)	538	1584	33.96%
2005/06 (062/63)	536	1576	34.01%
2006/07 (063/64)	659	1776	37.11%
Average	**543.8**	**1577.6**	**34.37%**

Nabil Bank Limited (NABIL)

Fiscal Year	Net Income (Million)	Total Operating Income (Million)	Profit Margin (PM) %
2002/03 (059/60)	416	1341	31.02%
2003/04 (060/61)	455	1334	34.11%
2004/05 (061/62)	520	1435	36.24%
2005/06 (062/63)	635	1360	46.69%
2006/07 (063/64)	674	1480	45.54%
Average	**540**	**1390**	**38.72%**

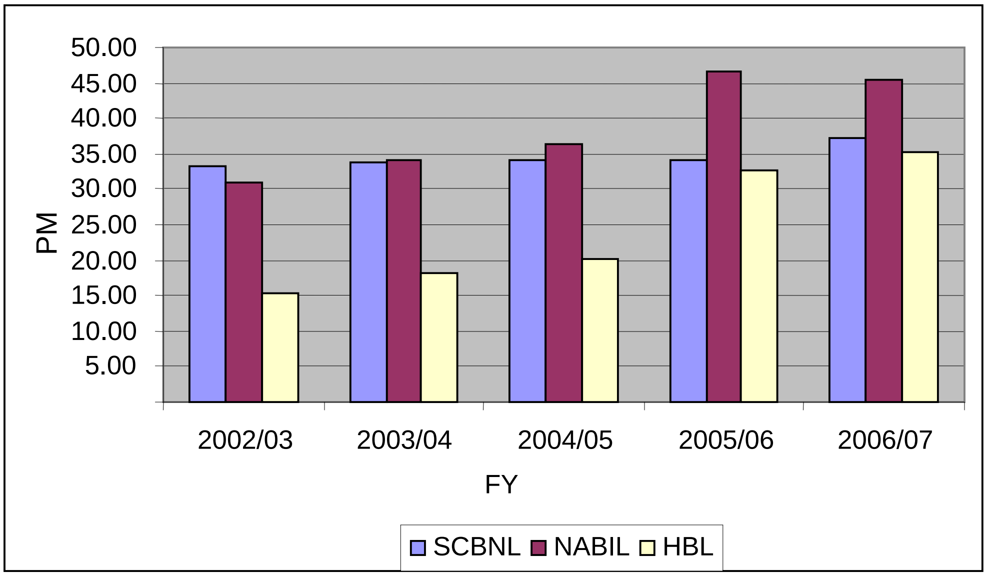
Himalayan Bank Limited (HBL)

Fiscal Year	Net Income (Million)	Total Operating Income (Million)	Profit Margin (PM) %
2002/03 (059/60)	212	1390	15.25%
2003/04 (060/61)	263	1454	18.09%
2004/05 (061/62)	308	1520	20.26%
2005/06 (062/63)	457	1394	32.78%
2006/07 (063/64)	492	1393	35.32%
Average	**346.4**	**1430.2**	**24.34%**

Source: Annual Reports, 2002-06

As shown in Figure 4.4, the PM ratios of SCBNL and HBL were found to have increasing trend in all observed fiscal years. However, the same ratio of NABIL was increasing trend till FY 2005/06 and decreased in FY 2006/07.

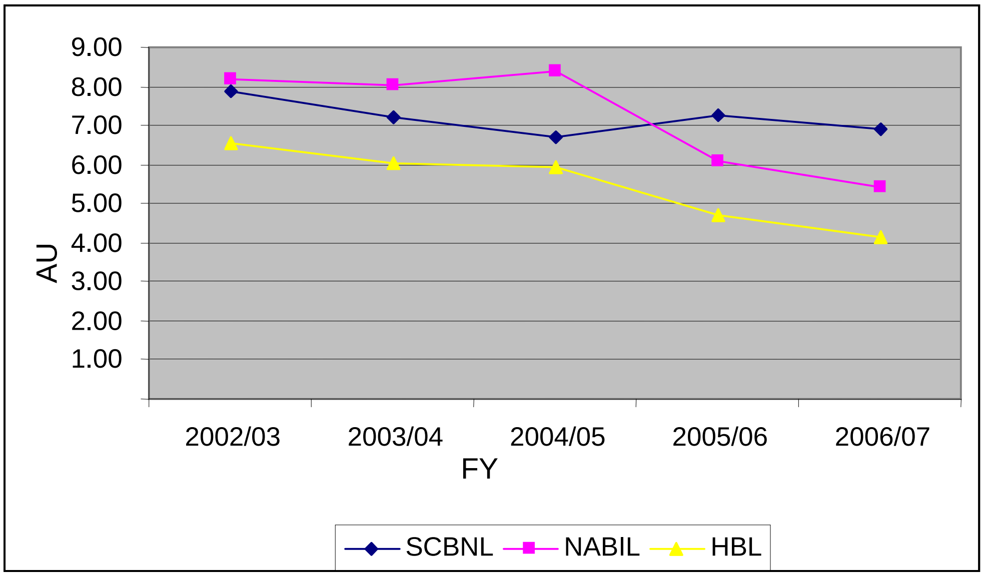
Figure 4.4: Profit Margin (PM)



4.1.5 Assets Utilization (AU)

The ‘Assets Utilization (AU)’ is the numerical relationship between interest income and non-interest income to total assets of a banks and financial institutions. It measures the amount of interest income and non-interest income generated per rupee of total assets.

Figure 4.5: Assets Utilization (AU)



The Figure 4.5 showed the values of Asset Utilization ratios of considered banks with a decreasing trend. The AU ratios of SCBNL were continuously lowering till FY 2004/05. Likewise, the AU ratios of NABIL were also with continuously decreasing trend except in FY 2004/05. On the other hand, the trend of ratio of HBL was decreasing during the study period.

Table 4.5: Assets Utilization (AU)

Standard Chartered Bank Nepal Limited (SCBNL)

Fiscal Year	Total Operating Income (Million)	Total Assets (Million)	Assets Utilization (AU)
2002/03 (059/60)	1447	18443	7.85%
2003/04 (060/61)	1505	20911	7.20%
2004/05 (061/62)	1584	23642	6.70%
2005/06 (062/63)	1576	21782	7.24%
2006/07 (063/64)	1776	25776	6.89%
Average	**1577.6**	**22110.8**	**7.17%**

Nabil Bank Limited (NABIL)

Fiscal Year	Total Operating Income (Million)	Total Assets (Million)	Assets Utilization (AU)
2002/03 (059/60)	1341	16437	8.16%
2003/04 (060/61)	1334	16633	8.02%
2004/05 (061/62)	1435	17064	8.41%
2005/06 (062/63)	1360	22330	6.09%
2006/07 (063/64)	1480	27253	5.43%
Average	**1390**	**19943.4**	**7.22%**

Himalayan Bank Limited (HBL)

Fiscal Year	Total Operating Income (Million)	Total Assets (Million)	Assets Utilization (AU)
2002/03 (059/60)	1390	21316	6.52%
2003/04 (060/61)	1454	24198	6.01%
2004/05 (061/62)	1520	25730	5.91%
2005/06 (062/63)	1394	29460	4.73%
2006/07 (063/64)	1393	33519	4.16%
Average	**1430.2**	**26844.6**	**5.46%**

Source: Annual Reports, 2002-2006

The Table 4.5 exhibited that the Asset Utilization ratio of SCBNL was maximum with 7.85% in FY 2002/03 and minimum with 6.70% in FY 2004/05. The average AU ratio of the bank was 7.17%. The AU ratio of the bank was found slightly fluctuating during study years. Meanwhile, the AU ratio of NABIL for the study period was in continuously lowering trend except in FY 2004/05. The ratio ranged from 5.43% in FY 2006/07 to 8.41% in FY 2004/05 with an average AU ratio of 7.22%. Likewise, the Asset Utilization ratio of HBL for the study period was also with decreasing trend. The ratios ranged from 4.16% in FY 2006/07 to 6.52% in FY 2002/03 with an average of 5.46%. However, the positive AU ratios of the banks during the study period indicated the sound earning level on the basis of total asset.

4.2 Major findings

The major findings of the study on the profitability analysis of commercial banks in the ROE framework are as follows:

i) The SCBNL had maintained the ROE of 32.21% with the minimum in 2005/06 and maximum of 35.74% in 2006/07. The ratio fluctuated between 32.21% in the year of 2005/06 and 35.74% of the final period of 2006/07. The average ROE ratio of the bank was 34.08%. During the study period, the average ROE ratio was above the 15% benchmark. Hence, the bank's ROE ratio was sound. Similarly, the ROE of NABIL was maximum with 33.87% in the FY 2005/06 and minimum of 30.70% in FY 2003/04. The average ROE ratio of the bank was 32.07%. The average ROE ratio was above the 15% benchmark which revealed the sound profitability situation of the bank. In the same way, the ROE ratio of HBL was maximum with 19.94% in the year of 2005/06 and minimum with 13.80% in the year of 2003/04. The average ROE ratio of the bank was 16.39%, the average ratio of the bank was observed above the 15% benchmark indicating sound condition of the bank in terms of the ROE ratio.

ii) The SCBNL maintained the ROA ratio minimum in FY 2004/05 with 2.28% and maximum in FY 2002/03 with 2.60%. Overall ROA ratio of the bank during study period was slightly fluctuating. The average ROA ratio of the bank was 2.46%. The Return on Asset ratio of NABIL was minimum in 2006/07 with 2.47% and maximum in 2004/05 with 3.05%. Overall ROA ratio of the bank was also slightly changing during the study period. The average ROA value of the bank was found as 2.73%. In case of both banks average ROA ratios were achieved two folds above the benchmark of 1%. This scenario showed the quality of assets and their efficiency to generate return to be sound. Similarly, the ROA of HBL was minimum of 0.99% in FY 2002/03 and maximum of 1.55% in

FY 2005/06. The average ROA of the bank was 1.26% during the study period. Though such average ROA ratio of the bank was above the benchmark of 1% and higher, the values were with decreasing tendency.

iii) In case of the SCBNL, the EM ratio was achieved maximum up to 15.16 in FY 2004/05 and minimum with 12.85 in FY 2002/03. The average EM ratio of the bank was 13.87. The ratio of the bank was slightly unstable over the study period. In the same way, Equity Multiplier of NABIL with 13.25 was maximum in FY 2006/07 and minimum with 10.29 in FY 2004/05 and the average EM ratio of the bank was 11.84. In the case of HBL, the EM ratio was maximum with 14.19 in FY 2002/03 and minimum with 12.10 in FY 2004/05 and the average EM ratio of the bank was 13.04.

iv) The SCBNL had the Profit Margin with maximum value of 37.11% in FY 2006/07 and minimum value of 33.10% in FY 2002/03. The average PM ratio of the bank was observed with 34.37%. Similarly, the PM value of NABIL was maximum with 46.69% in 2005/06 and minimum with 31.02% in FY 2002/03. The average PM value of the bank was 38.72%. Moreover, the Profit Margin ratio of HBL was maximum with 35.32% in FY 2006/07 and minimum with 15.25% in FY 2002/03. The average PM value of the bank was 24.34%. These situations revealed that the Profit Margin value of all banks had an increasing trend during the study period.

v) The Asset Utilization ratio of SCBNL was maximum with 7.85% in FY 2002/03 and minimum with 6.70% in FY 2004/05. The average AU ratio of the bank was 7.17%. The ratio of the bank was found slightly fluctuating in all years. Similarly, the AU ratio of NABIL for the study period was in continuously decreasing trend except in FY 2004/05. The AU ratio ranged from 5.43% in FY 2006/07 to 8.41% in FY 2004/05 with an average of 7.22%. Likewise, the Asset Utilization ratio of HBL for the study period had a decreasing trend. The ratio fluctuated from 4.16% in FY 2006/07 to 6.52% in FY 2002/03 with an average of 5.46%. However, the positive ratio of the banks indicated the sound earning level on the basis of total asset.

CHAPTER V

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary

The research study was focused on assessing the Profitability Analysis of three commercial banks named Standard Chartered Bank Nepal Limited (SCBNL), Nabil Bank Limited (NABIL) and Himalayan Bank Limited (HBL) comperatively in the framework ROE, by using descriptive and analytical research design. The study scrutinised the financial performance of SCBNL, NABIL and HBL as regards to their trend different earning level. The banks' audited annual reports of condition for the period 2002/03 to 2006/07 were the primary source of information and treated as authentic.

The shareholders, bankers, government, tax-collectors, employees and all bodies concerned with the company are generally concerned with the profitability of the company whereas the shareholders are interested with the rate of return, employees in the future prospectus of the company, government in the company's tax payment capacity and in the prosperity of the company. The profitability generally measures the efficiency of the organization. A good profitability situation refers their good position or efficiency of organization while low profitability saturation indicates the lower efficiency of the organization. It also indicates the financial condition of an income and expenditure of the organization. The net profit is a very basic indicator of an organization's profitability. Besides earning per share (measured by EPS), dividend paid per share (DPS), resource utilization and mobilization capacity, investment capacity are the other important indicators of profitability.

The ROE Frame work starts with the most frequently used measures of profitability, the ROE, and then breaks it down to identify strengths and weaknesses in a bank's performance. The resulting breakdown provides a convenient and systematic method to identify strengths and weaknesses of a bank's profitability. The identification of strengths and weaknesses, and the reasons for them provide an excellent tool for bank managers as they look for ways to improve the profitability. Under the ROE framework, five financial ratios were analyzed for the study; Return on Equity (ROE), Return on Assets (ROA), Equity Multiplier (EM), Profit Margin (PM) and Assets Utilization (AU).

The research was conducted within the framework of descriptive and analytical research design. For the study purpose, Standard Chartered Bank Nepal Limited, Nabil Bank Limited and Himalayan Bank Limited were chosen as a study units applying convenience sampling technique out of 25 commercial banks. The required data and information were collected from secondary sources. In addition with this, primary data also were used in this research work which were collected by using unstructured interview with senior staffsin the bankx. The financial ratios, simple mathematical had been applied to get the meaningful result of the collected data in this research work.

The analysis was conducted to compare the all banks' ratios with standard benchmark and analyze the trend of ratios. The ROE ratios of the banks were generally above than standard benchmark during the study period which leaded to conclude that the banks had maintained sound ROE level. Both SCBNL and NABIL had maintained the ROE ratios above 15% benchmark during years of study period. This indicated the sound return of the shareholders. However, the HBL was not able to maintain the ROE level at standard benchmark 15% in two years; however the bank had maintained average of ROE above 15%. In the same way, both SCBNL and NABIL were able to maintain the ROA ratio above 1% benchmark in all years, whereas, HBL failed to obtain ROA ratio at 1% benchmark in the first year of study period. The Equity Multipliers of the banks were slightly fluctuating during the study period. The Profit Margin ratios of the banks were in increasing trend in all years. The Profit Margin of HBL was below while compared with other two banks. The Asset Utilization values of the studied banks were positive but with decreasing trend during the study period. However, the positive ratio of the banks indicated the sound earning level on the basis of total asset.

5.2 Conclusions

The conclusions based on the findings, the profitability analysis of three commercial banks in the ROE framework are as follows:

i) The average ROE ratio of SCBNL was 34.08%. During the study period, the average ratio was above the 15% benchmark. Hence, the bank's ROE ratio was sound. Similarly, the mean ROE ratios of NABIL and HBL were also above the

15% benchmark which revealed the sound profitability situation of the banks. The ROE ratios of SCBNL and NABIL were above the standard benchmark but the ROE ratio of HBL was below the standard benchmark during few years. However, the average mean ROE ratios of all banks were above the standard benchmark. This showed the sound earning level of the banks. The ROE ratios of all banks seemed to be fluctuating during the study period indicating the unstable situation of the earning of the banks.

ii) The overall ROA ratio of SCBNL during the study period was slightly fluctuating. The average ROA ratio of the bank was 2.46%. The average ROA value of NABIL was found as 2.73%. In case of both banks, the average ROA ratios were achieved two folds above the benchmark of 1%. This scenario showed the quality of assets and their efficiency to generate return to be sound. Similarly, the ROA of HBL was minimum of 0.99% in FY 2002/03 and maximum of 1.55% in FY 2005/06. The average ROA ratio of the bank was 1.26% during the study period. Though the mean ROA of the bank was above the benchmark of 1% and higher, the values were with decreasing tendency. The ROA ratios of all banks were not stable during the study period. The ROA ratios of SCBNL and NABIL were above standard benchmark in all years of study. The HBL also maintained the ROA ratio above the standard benchmark except in the first year of study period. However, the average of the ROA ratio was above standard benchmark representing the quality of assets and their sound efficiency to generate the return.

iii) In case of the SCBNL, the EM ratio of the bank was slightly unstable over the study period. In the same way, Equity Multiplier ratio of NABIL with 13.25 was maximum in FY 2006/07 and minimum with 10.29 in FY 2004/05 and the average EM ratio of the bank was 11.84. In the case of HBL, the EM value was maximum with 14.19 in FY 2002/03 and minimum with 12.10 in FY 2004/05 and the average EM ratio of the bank was 13.04. The EM ratios of all banks were found to be slightly varying during the study period. Such trend showed the greater potential of the banks for high returns for its stockholders.

iv) The average PM ratio of SCBNL was observed with 34.37%. Similarly, the PM value of NABIL was maximum with 46.69% in 2005/06 and minimum with 31.02% in FY 2002/03. The average PM value of the bank was 38.72%. Moreover, the Profit Margin of HBL was maximum with 35.32% in FY 2006/07 and minimum with 15.25% in FY 2002/03. The average PM value of the bank was 24.34%. These situations revealed that the Profit Margin values of all banks had an increasing trend during the study period. The PM ratios of all banks were achieved at higher side and increasing trend during the study years. It reminded that the banks' ability to increase their earnings and their returns to their stockholders by successfully controlling expenses and maximizing the revenues.

v) The average AU ratio of SCBNL was 7.17%. The AU ratio of the bank was found slightly fluctuating in all years. Similarly, the AU ratio of NABIL for the study period was in continuously decreasing trend except in FY 2004/05. The ratio ranged from 5.43% in FY 2006/07 to 8.41% in FY 2004/05 with an average of 7.22%. Likewise, the Asset Utilization ratio of HBL for the study period had a decreasing trend. However, the positive ratio of the banks indicated the sound earning level on the basis of total assets. The AU ratios of all banks were positive during the study period. This revealed the sound utilization of the assets. Similarly, careful allocation of the banks' assets to the highest yielding loans and investments while avoiding excessive risks were represented by such analysis.

5.3 Recommendations

i) Since the ROE ratio of HBL was comparatively lower than that of other banks, rethinking for minimizing managerial expenses and maximizing the net income might be positive step to achieve higher ROE ratio.

ii) Similarly, the ROA ratio of HBL was also found lesser than the benchmark value of 1% during the early period of the study duration. This indicated inefficient utilization of the assets for attaining enough net income. The management of the bank can further emphasize for the effective use of its assets to achieve higher ROA ratio in future.

iii) The increasing trend of the EM ratios after fluctuation will need to be strengthened for its consistency. The similar strategy might be followed by the banks to have increasing trends in case of PM ratios and AU ratios.

iv) The detailed study of all commercial banks shall be conducted for more exact results and effective interpretation of the ratios to obtain proper suggestions for sound financial conditions of such institutions.

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APPENDIX 1

List of Commercial Banks in Nepal

S.N.	Name of the Banks	Established Year
1	Nepal Bank Limited	1994
2	Rastriya Banijya Bank	2022
3	Agriculture Development Bank	NA
4	NABIL Bank Limited*	2041
5	Nepal Investment Bank Limited	2042
6	Standard Chartered Bank Nepal Limited *	2043
7	Himalayan Bank Limited *	2049
8	Nepal SBI Bank Limited	2050
9	Nepal Bangladesh Bank Limited	2050
10	Everest Bank Limited	2051
11	Bank of Kathmandu Limited	2051
12	Nepal Credit and Commerce Bank Limited	2053
13	Lumbini Bank Limited	2055
14	NIC Bank Limited	2055
15	Machapuchhre Bank Limited	2056
16	Kumari Bank Limited	2057
17	Laxmi Bank Limited	2058
18	Siddhartha Bank Limited	2058
19	Global Bank Limited	2064
20	Citizen Bank International Limited	2064
21	Sunrise Bank Limited	2064
22	Prime Bank Limited	2064
23	Bank of Asia	2064
24	Development Credit Bank Limited	2065
25	NMB Bank Limited	2065

Source: http://www.nrb.org.np
** Sample of the study*

APPENDIX 2

Shareholding Pattern of SCBNL

<table>
<tr><th>S.N.</th><th colspan="3">Subscription</th><th>% Stake</th></tr>
<tr><td>1.</td><td colspan="3">General Public</td><td>25%</td></tr>
<tr><td rowspan="3">2.</td><td colspan="3">Foreign Investment</td><td></td></tr>
<tr><td>a.</td><td>SCGL, Australia</td><td>50%</td><td rowspan="2">75%</td></tr>
<tr><td>b.</td><td>SCB, UK</td><td>25%</td></tr>
</table>

Source: Annual Reports 2005/06

APPENDIX 3

Shareholding Pattern of NABIL

S.N.	Subscription			% Stake
1.	**Financial Institution**			**20%**
	a.	NIDC	10%	
	b.	RBS	9.67%	
	c.	NEPSE	0.33%	
2.	**General Public**			**30%**
3.	**Foreign Investment**			**50%**
		NB International	50%	

Source: Annual Reports 2061/62

APPENDIX 4

Shareholding Pattern of HBL

S.N.	Subscription			% Stake
1.	**Financial Institution**			**14%**
		EPF	14%	
2.	**General Public (Promoters+General Public)**			**66%**
3.	**Foreign Investment**			**20%**
		Habib Bank of Pakistan	20%	

Source: Annual Reports 2061/62

APPENDIX 5

Standard Chartered Bank Nepal Limited

Comparative BALANCE SHEET (Amount in Lakh)

A. ASSETS	**FY 2059/60**	**FY 2060/61**	**FY 2061/62**	**FY 2062/63**	**FY 2063/64**
	2002/03	**2003/04**	**2004/05**	**2005/06**	**2006/07**
Cash	**2,578.00**	**1,988.00**	**1,877.00**	**1,954.00**	**2,795.00**
Local Currency	2,240.00	1,532.00	1,542.00	1,621.00	2,434.00
Foreign Currency	338.00	456.00	335.00	333.00	361.00
Bank Balance	**5,674.00**	**13,135.00**	**18,355.00**	**9,157.00**	**9,967.00**
Nepal Rastra Bank	3,762.00	11,411.00	15,342.00	6,922.00	7,497.00
Other Local Banks	68.00	78.00	215.00	155.00	186.00
Foreign Banks	1,844.00	1,646.00	2,798.00	2,080.00	2,284.00
Money at Call or Short Notice (Placements)	20,620.00	16,579.00	22,186.00	22,597.00	19,773.00
Investment (At Cost)	92,760.00	102,162.00	113,603.00	97,025.00	128,504.00
HMG Securities	57,848.00	65,813.00	79,482.00	72,031.00	86,448.00
Treasury Bills	40,228.00	44,385.00	61,305.00	50,894.00	72,105.00
Development Bonds	17,214.00	20,796.00	17,130.00	19,820.00	12,965.00
National Savings Bond					
Company Shares	406.00	632.00	1,047.00	1,317.00	1,378.00
NHFDC Limited					
NIDC Capital Markets Ltd.					
Debentures & Bonds	112.00	112.00	112.00	133.00	153.00
Shares in Subsidiary Companies					
Other Investments	34,800.00	36,237.00	34,009.00	24,861.00	41,903.00

A. ASSETS (contd….)	**FY 2059/60**	**FY 2060/61**	**FY 2061/62**	**FY 2062/63**	**FY 2063/64**
	2002/03	**2003/04**	**2004/05**	**2005/06**	**2006/07**
Foreign Banks	31,948.00	31,374.00	33,709.00	24,861.00	41,903.00
Others	2,852.00	4,863.00	300.00		
Bills Purchases & Discounted	1,156.00	973.00	874.00	3,116.00	2,981.00
Local	26.00	28.00	33.00	41.00	44.00
Foreign	1,130.00	945.00	841.00	3,075.00	2,937.00
Local	52,484.00	55,985.00	63,228.00	78,311.00	86,373.00
Foreign				5.00	
Fixed Assets	1,011.00	1,917.00	1,362.00	714.00	1,013.00
Other Assets	8,150.00	16,370.00	14,935.00	6,056.00	6,386.00
Non-Banking Assets					
Loan Loss Provision adjusted					
Total Assets	**184,433.00**	**209,109.00**	**236,420.00**	**218,935.00**	**257,792.00**
B. LIABILITIES & CAPITAL					
Share Capital	3,395.00	3,395.00	3,746.00	3,746.00	3,746.00
Authorized Capital	3,395.00	3,395.00	10,000.00	10,000.00	10,000.00
Issued Capital	3,395.00	3,395.00	5,000.00	5,000.00	5,000.00
Paid-Up Capital	3,395.00	3,395.00	3,746.00	3,746.00	3,746.00
Reserve Funds	8,960.00	10,294.00	11,212.00	12,077.00	13,825.00
General Reserve	6,791.00	6,791.00	7,493.00	7,493.00	7,493.00
Capital Adjustment Reserve		340.00	375.00	749.00	749.00

B. LIABILITIES & CAPITAL (contd..)	FY 2059/60	FY 2060/61	FY 2061/62	FY 2062/63	FY 2063/64
	2002/03	2003/04	2004/05	2005/06	2006/07
Retained Earning	1,309.00	2,160.00	2,176.00	2,513.00	3,706.00
Contingent Reserve					
Dividend Equalization Fund					375.00
Exchange Fluctuation Reserve	860.00	1,003.00	1,168.00	1,322.00	1,472.00
Special Reserve Fund					
Other Reserve					30.00
Borrowing from other Banks/Agencies	6,848.00	791.00	782.00	560.00	-
Local	246.00	281.00	647.00	284.00	
Deposits	158,358.00	187,557.00	211,614.00	193,351.00	230,610.00
Current	38,084.00	57,686.00	58,169.00	43,563.00	46,819.00
Savings	94,419.00	106,332.00	127,718.00	130,309.00	145,977.00
Call	1,011.00	1,852.00	9,410.00	2,949.00	11,357.00
Fixed	22,648.00	19,486.00	14,285.00	14,164.00	21,363.00
Others					
Margin	2,196.00	2,201.00	2,032.00	2,366.00	5,094.00
Bills Payable	514.00	548.00	590.00	563.00	558.00
Dividend Payable					4,999.00
Other Liabilities	6,358.00	6,524.00	8,476.00	8,638.00	4,054.00
Total Liabilities	**184,433.00**	**209,109.00**	**236,420.00**	**218,935.00**	**257,792.00**

APPENDIX 6

Standard Chartered Bank Limited

Comparative INCOME EXPENSE STATEMENT (Amount in Lakh)

A. INCOME	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**
Interest Income	10136	10014	10422	10587	11896
Commission & Discount	1635	2152	1989	1848	2483
Exchange Gain	2281	2325	2731	2669	2835
Revaluation Gain					
Trading Gain					
Non-Operating Income				30	14
Profit/Loss on Sale of Assets					
Dividend					
A. INCOME	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**
Other Income	416	555	698	629	507
Total	**14468**	**15046**	**15840**	**15763**	**17735**
B. EXPENSES					
Interest Expenses	2999	2552	2758	2541	3032
Personnel Expense	1265	1283	1347	1486	1682
B. EXPENSE	**2002/03**	**2003/04**	**2004/05**	**2005/06**	**2006/07**
Office Overhead Expense	1909	3120	2797	2566	2211
Exchange Loss					
Non-Operating Expenses	185	155	107		
Book Write Off of Bad Loans	5				
Provision for Loan Loss	750	23	235	301	477
Provision for Staff Bonus	721	761	860	887	939
Provision for Income Tax & Special Fee	1842	2083	2358	2589	2806
Net Profit Carried Down	4792	5069	5378	5393	6588
Total	**14468**	**15046**	**15840**	**15763**	**17735**

Source: Annual Reports

APPENDIX 7

HIMALAYAN BANK LIMITED

Comparative Balance Sheet

(in million Rs.)

Fiscal Year (as at mid July)	2002	2003	2004	2005	2006
Capital and Liabilities					
Share Capital	390.0	429.0	536.3	772.20	810.81
Reserve Funds	1111.5	1476.9	1755.5	1665.97	1929.84
Borrowings	534.0	645.8	659.0	144.62	235.97
Deposit Accounts	18619.4	21007.4	22010.3	26490.85	30048.42
Other Liabilities	660.9	638.9	768.5	386.75	494.10
Total Liabilities	21315.8	24198.0	25729.6	29460.39	33519.14
Assets					
Cash & Bank Balance	1264.7	1979.2	2001.1	1717.35	1757.34
Money at Call	352.4	150.1	368.9	1005.28	1710.02
Investment	9157.1	10175.4	9292.1	10889.03	11822.98
Loan and Advances	9557.1	10844.6	12919.6	14642.56	16998
Fixed Assets	318.8	229.9	299.6	840.82	574.06
Other Assets	665.7	818.8	848.3	365.40	656.70
Total Assets	21315.8	24198.0	25729.6	29460.39	33519.14

Source: Annual Reports.

APPENDIX 8

HIMALAYAN BANK LIMITED

Comparative Profit and Loss Account

(in million Rs.)

Fiscal Year(for the mid July)	2002	2003	2004	2005	2006
Expenses					
Interest Expenses	578.134	554.128	491.543	648.84	767.41
Staff Expenses	101.537	120.146	152.508	234.59	272.23
Office Operating Expenses	155.786	177.132	211.047	329.70	341.56
Provision for Doubtful Debts	166.506	202.873	186.226	145.15	90.69
Provision for Staff Bonus	38.783	40.003	46.731	67.24	71.74
Non-operating Expenses	--	—	10.988	2.90	315.89
Income Tax Provision	114.023	147.896	157.522	214.94	225.58
Net Profit	235.023	212.129	263.053	457.46	491.82
Total Expenses	1389.79	1454.31	1519.62	2100.82	2219.39
Incomes					
Interest Income	1149	1201.23	1245.9	1626.47	1775.58

Fiscal Year(for the mid July)	2002	2003	2004	2005	2006
Commission & Discount	101.704	102.562	123.929	165.45	193.22
Foreign Exchange Gain	104.601	109.599	112.419	198.13	151.64
Non-Operating Income	2.451	10.76	3.299	1.89	3.49
Other Income	32.038	30.154	34.076	108.88	95.46
Total Income	1389.79	1454.31	1519.62	2100.82	2219.39

Source: Annual Reports.

APPENDIX 9

NABIL BANK LIMITED

Comparative Balance Sheet

(in million Rs.)

Fiscal Year (as at mid July)	2002	2003	2004	2005	2006
Capital and Liabilities					
Share Capital	492	492	492	492	492
Reserve Funds	635	648	1026	1383	1565
Borrowings	1022	459	34	173	883
Deposit Accounts	13448	14119	14587	19347	23342
Other Liabilities	839	915	925	934	971
Total Liabilities	16437	16633	17064	22330	27253
Assets					
Cash & Bank Balance	1145	970	559	629	1399
Money at Call	670	919	868	1735	564
Investment	6031	5836	4267	6179	8945
Loan and Advances	7454	7954	10465	12923	15546
Fiscal Year (as at mid July)	**2002**	**2003**	**2004**	**2005**	**2006**
Fiscal Year (as at mid July)	**2002**	**2003**	**2004**	**2005**	**2006**
Fixed Assets	252	338	361	319	287
Other Assets	885	616	542	545	512
Total Assets	16437	16633	17064	22330	27253

Source: Annual Reports.

APPENDIX 10

HIMALAYAN BANK LIMITED

Comparative Profit and Loss Account

(in million Rs.)

Fiscal Year(for the mid July)	2002	2003	2004	2005	2006
Expenses					
Interest Expenses	317	283	244	357	556
Staff Expenses	211	181	200	220	240
Office Operating Expenses	166	153	190	183	188
Provision for Doubtful Debts	52	82	31	4	14
Provision for Staff Bonus	66	72	84	90	100
Non-operating Expenses	199	203	243		
Income Tax Provision	199	202	239	263	321
Net Profit	416	455	519	635	674
Total Expenses	1427	1429	1511	1752	2093
Incomes					
Interest Income	1018	1002	1069	1310	1588
Commission & Discount	144	139	129	138	151
Foreign Exchange Gain	144	157	185	185	210
Non-Operating Income	97	93	72	1	5
Other Income	34	39	56	118	139
Total Income	1427	1429	1511	1752	2093

Source: Annual Reports.